

2010



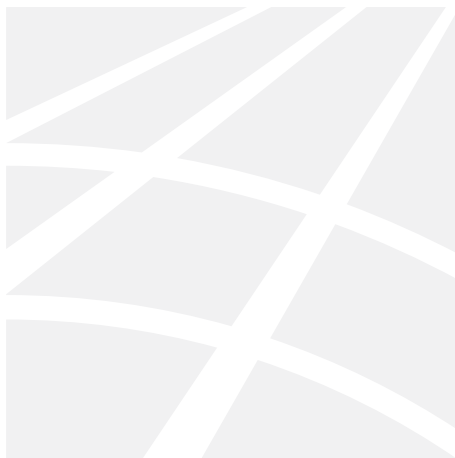
## Annual Report

Terna S.p.A. and the Terna Group

Terna is a leading grid operator for energy transmission. The company manages electricity transmission in Italy and guarantees its safety, quality and affordability over time. It ensures equal access conditions for all grid users. It develops market activities and new business opportunities with the experience and technical expertise acquired in managing complex systems. It creates values for shareholders with a strong commitment towards professional excellence and with a responsible approach towards the community, fully respecting the environment it operates in.



2010



## Annual Report

Terna S.p.A. and the Terna Group



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## Chairman's message



**Dear Terna Shareholders and Stakeholders,**

2010 was Terna's best year in terms of accelerating the development of the grid, with over 1,000 km of new power lines and 48 new stations for a total investment of 1,161.7 billion euros. Through these measures, Terna has also provided impetus to employment and growth during a difficult phase of the Italian economy. In 2010, thousands of people worked in Terna's building sites, not counting the activities created by the purchase of goods and other services.

Increasing grid development has a positive impact on the community not only because it improves the efficiency and safety of the electricity system but also because the public benefit that it provides in terms of reduction in the national electricity bill is greater than the investment. It also has a positive impact on the environment, such as a reduction in CO<sub>2</sub> emissions due to grid losses reduction, more efficient production assets and the connection to the grid of production plants from renewable sources.

As in the past, and even more so this year, Terna's commitment was focused on creating value and trust for shareholders and all stakeholders. We believe we have achieved our goal by integrating our core business – energy transmission – with the protection of the environment and territory and with the public interest. It is nothing new: since 2002, Terna has experienced how the sustainable development of the electricity grid can be achieved through the sharing of projects with the territory. In recent years this approach has been extended in an effort to interact with the major environmental organizations.

The vision of a sustainable electricity grid also focuses on pylons, the most distinctive elements in terms of environmental impact, through a search for solutions that take into account their aesthetic dimensions. The pylons designed by Sir Norman Foster have already been installed along the "Tavarnuzze-Santa Barbara" electricity line and are visible near the Scandicci (Florence) highway exit while in 2010 the engineering phase of the new pylons designed by architect Hugh Dutton of the Rosental Studio – the winner of the international contest ended in 2009 – was started.

As we note Terna's success, we cannot forget to mention the significant role played by the human resources in our activities. People have, indeed, distinctive technical skills that allow Terna to best fulfill its national interest task. Updating their skills – and providing them with constant training – is a key element in human resource development, as is placing focus on occupational safety which is required by operating activities involving risk, working at several meters above ground and maintaining high voltage power lines.

Our ongoing efforts have led to significant returns for Terna in both its economic results and in terms of sustainability coupled with a steady growth of specialized rating assessments, Terna's inclusion in the major international stock sustainability indexes and its appreciation by socially responsible investors.

There is one award in particular, among many, that I would like to mention because it reflects our way of being: fine professionals who are proud of their work and who have made a contribution to an important solidarity initiative. Terna won the "5<sup>th</sup> Business Awards for the Environment", promoted by the Chamber of Commerce of Rome and sponsored by the UNIDO (United Nations Industrial Development Organization) in the "Best cooperation for sustainable development" category, for a project aimed at bringing electricity to Kami (Bolivia), which was undertaken by some employee volunteers: an international initiative for the development of a community in which Terna's specific technical skills have played a significant role.

Technical expertise, focus on results and attention to the community: balancing these factors is our way to create value. It is also because of this that Terna is one of the leading electricity grid operators in the world.

The Chairman  
LUIGI ROTH

# Letter to Shareholders



**Ladies and Gentlemen Shareholders,**

2010 closed with important results that are rewarding for you and thus, for Terna's entire team. Our action was twofold: core business and the opportunities outside of the traditional activities. With the sale of Rete Rinnovabile, we closed the third M&A operation in two years, in record time, once again creating value to the advantage of the Country, the electricity system and shareholders.

Once again, we demonstrated we can keep our promises.

We said that 2010 would be the year of the building sites: works were completed for the construction of SA.PE.I., the submarine cable connecting Sardinia and the mainland, for the "Casellina-Tavarnuzze-Santa Barbara" power line in Tuscany as well as for upgrading the Val d'Ossola grid; several other worksites were opened among which those for the "Sorgente-Rizziconi" connection between Sicily and Calabria and for the Chignolo Po-Maleo power line.

The fundamentals of the Terna Group are solid. The 2010 financial statement shows a double digit growth of all key economic indicators.

At the consolidated level and comparing data with the 2009 financial statement, revenues increased by 14% and stood at 1 billion and 589 million euros, the Gross Operating Margin amounted to 1,174.9 million euros increasing by 17% and Profits rose to 466.7 million euros increasing by nearly 32%. The acceleration of investments for the grid's development continued. Investments reached 1,161.7 million euros (nearly +30%), for over 1,000 km of new power lines and 48 new power stations.

These results allow us to propose, once again, a distribution of dividends per share increased by 10.5% compared to the previous year.

With regard to the share's trend, despite an unfavorable macro-economic situation and high volatility of the principal stock markets, the defensive nature of Terna's shares was appreciated by the markets and enabled us to achieve the positive performance of 5.3%, in counter-trend with the poor performance of the Italian Blue Chips (FTSE-MIB -13.2%). Moreover, Terna was the only European utility to reach its record high of 3.3925 euros per share in 2010.

Our Company's goals remain focused on achieving greater operational efficiency while ensuring the highest quality in the transmission service and a more efficient and safer management of the energy flows in the electricity system.

2011 will focus on the implementation of the provisions included in the 2011-2015 Strategic Plan. In particular, planned investments will be aimed at increasing interconnections with other countries, reducing grid congestion and removing the constraints caused by the increased renewable sources production.

Moreover, Terna will hold the usual debate with the Authority for Electricity and Gas aimed at ensuring continuity and stability of principles for establishing the tariffs also in the 4<sup>th</sup> regulatory period (2012-2015). As part of its non-regulated activities in 2011, the Company will also be involved in implementing a second group of PV projects, intended to further enhance the Group's assets.

The CEO  
FLAVIO CATTANEO

# Call of ordinary and extraordinary Shareholders' Meeting

The Shareholders' Meeting of Terna S.p.A. has been convened in Rome at Terna's Auditorium in Piazza Giuseppe Frua no.2 in ordinary session for May 12 and 13, 2011, respectively on first call at 11 o'clock and in second call at 14,30 and, the extraordinary meeting is convened for May 12, 13 and 14 2011, respectively on first call at 11 o'clock, on second call at 14,30 and on third call at 11 o'clock, to discuss and resolve on the following

## Agenda

### Ordinary session

1. Financial Statement as of December 31, 2010. Reports by the Board of Directors, the Board of Statutory Auditors and the Independent Auditors. Related resolutions. Presentation of the Consolidated Financial Statement as of December 31, 2010;
2. Allocation of the net income of the fiscal year;
3. Determination of the number of members of the Board of Directors and their term of office;
4. Appointment of the members of the Board of Directors;
5. Appointment of the Chairman of the Board of Directors;
6. Determination of the remuneration of the members of the Board of Directors;
7. Appointment of the Board of Statutory Auditors;
8. Determination of the remuneration of the Statutory Auditors of the Board of Statutory Auditors;
9. Mandate for the statutory auditing for the 2011 – 2019 period, and consequent resolutions;
10. Adapting the Regulations of the meetings to the provisions of Legislative Decree No. 27 of January 27, 2010. Amendments to articles 1.2, 2.1, 2.2, 3.2, 3.4, 3.5, 4.2, 4.8, 6.4, 6.6.

### Extraordinary session

1. Amendments to Art. 9.1 and Art. 13 of the Corporate Bylaws, respectively, in compliance with the provisions introduced by Art. 1 of Legislative Decree No. 27 of January 27, 2010 and for the implementation of the Procedure for Related Party Transactions under the "Regulations on provisions relating to Transactions with Related Parties" (adopted by CONSOB with Resolution No. 17221 of March 12, 2010 and as subsequently amended by Resolution No. 17389 of June 23, 2010) as well as the re-numbering of the individual paragraphs that make up Art. 13.

### Reports and documentation

The illustrative reports by the Directors on the items on the agenda, required by governing rules, will be made available to the public at the company headoffice and at Borsa Italiana S.p.A. according to the following timetable:

- by April 2, 2011, the reports concerning items 3, 4, 5, 6, 7 and 8 of the agenda for the ordinary Shareholders' Meeting;
- by April 12, 2011, the reports concerning items 1, 2, 9 and 10 of the agenda for the ordinary Shareholders' Meeting;
- by April 21, 2011, the reports concerning the sole item on the agenda of the extraordinary Shareholders' Meeting.

Documents submitted to the Shareholders' Meeting will be made available to the public at the company headoffice and at Borsa Italiana S.p.A. in the terms provided for by rules in force.

The reports and documentation will also be published in the Company's website ([www.terna.it](http://www.terna.it) - "Investor Relations"). Shareholders have the right to obtain copies.

### Right to supplement the agenda

Shareholders who, also as a group, represent at least one fortieth of the share capital with voting rights, may ask, pursuant to and in the modes pursuant to Article 126-bis of Legislative Decree no. 58 of February 24, 1998 (TUF), within ten days from the publication of this notice, to add subjects to be discussed, indicating the proposed subjects in the request. The request must be submitted in writing and must be accompanied by a report on the matters being proposed, and be brought to Terna S.p.A. at its head office (attention: Terna S.p.A. Company Secretariat), or sent by mail or by fax to 06 83138218, or by e-mail or certified electronic mail at the following certified e-mail address: [Assemblea2011@pec.terna.it](mailto:Assemblea2011@pec.terna.it).

Please remember that pursuant to law, supplements to the agenda are not allowed for subjects which the Shareholders' Meeting will be resolving upon according to the law and based on Directors' proposals or on the basis of a project or a report prepared by them that is different from the one dealing with the subjects in the agenda. In the event of supplements to the agenda, the modified list of subjects to be dealt with in the Shareholders' Meeting will be published, with the same modes of publication as this notice, at least fifteen days before the one scheduled for the Shareholders' Meeting.

## Share capital

Please note that as of the date of this notice, and pursuant to Article 5.1 of the Bylaws published in the website of the Company ([www.terna.it](http://www.terna.it) - “Investor Relations”) (the “Bylaws”), the share capital is of 442,088,020 euros, completely paid-in and divided into 2,009,491,000 ordinary shares having a value of 0.22 euros each, each of which, pursuant to Article 6.1 of the Bylaws, entitles to one vote. The Company does not hold its own shares.

## The right to participate in the Shareholders’ Meeting and exercising the right to vote

The right to participate in the Shareholders’ Meeting and exercising the right to vote, according to the provisions in Article 10.1 of the Bylaws, is governed by applicable regulatory standards in force. Pursuant to governing Article 83-sexies TUF, such right is demonstrated by notification to the Company by an intermediary, in compliance with its own accounting records, on behalf of the individual who is entitled to the right to vote, based on evidence related to the close of the accounting day of the seventh open-market day prior to the date set for the Shareholders’ Meeting in first call (i.e., May 3, 2011), the so-called “record date”.

The credit and debit registrations made on accounts subsequent to said term are not material for purposes of legitimizing the exercise of the right to vote in the Shareholders’ Meeting. Therefore, those who appear as owners of the Company shares subsequent to said date will not be allowed to participate and vote.

Communications by intermediaries for participation must be received by the Company by the end of the third open-market day prior to the date set for the first call of the Shareholders’ Meeting (i.e., May 9, 2011). There is no prejudice to the entitlement to participate and vote if the Company has received the communications after said indicated term, provided that it is received by the start of the Meeting proceedings on single call.

There are no procedures for voting by mail or by electronic means.

## Representation at the Shareholders’ Meeting

### Ordinary proxy

Each party entitled to participate and vote at the Shareholders’ Meeting may be represented by means of a proxy pursuant to governing law provisions. For this purpose, the proxy form issued upon request of the entitled party by the qualified intermediary can be used, or the [proxy form](#) available on the Company’s website ([www.terna.it](http://www.terna.it) - “Investor Relations”) or at the headoffice.

The Company can be notified of the proxy by filing it with the headoffice (the Segreteria Societaria (Company Secretariat) of Terna S.p.A.) or by mail, or e-mail or certified electronic mail to the following certified e-mail address: [Assemblea2011@pec.terna.it](mailto:Assemblea2011@pec.terna.it), or using the section of the Company website ([www.terna.it](http://www.terna.it) - “Investor Relations”) and the proxy must be received by the Company by the start of the Meeting proceedings on single call. In replacement of the original, the representative may deliver or transmit to the Company a copy of the proxy, also by electronic means, stating under his/her own responsibility that the proxy is in compliance with the original, as well as to the identity of the person issuing the proxy.

### Designated Representative Proxy

The proxy may also be granted with voting instructions to Servizio Titoli S.p.A., with headoffice in Via Mantegna no. 6, Milan, named by the Company for this purpose “Designated Representative” pursuant to Article 135-undecies TUF. In this regard, the specific guided web application prepared and managed by Servizio Titoli S.p.A., which can be accessed on the Company’s website ([www.terna.it](http://www.terna.it) - “Investor Relations”), can be used to fill in the proxy form for the designated representative. The Designated Representative [proxy form](#) is also available in a printable version from the website, or from the Company’s headoffice. The Designated Representative proxy must contain voting instructions to all or some of the subjects on the agenda and the original must be given to said Designated Representative by the end of the second open-market day prior to the date set for the Shareholders’ Meeting on first call (i.e., by May 10, 2011) at the following address: Servizio Titoli S.p.A. (ref. “Shareholders’ Meeting proxy Terna S.p.A.”), Via Monte Giberto no. 33 - 00138 Rome. A copy of the proxy, accompanied by a declaration stating that it is in compliance with the original, can be anticipated to the Designated Representative by the same term by fax at 06 88345203 or at the certified e-mail address [terna@pecserviziotitoli.it](mailto:terna@pecserviziotitoli.it).

A “Designated Representative” proxy is valid only for resolutions proposed at the Shareholders’ Meeting for which the person issuing the proxy gave voting instructions. The proxy and the voting instructions are revocable within the same term as hereinabove (i.e., by May 10, 2011), with the manner and terms indicated above.

### Right to pose questions on items on the agenda

Pursuant to Article 127-ter TUF, parties entitled to participate in the Shareholders’ Meeting may pose questions on subjects on the agenda also before the Shareholders’ Meeting. The questions must be made in writing and sent to Terna S.p.A. to its headoffice (to the attention of the Company Secretariat of Terna S.p.A.) by fax at the number 06 83138218, or by e-mail or certified electronic mail at the certified e-mail address: [Assemblea2011@pec.terna.it](mailto:Assemblea2011@pec.terna.it).



#### Filing of the Board of Directors' and Board of Statutory Auditors' lists

Appointment of the members of the Board of Directors and the Board of Statutory Auditors will take place by voting on the basis of lists with the manner and terms provided for in Articles 14.3 and 26.2 of the Bylaws, respectively, and by governing legislation. For the appointment of the members of the aforementioned corporate bodies, each shareholder may submit or contribute towards the submission of one list, and each candidate may be included only in one list, or he will be considered ineligible.

The lists of candidates for the positions of Director and Auditor may be submitted by shareholders who, either individually or as a group, are owners of at least 1% of shares with voting rights in the Shareholders' Meeting.

The submission and filing of the lists must take place at the headoffice of the Company at least 25 days prior to the scheduled date of the Shareholders' Meeting on first call (i.e., by April 17, 2011 and it has to be deemed extended to April 18, 2011, the first subsequent business day) with the manner and terms provided for by the Bylaws and governing legislation, respectively.

Ownership of the minimal stake necessary for submitting the lists is determined with regard to the shares that are registered in favor of the shareholder(s) on the day on which the lists are filed with the Company. In order to prove ownership of the number of shares required to submit lists, the entitled shareholders must submit and/or deliver the relevant certification to the Company's registered office, also subsequent to filing the list, provided it is by the term anticipated for the publication of the lists (i.e., by April 21, 2011).

Taking into account the provisions of Article 144-sexies, paragraph 4-ter, of CONSOB Regulation no. 11971 of May 14, 1999 as subsequently amended (hereinafter referred to as the "CONSOB Issuers Regulation"), the lists and the copy of the required accompanying documentation can also be filed by e-mail or by certified electronic mail at: [Assemblea2011@pec.terna.it](mailto:Assemblea2011@pec.terna.it), jointly with information that allows for identification of the individual filing the lists, also indicating a telephone number.

Together with each list a statement must be filed, whereby individual candidates accept their candidature and represent, under their responsibility, the inexistence of any of the causes for ineligibility and incompatibility, as well as the existence of the requirements provided for by the applicable law and by the Bylaws for their respective offices and any other information required by the applicable rules and regulations and the Bylaws.

The lists, accompanied by information concerning the candidates' characteristics, shall be made available to the public in a timely fashion at the headoffice, on the Company website ([www.terna.it](http://www.terna.it) - "Investor Relations") and with other modalities provided for by CONSOB, at least 21 days before the date of the Shareholders' Meeting (i.e., by April 21, 2011).

With respect to the appointment of the Board of Directors, please remember that provisions according to the Bylaws are applied as regards (I) limits on exercising the right to vote when appointing the Directors as indicated in Article 14.3, letter e) and, (II) the requirements of integrity, professional skills and independence they each possess, indicated in Article 15. It must also be remembered that pursuant to Article 147-ter, paragraph 3, TUF, at least one of the members of the Board of Directors shall be proposed by the minority list that obtained the highest number of votes, and is not connected in any way, even indirectly, to the shareholders who submitted or voted the list that was first due to the number of votes, and that the shareholders that submit a "minority list" are the recipients of CONSOB Communication no. DEM/9017893 of February 26, 2009 entitled "Appointment of the members of administrative and control bodies".

The lists for the Board of Directors shall indicate the candidates who possess the requirements of independence as provided for by the law and by Art. 15.4 of the Bylaws and all other information or declarations required by applicable regulatory standards and by the Bylaws.

With respect to the requirements for the Directors, please remember that Article 6 of the Governance Code of listed companies published by Borsa Italiana, which Terna adopted, provides that together with said lists, the following must be filed: an exhaustive description of the personal and professional characteristics of the candidate, accompanied by indications that the candidate is qualified as independent, pursuant to Article 3 of said Code, to be published in a timely fashion on Terna's website, together with the lists.

Concerning the appointment of the Board of Statutory Auditors, the lists are divided into two sections, one for the candidates to the office of statutory auditor and the other for the candidates to the office of substitute auditors. The first one of the candidates of each section must be registered in the register of statutory auditors and must have exercised the activity of legal control of the accounts for a period being not less than three years.

The names of the candidates are numbered progressively and do not exceed the number of members of the body being elected. Candidates for the position of Auditor must possess the requirements of integrity and professional skills relative to the auditors of listed companies, pursuant to Ministerial Decree no.162 of March 30, 2000 issued by the Ministry of Justice, as supplemented by the provisions of the Article 26.1 of the Bylaws.

As far as situations of ineligibility and the limit to the number of offices that members of the Board of Statutory Auditors may hold on boards of directors and boards of statutory auditors are concerned, the provisions of the Bylaws and governing legislation shall be applied.

Pursuant to Article 144-*sexies*, paragraph 4, of the CONSOB Issuers Regulation, the lists must be deposited and accompanied by:

- a) information concerning the identity of the shareholders submitting the lists, with an indication of the percentage of shares held;
- b) a declaration from those shareholders who do not hold, also as a group, a controlling or majority stake, certifying the absence of relationship connections such as those provided for in Article 144-*quinquies* of the CONSOB Issuers Regulation with them. In its Communication no. DEM/9017893 of February 26, 2009, CONSOB advised the shareholders who submit a “minority list” to provide information indicated in the aforementioned declaration by CONSOB;
- c) an exhaustive description of the personal and professional characteristics of the candidates, as well as a declaration by said candidates stating that they possess the requirements provided for by law (including possessing independence requirements as provided for in Article 148, paragraph 3, TUF) and in acceptance of their candidacy.

Taking into account that pursuant to Article 2400, last paragraph, of the Civil Code, at the time of the appointment and before accepting the position, the Shareholder’s Meeting must be made aware of any administrative or supervisory positions held by the Auditors at other companies, it is suggested that a special declaration be provided within the framework of the description of the personal and professional characteristics of the candidate, emphasizing that it should be kept updated up to the day the Shareholders’ Meeting is effectively held.

The statutory member of the Board of Statutory Auditors appointed by the minority based on the modalities provided for in Article 26.2 of the Bylaws will be appointed by the minority shareholders who – as required by Article 148, paragraph 2, TUF – are not in any way connected, not even indirectly, with the shareholders who submitted or who voted the list which was first, due to the number of votes.

The Statutory Auditor taken from the minority list is entitled to the Chairmanship of the Board of Statutory Auditors.

Please remember that pursuant to Article 144-*sexies*, paragraph 5, of CONSOB Issuers Regulation, in the event that at the date of expiration of the term for submitting the lists for the Board of Statutory Auditors (i.e., by April 17, 2011 and it has to be deemed extended to April 18, 2011, the first subsequent business day) only one list has been filed, or only lists submitted by shareholders connected to each other pursuant to applicable provisions, lists may be submitted up until the third day after said date; in this case, the thresholds provided for hereinabove are reduced by half.

#### Other Information

Further information concerning the subjects on the agenda is made available to the shareholders in the Directors’ Reports concerning the respective items on the agenda, as well as in the Bylaws and in governing legislation, which shall be specifically referred to for what is not expressly provided for in this notice.

For the purposes of exercising the company rights mentioned in this notice, please remember that pursuant to Articles 22 and 23, paragraph 1, of the Regulation adopted by the Bank of Italy and by CONSOB with the provision of February 22, 2008 and subsequently amended by deed of the Bank of Italy/CONSOB dated December 24, 2010 (hereinafter referred to as the “Bank of Italy/CONSOB Regulation”), the legitimacy of exercising, also jointly, corporate rights such as: participation in and exercising the right to vote in the Shareholders’ Meeting, the right to supplement the agenda, the right to pose questions on subjects on the agenda, the filing of the lists, is certified by a communication to the issuer made by the intermediary in compliance with its accounting records for holders.

Pursuant to Article 25 of the Bank of Italy/CONSOB Regulation, legitimization to rights different from those provided for in Articles 22 and 23 is assessed by certification issued by the intermediary in compliance with his own accounting records. In order to facilitate the verification of their entitlement to participate in the Shareholders’ Meeting, the holders of the right to vote may send documentation demonstrating said entitlement to the Company by mail (to the Company Secretariat of Terna S.p.A. - Viale Egidio Galbani, 70 - 00156 Rome), also a copy or by fax to 06 83138218, at least two days prior to the scheduled date for the Shareholders’ Meeting on first call.

Please note that the offices in charge of personal identification and verification of entitlement to participate in the Shareholders’ Meeting will be available two hours before the beginning of the Shareholders’ Meeting.

A service dedicated to Meeting assistance is available to give further information at the following numbers: telephone 06 88345112 - fax 06 88345203.

This notice has been published in the company website at [www.terna.it](http://www.terna.it) and in the April 1, 2011 edition of the newspaper “Il Sole 24 Ore”.

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#### Chairman of the Board of Directors

**Luigi Roth**

Considering the shareholding of the Company and how previous occasions unfolded, it is estimated that the ordinary and extraordinary Shareholders’ Meeting will be able to be convened and resolve on May 13, 2011.

Terna S.p.A. - Headoffice in Rome - Viale Egidio Galbani, no. 70  
Share Capital 440,199,936 euros (as of 31 December 2009) fully paid-in  
Company Register of Rome, Tax ID code and VAT code no. 05779661007  
R.E.A. of Rome no. 922416





# Summary of the resolutions of the ordinary and extraordinary Shareholders' Meeting

Terna S.p.A.'s Shareholders' Meeting met on second call on 13 May 2011 for the ordinary and extraordinary session at Terna's Auditorium in Piazza Giuseppe Frua No. 2 in Rome and in the ordinary session it:

- approved Terna S.p.A.'s financial statement as of 31 December 2010;
- examined the data of the Terna Group's consolidated financial statements also as of 31 December 2010 that closed with the Group's net profits equal to € 613.6 million;
- resolved to allocate Terna S.p.A.'s 2010 net profits, equal to € 433,688,347.37 as follows:
  - € 193,410.80 to Legal Reserves (or up to reaching 20% of the share capital as of the financial statement's reference date);
  - € 160,351,656.00 to cover the interim dividend paid on 25 November 2010;
  - € 261,233,830.00 as a final dividend to be distributed in the amount of 0.13 for each one of the 2,009,491,000 ordinary shares (as of 31 March 2011) to be paid – gross of any withholdings according to the law – on 23 June 2011 with “registration date” of coupon No. 14 on 20 June 2011. The total amount determined may vary based on the possible greater number of ordinary shares that will actually be in circulation as of the date set for the registration of the coupon relative to the 2010 final dividend;
  - € 11,909,450.57, or a different amount that remains after any and further previous allocations, as balance brought forward;
- resolved to assign the task to the Board of Directors – and on its behalf to its CEO – to verify in due time, in relation to the final number of shares to be remunerated, the amount of profits distributed and of the balance brought forward.

In its ordinary session, the Meeting also:

- renewed the Company's Board of Directors, that will hold office until the approval of the 2013 financial statement with the following members:

- 1) Luigi Roth – Chairman <sup>(1)</sup>
- 2) Flavio Cattaneo – Director <sup>(1)</sup>
- 3) Fabio Buscarini – Director <sup>(2) (3)</sup>
- 4) Andrea Camporese – Director <sup>(1)</sup>
- 5) Paolo Dal Pino – Director <sup>(1) (3)</sup>
- 6) Matteo Del Fante – Director <sup>(1)</sup>
- 7) Salvatore Machì – Director <sup>(2) (3)</sup>
- 8) Romano Minozzi – Director <sup>(2) (3)</sup>
- 9) Michele Polo – Director <sup>(1) (3)</sup>

setting the relative remuneration at € 50,000 gross per year for the Chairman and € 35,000 gross per year for each Director;

- renewed the Board of Statutory Auditors, that will hold office until the approval of the 2013 financial statement with the members:

- Luca Aurelio Guarna – Chairman <sup>(4)</sup>
- Alberto Luigi Gusmeroli – Standing Auditor <sup>(5)</sup>
- Lorenzo Pozza – Standing Auditor <sup>(5)</sup>
- Stefania Bettoni – Alternate Auditor <sup>(4)</sup>
- Flavio Pizzini – Alternate Auditor <sup>(5)</sup>

setting the relative remuneration at € 55,000 gross per year for the Chairman and € 45,000 per year for the other Standing Auditors;

- approved the proposal of the Board of Statutory Auditors and conferred the assignment of legal auditing, for the nine-year period from 1 January 2011 to 31 December 2019, to the company PricewaterhouseCoopers S.p.A., according to the terms and conditions proposed by the Board of Statutory Auditors itself;
- approved the proposal to change articles 1.2, 2.1, 2.2, 3.2, 3.4, 3.5, 4.2, 4.8, 6.4 and 6.6 of the Regulations of the general Meetings of the company according to the text proposed by the Company's Board of Directors to allow adjusting the text to the new provisions of Legislative Decree No. 27 dated 27 January 2010 (regarding the “Implementation of Directive 2007/36/CE, relating to shareholders' rights of listed companies”) and to better define the extent of some provisions of these Regulations based on accrued applied procedures.

In its extraordinary session, the meeting approved changes to articles 9.1 and 13 of the Company's Bylaws to adapt respectively to the provisions of article 1 of Legislative Decree No. 27 dated 27 January 2010 and to implement the Procedure for related party transactions according to the “Regulations for provisions regarding related party transactions” (adopted by CONSOB with resolution No. 17221 dated 12 March 2010 and subsequently modified with resolution No. 17389 dated 23 June 2010) with new numbers for each paragraph forming article 13.

The main changes concern:

- the possibility by the Board of Directors to summon Shareholders' Meetings on a single call, replacing the past first, second and (in the case of an extraordinary Meeting) third call, provided the rule of multiple calls be applied should the Board deem appropriate not to make use of such possibility;
- the introduction in the Bylaws of the necessary provisions to attribute full effectiveness to the “Procedure for Related Party Transactions” adopted by Terna according to “Regulations for provisions regarding related party transactions” adopted by CONSOB.

(1) Taken from the list submitted by the majority shareholder Cassa Depositi e Prestiti S.p.A.

(2) Taken from the list submitted by the minority shareholder Romano Minozzi and his subsidiaries.

(3) In possession of the independence requirements established by the law, by Terna S.p.A.'s Bylaws and by the Governance Code.

(4) Taken from the list submitted by the minority shareholder Romano Minozzi and his subsidiaries.

(5) Taken from the list submitted by the majority shareholder Cassa Depositi e Prestiti S.p.A.

# Corporate bodies

## Board of Directors

### Chairman

Luigi Roth

### CEO

Flavio Cattaneo

### Directors

Cristiano Cannarsa

Paolo Dal Pino

Matteo Del Fante

Claudio Machetti

Salvatore Machi

Michele Polo

Vittorio Rispoli

### Secretary of the Board of Directors

Ernesto Calaprice

## Board of Statutory Auditors

### Chairman

Luca Aurelio Guarna

### Standing auditors

Marcello Cosconati

Lorenzo Pozza

### Alternate Auditors

Stefania Bettoni

Mario Paolillo <sup>(1)</sup>

### Independent auditors

KPMG S.p.A.

## Powers

### Board of Directors

The Board is vested by the bylaws with the broadest powers for the ordinary and extraordinary management of the Company, and specifically has the power to carry out all the actions it deems advisable to implement and attain the corporate purpose, with the sole exception of those actions that are reserved to the shareholders by law and the bylaws.

### Chairman of the Board of Directors

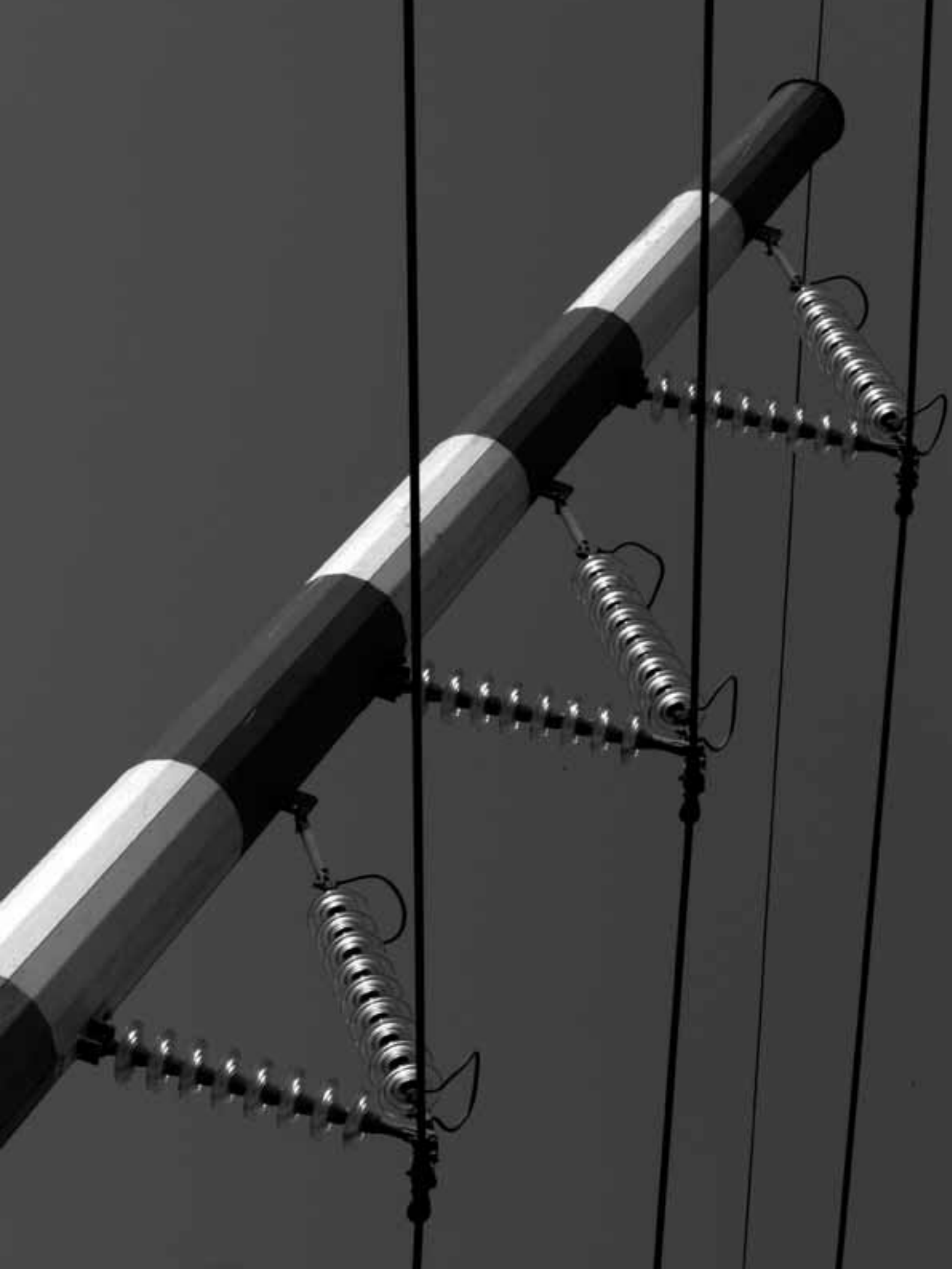
The Chairman is vested by the bylaws with the powers to represent the Company legally and to sign on its behalf, presides over Shareholders' Meetings, convenes and presides over the Board of Directors, and ascertains that the Board's resolutions are carried out.

### CEO

The Chief Executive Officer is also vested by the bylaws with the powers to represent the Company legally and to sign on its behalf, and in addition is vested by a Board Resolution with all powers for managing the Company, with the exception of those that are otherwise assigned by law or the bylaws for the Board of Directors.

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(1) Deceased on 30 November 2010.



## Terna's management



**Flavio  
Cattaneo**  
Chief  
Executive  
Officer



**Giuseppe  
Saponaro**  
Business  
Development  
Director



**Luigi  
De Francisci**  
Regulatory  
Affairs  
Director



**Giuseppe  
Lasco**  
Company  
Security  
Director



**Giovanni  
Butitta**  
External  
Relations and  
Communication  
Director



**Fabio  
Todeschini**  
Finance, Control,  
International  
and M&A  
Director



**Stefano  
Conti**  
Institutional  
Affairs  
Director



**Elisabetta  
Colacchia**  
Investor Relations  
Manager



**Gianni  
Armani**  
Italian  
Operations  
Director



**Cesare  
Ranieri**  
Human  
Resources and  
Organisation  
Director





**Luigi Roth**  
Chairman



**Alessandro Fiocco**  
Procurement Director



**Fulvio De Luca**  
Internal Audit Manager



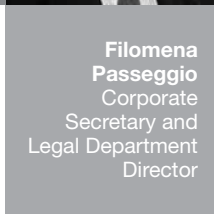
**Francesco Del Pizzo**  
Dispatching and Energy Operation Director



**Umberto Colonna**  
Facility Maintenance Director



**Pier Francesco Zanuzzi**  
Investment Planning Manager



**Filomena Passeggio**  
Corporate Secretary and Legal Department Director



**Carlo Sabelli**  
Real Time Manager



**Luciano Di Bacco**  
Administration Director and Officer in charge



**Evaristo Di Bartolomeo**  
Grid Development and Engineering Director



# The Terna Group

## The Grid, development driver

Terna is a leading grid operator for electricity transmission, chaired by Chairman Luigi Roth, and headed by CEO Flavio Cattaneo.

With over 63,000 km of electricity lines, Terna is the main owner of the high voltage National Electricity Transmission Grid, first in Europe among independent grid operators and seventh in the world.

For years, the Terna Group has been an Italian outstanding example, with 3,500 professionals involved daily in the safety of the national electricity system. The Company is responsible for the electricity grid's planning, development and maintenance joining technological expertise and innovation in line with the international best practices. It is responsible for safely transmitting and managing the electricity flow in Italy, 365 days a year, guaranteeing the balance between electricity demand and supply.

The Terna Group represents an example of excellence as an independent Transmission Grid Operator in line with the unbundling model established in the 3<sup>rd</sup> energy package of the European Union.

Terna is also a founding member of the ENTSO-E, the important European network of the Grid Operators that operates as a EU cooperation body for promoting the internal energy market and cross-border exchanges as well as guaranteeing the coordinated management and development of the electricity transmission grids.

ENTSO-E includes the participation of 41 grid operators from 34 countries with the principal objective of drafting European grid codes and adopting a ten year development plan of the electricity grid at the EU level as well as implementing medium and long term outlooks regarding the adequacy of the electricity system's generation capacity.

Terna has been listed in the Italian Stock Exchange since 2004 (ticker Bloomberg: TRN IM; ticker Thomson-Reuters: TRN.MI).

The Major Shareholder is Cassa Depositi e Prestiti with 29,86%. 67% of the share capital is owned by Italian investors while 33% belongs to over 300 foreign Institutional Investors, increased by over 50% by the IPO.

Terna's other principal shareholders include: Enel with 5.1%, Romano Minozzi with 4.4%, Pictet Funds (Europe) S.A. with 2.8% and BlackRock Inc. with 2.2 % and Assicurazioni Generali with 2%. The remaining share capital is divided among Institutional and Retail Investors. This situation is in line with the Corporate Mission: ensuring with features of the services sector a public service such as electricity transmission and creating value for shareholders.

## Asset growth in Italy

In 2010, Terna enhanced its own assets in Italy by expanding and creating greater safety for its Grid by strongly increasing lines for over 1,000 km of new power lines and 48 new stations. With the photovoltaic solar transaction, Terna began an important process for enhancing unused areas within the area of the Company-owned power stations where 60 photovoltaic solar plants have already been built that have significantly contributed to energy production from renewables in Italy.

In 2010, Terna indeed closed the greatest deal on photovoltaic solar energy in Europe: with this transaction, carried out in record breaking time, the Italian photovoltaic solar production increased by 10% and the electricity system will save 135 thousand tons a year of CO<sub>2</sub> emission. A very positive deal for Terna, for the country and its electricity system that was closed with the agreement for transferring 100% of the share capital of Rete Rinnovabile S.r.l., the photovoltaic solar company, to the London private equity fund Terra Firma. The transaction was finalized according to all obligations during the first three months of 2011 for a consideration in terms of Enterprise Value of € 641 million and net proceeds for over € 200 million.

- 63,578 km of electricity lines
  - 380 kV lines: 11,759 km
  - 220 kV lines: 12,089 km
  - ≤150 kV lines: 39,730 km
- 431 transforming and switching stations
- 634 transformers for 125,570 MVA
- 22 interconnection lines with foreign countries
- 8 Territorial Operational Areas
- 3 remote operational centers
- 1 National Control Center







## Territorial Presence

Terna continued its commitment toward a greater rootedness throughout the territory with the plan for realigning its property and enhancing its assets. New corporate offices were also planned and built in Lombardy in the Rho Pero building that is sustainable and technological. New offices were also purchased in Florence. In Rome, at the CNC National Control Center – the heart of the entire Italian electricity system – an important technological upgrade was implemented of the sophisticated management systems with the installation of a synoptic wallscreen of over 40 square meters that monitors 293 electricity lines, including 9 interconnections with foreign countries, 3 super submarine cables and 281 380 kV national lines. Terna operates in this scenario for the community making available technical and outstanding human resources, defining its strategy within a framework of great social and civil responsibility.

## Grid continental systems

In the large “European electricity continent” the fundamental resource for operating in the present and building for the future is the availability of electricity. Today, Europe has a sophisticated interconnected electricity transmission grid that integrates tens of thousands of sources located throughout the continent and the leading national energy operators. Technologically advanced, the grid must constantly be upgraded since each day new sources are added and new more efficient technology is defined; the close supervision of the entire system is the guarantee for its stability.

All of a country’s activities depend on the availability of energy and the challenge in the next years will be to face a significant growth with new business models, new technology and major transformations. Terna has been assigned a central role in achieving these objectives.

Moreover, the Company assesses international development opportunities through strategic initiatives in line with the Group’s growth objectives. Initiatives located in areas that represent a natural extension of its present activities: first of all, the Balkans and Eastern Europe. Particularly in the Balkans, Terna is ready to grasp any opportunities created by the presence of private investors in electricity transmission and to support submarine cable interconnections in the Adriatic, first of which the interconnection with Montenegro, 415 km long.

A new, major interconnection line with other countries, authorized in April 2011, will connect Italy with France, a record project for investments and technology used.

In 2010, the Company became part of the shareholders of DESERTEC Industrial Initiative (“DII”), with the same share percentage as 17 other shareholders and 25 associated partners. The project’s objective is to produce and transmit solar energy and wind power to areas in the Middle East and in North Africa (MENA), both to satisfy the local demand as well as to supply approximately 15% of the European energy demand within 2050.

Abroad, the Terna Group offers consulting services to grid operators, enhancing its know-how and technological experience, with particular focus on quality of services offered and economic-financial efficiency.

## Technology at the service of the system: efficiency and lower costs for the electricity system

Terna's National Control Center, just outside of Rome, is the heart of the national electricity system. This center carries out a detailed control of the country's entire electricity transmission grid. Sophisticated monitoring and management systems allow Terna to control, instant by instant, the electricity produced in Italy or imported from other countries and to safely manage the energy flows. Electricity cannot be stored: for this reason energy "dispatching" activity from the production plants to the places of consumption is carried out continuously and constantly 24 hours a day for a flow of approximately 326 billion kWh a year. Through the SOC Security Operations Center, the high-tech center planned and built by Terna, the Company is also capable of preventing, facing and managing critical situations in real time.

The electricity system is a complex system managed by using innovative technology for improving the safety and efficiency of the dispatching services supplies. The innovative program implemented and ongoing research for new solutions, have contributed to reaching excellent quality levels of the Italian electricity service and structurally reducing the cost of the dispatching service.

The areas of innovation include the use of complex ICT (Information and Communication Technologies) for defending the integrity of the national electricity system, safety assessments and balancing the demand as well as medium term forecasting models for optimizing maintenance programs of the grid elements with particular attention to reducing the impact of the unavailability of these elements on electricity production from non-programmable renewable sources.

The high efficiency level reached in 2010 in dispatching activities stands to witness the important reduction in the energy volume supplied to the dispatching services market both with reference to 2008 (-57%) and to 2009 (-40%). These results have led in the past two years to significant benefits for the system, such as a reduction of dispatching costs, known as the uplift, equal to € 1 billion on an annual basis comparing 2009/2010 with 2008.

The importance of the value generated by Terna for the system is also confirmed by the Authority for Electricity and Gas through incentives connected with supply activities of resources for dispatching and forecasting the demand and production from wind power, pursuant to Resolution n. 351/07 of 29 December 2007. The results obtained on incentives, exceeding the increasingly challenging targets set by the Authority, represent further evidence of the Company's strong commitment toward constantly improving the high management standards of the electricity system already reached.

As part of maintaining this commitment, Terna will continue in the next few years to invest in resources for obtaining benefits deriving from the completion of important planning initiatives and for developing new initiatives under examination.



# 362.2

**Billion kWh**  
of electricity managed in 2010.

The electricity demand  
in 2010 increased:

**+1.8%**  
**compared to 2009**

## The system in numbers

|       |  |
|-------|--|
| 0.4   | KM THE SHORTEST 380 KV LINE, OSTIGLIA-OSTIGLIA C.LE, IN LOMBARDY                           |
| 22    | INTERCONNECTION LINES WITH OTHER COUNTRIES   |
| 271   | KM THE LONGEST 380 KV OVERHEAD LINE, "SUVERETO-VALMONTONE" BETWEEN TUSCANY AND LAZIO       |
| 362.2 | BILLION OF KWH REQUIRED IN ITALY IN 2010   |
| 431   | TRANSFORMING AND SWITCHING STATIONS  |
| 435   | KM THE LENGTH OF THE SA.PE.I. SUBMARINE CABLE BETWEEN SARDINIA AND THE MAINLAND            |
| 1,000 | MW THE TRANSFER CAPACITY OF THE MOST POWERFUL LINES  |
| 1,640 | METERS THE RECORD-BREAKING DEPTH OF THE SA.PE.I. SUBMARINE CABLE, THE DEEPEST IN THE WORLD |

## History

Terna has been an essential industrial and service reality for years, among the leading players of the national energy scenario. On 1 November 2005 the unification of the ownership and management of the National Transmission Grid became effective headed by Terna, as part of the liberalization process of the electricity market that included the privatization of the grid ownership and the establishment of many different market competitors in Italy and abroad.

The appointment of the Company's new Board of Directors with Luigi Roth and Flavio Cattaneo, respectively as Chairman and CEO, marked the beginning of a new approach toward the development of the Italian electricity grid and its investments on the Italian electricity grid.

Below is a brief summary of Terna's most recent history:

**1 May 1999:** the Terna company was established within the Enel Group in compliance with Legislative Decree no. 79/99 ("Decreto Bersani") that as part of the liberalization process of the Italian electricity sector authorized the separation between the ownership and management of the National Transmission Grid. Terna's activities concern the operation and maintenance of the National Transmission Grid's plants and systems belonging to the Enel Group and their development according to the guidelines issued by the GRTN (Gestore della Rete di Trasmissione Nazionale-National Transmission Grid Operator).

**23 June 2004:** Terna was listed in the Italian Electronic Stock Exchange, with a value of € 1.70 per share.

**2005 marked a turning point: on 31 March,** Enel transferred to Institutional Investors 13.86% of Terna's share capital that it owned. On 15 September, Enel transferred 29.99% of Terna's share capital to Cassa Depositi e Prestiti and the company took on its present shareholding structure. On 1 November, the unification of ownership and management of the transmission grid became effective headed by Terna. On 2 November, the Shareholders' Meeting appointed the new Board of Directors for the 2005-2007 three year period; Luigi Roth as Chairman and Flavio Cattaneo as CEO, reconfirmed for a second three-year term on 28 April 2008.

**27 October 2006:** Terna successfully carried out the takeover aimed at listing its subsidiary Terna Participações in the Segmento Nivel 2 of the San Paolo Stock Exchange in Brazil (Bolsa de Valores de São Paulo - BOVESPA).

## Five record-breaking years

**History is built with each day: from 2005 to 2010, five years of success for Terna in the economic, financial, technological and development fields.**

With a Stock Market value that increased by over 55% from November 2005 to the end of 2010, Terna is confirmed as the leading company of the Italian Stock Exchange. Its capitalization rose from € 4.1 billion in November 2005 to € 6.3 billion at the end of 2010, allowing the Company to climb 12 positions in the FTSE Mib ranking, from 26<sup>th</sup> to 14<sup>th</sup> (11<sup>th</sup> in the industrial sector).

The Company's last 6 financial statements have demonstrated a constant growth trend for all the fundamental indicators. Over 20 consecutive steady quarters. Revenues doubled while the EBITDA margin rose from 65% to 74%. Grid investments reached € 4 billion – quadrupling the previous five year period – for 2,200 km of new power lines, a value 6 times higher than that implemented in the 2000-2004 period. The dividends policy always ensured coupons increasing over the guaranteed minimum growth of 4%: from 2005 approximately € 2 billion were distributed among shareholders, with an average annual growth of 10%.

Terna acquired over 5,000 km of grid from Acea, Edison, AEM Milano, AEM Torino, A2A and 18,000 km from Enel consequently owning more than 63,000 km of electricity lines, nearly all of the national electricity transmission grid. In 2009, Terna also sold its entire shareholding in Terna Participações, equal to 66% of the capital, leaving Brazil with returns of € 400 million. On 15 March 2010, Terna was appointed the "best utility in Europe". The "EEI International Utility Award", was received by Terna's CEO Flavio Cattaneo in London and was assigned to Terna as the best European utility for total shareholder return in the past three years: +40%, nearly 55 percentage points more compared to the average in the European sector (that registered -15%).



## “Electricity bridges”

Terna strongly accelerated activity in 2010 for four new interconnections to make Italy a Mediterranean “electricity hub”. Two with foreign countries: France and Montenegro that will add 2,000 MW of transfer capacity to the country’s import capacity. The new infrastructure toward France, in particular, represents a unique project in the world in terms of technological innovation for transforming and switching stations and materials, as well as for complex installation methods with buried cables along the Frejus tunnel and the existing highway infrastructures. The cross-border interconnections provide greater safety for the international and national electricity systems, a diversification of energy mix, Italy’s reduced dependence on a limited number of energy supplier “systems” and lower costs for the system, equal to approximately € 300 million a year.

The other two interconnections, the SA.PE.I. with Sardinia, already completed and the “Sorgente-Rizziconi” with Sicily, whose work is in progress, will contribute to reducing “bottlenecks” along the grid, also allowing to increase the quantity of energy transferred from renewables produced mainly in southern Italy. Both represent world records for the Italian electricity system. Only a few figures are necessary for the SA.PE.I., defined by the press as a record-breaking cable: the deepest in the world (-1,640 meters) and the longest in the world (435 km) with 1,000 MW of power, the highest investment ever made in Italy for an electricity project (€ 750 million), the most sustainable thanks to the innovative cable anchoring system to the sea floor for preserving and respecting the marine flora and fauna. Once completed, the new Sicily-Calabria infrastructure that is 105 km in length of which 43 in submarine cable will establish the record for the longest AC 380 kV submarine connection in the world. The project also includes building two stations in Villafranca and Scilla and a complex grid of submarine, land and overhead cables.



# Operational efficiency and sustainability

## The benefits of grid development

In 2010, Terna confirmed the acceleration implemented in these past years toward grid development with total investments for € 1,161.7 million (+30% compared to 2009).

During the year of building sites, work was completed for the SA.PE.I., the submarine connection between Sardinia and the Italian mainland, for upgrading the Val d'Ossola grid and for the "Casellina-Tavarnuzze-Santa Barbara" power line in Tuscany while work is in progress for the "Sorgente-Rizziconi" connection between Sicily and Calabria and for the Chignolo Po-Maleo power line in Lombardy.

These projects, included in Terna's Development Plan, will have many benefits for the community not only because they improve the efficiency and safety of the electricity system for everyone, but also because they will produce collective economic advantages in terms of reducing electricity bills, advantages that exceed their cost.

Terna has also constantly increased in the past years its building capacity (investments rose from € 346 million in 2006 to € 1,161.7 million in 2010), generating employment and growth in a time of economic turmoil in Italy. In 2010, only in Terna's building sites, thousands of people were employed totalling 1,973 full time employees, without considering the activities created by purchasing other goods and services.

Terna carries out its role in the electricity system, particularly for supplying a service that must have characteristics of safety, reliability, continuity and affordability, with a sense of responsibility toward the entire community which is the end user of the electricity service. This allows also carefully considering the environmental consequences of its activities and seeking benefits for the environment connected to grid development.

Particularly significant are the upgrading projects that involve, with respect to new ones, the removal of many kilometers of existing grid compared to the kilometers of new lines to be built.

In 2010, the upgrade of the Bussolengo (VR) was completed with the removal of the old "Bussolengo-Chievo" electricity line: 27 km of new electricity lines were built, 24 of which in buried cable. Approximately 45 km of obsolete overhead lines were removed for a total of 160 pylons, with important environmental advantages. The project was part of the broader plan to upgrade the HV electricity grid in the Bussolengo and Verona area that includes a series of works aimed at strengthening and creating greater safety for the territory's electricity system with savings equal to € 1.3 million a year and significantly reducing the environmental impact of the transmission plants.

Moreover, still in 2010, work began to remove the 132 kV Tirano-Campocologno overhead electricity line in Valtellina. The project is part of the upgrading of the electricity grid in Valtellina, which in turn is part of an even broader restructuring project extended also to Valcamonica. With regard to the environment, removal of the old lines will lead to important benefits regarding respecting and protecting the territory. Once the work for removing the obsolete electricity lines is completed, a total area of 1,400,000 sq.mt. of land will be eased in Valtellina involving mountains areas of particular value.

An additional environmental benefit connected to grid development will be the result of reduced CO<sub>2</sub> emissions of the electricity system owing to the reduction of losses and above all to more efficient productive assets made possible by development investments as well as connections to renewable source plants (+2,470 MW in 2010).

Overall, investments included in the 2011 Development Plan will lead to reducing 9 million tons of CO<sub>2</sub>, 5 of which for connections to renewable source plants.

In 2010, a significant contribution was made also by the activities of Rete Rinnovabile S.r.l., Terna's 100% subsidiary and sold in March 2011 which with its 62 photovoltaic solar plants located in 11 Italian regions in only one year of activity increased by 10% the Italian photovoltaic solar production, with a saving when fully operating, of approximately 135 million tons of CO<sub>2</sub> emissions.

The electricity grid's sustainable development also includes searching for shared projects with territorial authorities pursued using the SEA method - Strategic Environmental Assessment. Not only for the approval of the Development Plan, but also voluntarily on the territory (since 2002) with the local authorities for each significant project.

Still with respect to stakeholder involvement, it is highly important to include historically critical partners such as environmentalist associations in the decision-making process for identifying locations of the new lines. In this respect, in January 2009, a partnership was established with the WWF Italia for integrating planning criteria for the electricity grid with the WWF's eco-regional preservation strategy and planning environmental enhancement measures in various naturalistic WWF oases. In 2010, environmental mitigation and compensation measures were implemented in the Tuscan WWF Oases of Stagni in Focognano (FI) and Padule-Orti Bottagone (LI) and in Sicily in the Torre Salsa (AG) oasis.

The vision of a sustainable electricity grid is also focused on pylons, the elements that characterize electricity lines and which are also the most visually impacting on the environment. Solutions are being researched that consider them not

only as necessary infrastructures, but also objects with their own aesthetic dimension that can better be integrated into the landscape.

This awareness has led Terna to constantly focus on industrial design: the pylons designed by Sir Norman Foster have already been installed in Tuscany along the “Tavarnuzze-Santa Barbara” electricity line and are visible underneath the Scandicci (FI), highway exit. In 2010 the new pylons designed by the architect Hugh Dutton of the Rosental studio – winner of the International Contest that ended in 2009 – were engineered. Furthermore, still in 2010, the new tubular single pole pylons that drastically reduce both the visual impact and ground volume were installed on the Chignolo Po-Maleo electricity line in Lombardy.

## Supporting culture

During research conducted for improving the new installations, carried out together with the local authorities, Terna has offered its resources for cultural initiatives that would allow sharing with the territory the value generated with corporate activities. The Company renewed its support to the university world and was also involved in primary schools for educating on energy themes and environmental respect.

Terna's commitment was also confirmed in enhancing Italian culture both nationally and internationally and the willingness to involve a wider public of citizens while also contemplating the accessibility to the artistic heritage. With the Terna Prize for Contemporary Art, at its third edition, the Company offered culture its entrepreneurial know-how that is translated in researching, creating and experimenting innovative solutions in developing the country's electricity infrastructures at the service of culture. Meritocracy, creating value and opportunities, emerging talents and participating energies led the organization and implementation of what is today the most complete and complex project supporting Italian contemporary art based on the public/private partnerships that reflect a new type of entrepreneurial patronage of the arts.

## Grid management

Even in grid management, Terna focuses on environmental aspects. As part of protecting biodiversity, it is particularly important in building new lines to install dissuaders along the electricity lines. These are devices that make the electricity lines visible and perceivable to the birds in flight reducing the risk of collisions and installing bird houses on the pylons favouring the reproduction of various protected species. Both activities continued throughout 2010. For the first time European Rollers, protected species that are closely followed in Europe, made their nests in the bird houses installed in the upper Lazio region. There are over 500 artificial nests installed and monitored by Ornithologica, the ornithologist association with whom Terna has been collaborating for years.

Still in 2010, the study ended that was being conducted by LIPU - Italian Bird Protection League, as part of a specific agreement with Terna to assess any collision risk on the part of the birds with the electricity lines. The study, that was conducted in seven areas representing various different environmental typologies in our country, marked a first step toward scientific knowledge of the topic and identified appropriate mitigation measures.

As part of respectfully managing the environment and biodiversity, equipment containing oils with polychlorinated biphenyls (PCB) is being progressively disposed of.

Following the early elimination in 2009 of the oils with concentrations over 500 ppm, in 2010 a significant elimination occurred of those with concentrations over 50 ppm, decreasing to only 8 tons from 132 registered in 2009.



## People

In Terna's activities, human resources play a crucial role. In people, the technical expertise lies that is distinctive, rare and unique in the electricity sector allowing Terna to carry out as best as possible its activities with high professional and operational efficiency levels and to achieve its corporate objectives. The attention toward renewing this expertise represents a fundamental element in Terna's management approach toward human resources. A second element that is just as important is focusing on occupational safety, required in operational activities marked by particular risks such as the work carried out many meters about the ground and maintenance activity along the high voltage lines.

Training plays a crucial role in guaranteeing persistence and development over time of technical, managerial and behavioural expertise necessary for the electricity service and more in general for implementing corporate strategy. Terna's training programs are designed to provide people – upon entering into the Company and as ongoing training during one's professional career – with the know-how and technical expertise required for effectively covering the various different roles within the Company. During 2010, 171,146 hours of training were held (+0.5% compared to 2009), 97% of which in the classroom and 3% on line, with 49 hours of training per capita (+2% compared to 2009); in brief, in 2010, 96% of Terna's employees participated in at least one training course.

With regard to safety, in 2010, activities for monitoring building sites and contracted works were intensified and – as usual – special focus was placed on prevention: the number of safety training hours increased by 6% compared to 2009 (49,222 hours, 24,222 of which intended for workers, 20,265 for employees, 3,897 for senior staff and 175 for managers).

Terna's focus on people is confirmed in restyling and enriching its corporate intranet contents "InTernamente" and in organizing broad participation events such as the annual internal convention We:Me and meetings with the management in its territorial offices. The artistic contest "CreativInterna" received wide internal consent even in 2010 and was dedicated to biodiversity during its international year.



|              |                               |
|--------------|-------------------------------|
| <b>3,468</b> | Employees                     |
| <b>1,017</b> | Workers                       |
| <b>397</b>   | Engineers for grid developing |
| <b>10%</b>   | Women employees               |
| <b>90%</b>   | Male employees                |

## External recognition

Constantly improving its ESG performance (Environmental, Social, Governance) in the last years contributed to Terna's constant growth in sustainability ratings as well as being included in the principal international stock market sustainability indexes as well as the appreciation of socially responsible investors.

During 2010, Terna was confirmed in the Dow Jones Sustainability Index World, in the FTSE4Good Global and Europe, in the Axia Ethical and CSR, in the ECPI Ethical Global, Euro and EMU, in the MSCI (formerly known as KLD) Global Sustainability and Europe, in the ASPI Eurozone and in the Ethibel Excellence and Sustainability Europe.

Terna was also admitted to the Dow Jones Sustainability Europe Index and to the new FTSE ECPI Italia SRI Benchmark and Italia SRI Leaders indexes, the only ones considering only listed companies in the Italian Stock Market.

Terna's sustainability is also being examined by banks, investment funds, financial analysts and sustainability agencies with results that stand to witness its value.

In 2010, Terna was included as the sole transmission operator and sole Italian company in the "SAM 2011 Silver Class" of the Electric Utilities. Also this year, the German sustainability agency Oekom assessed Terna for the first time, including the company immediately into the class of "Prime Status" that indicates to socially responsible investors a condition of excellent in sustainability performances. Other recognition received by Terna in 2010 is its inclusion at 44th place and at the second among the utilities in the "Global 1000 Sustainable Performance Leader 2010" the special ranking of results obtained in the social, environment and governance field obtained by the 1,000 major world companies for capitalization and reaching the first place among the utilities and second (only 6 Italian companies are present) in the "Carbon Disclosure Leadership Index" for transparency in communication regarding its CO<sub>2</sub> emissions management.

In March 2011, Terna won the "5<sup>th</sup> Environment Enterprise Prize", promoted by the Chamber of Commerce, Industry, Crafts and Agriculture (CCIAA) in Rome and sponsored by the UNIDO - United Nations Industrial Development Organization, for the category "Best cooperation for sustainable development" with the project of bringing electricity to Kami (Bolivia) implemented by various volunteer employees with Terna's support that supported an international solidarity initiative where Terna's specific technical expertise played an important role.





# Terna and the financial markets

| FINANCIAL INDICATORS                         |                         | 30 December 2010 |
|--|-------------------------|------------------|
| <b>Weight of Terna shares <sup>(1)</sup></b> |                         |                  |
| > on the FTSE MIB index (%)                  |                         | <b>1.76%</b>     |
| > in the FTSE Italy All Share index (%)      |                         | <b>1.62%</b>     |
| <b>Rating</b>                                |                         |                  |
| Standard & Poor's                            | <i>Outlook</i>          | <b>Stable</b>    |
|  | M/L Term                | <b>A+</b>        |
|  | Short Term              | <b>A-1</b>       |
| Moody's                                      | <i>Outlook</i>          | <b>Stable</b>    |
|  | M/L Term                | <b>A2</b>        |
|  | Short Term              | <b>Prime -1</b>  |
| Fitch  | <i>Outlook</i>          | <b>Stable</b>    |
|  | M/L Term <sup>(2)</sup> | <b>A</b>         |
|  | Short Term              | <b>F1</b>        |

(1) Source: Bloomberg. Amounts at 30 December 2010.

(2) Issuer Default Rating.

## Performance of Terna share

2010 was marked by a difficult macroeconomic context and a high level of volatility on the main equity markets. In the United States and in Europe, the weak economic upturn and the high unemployment rates have led governments to adopt new plans to boost the economy and central banks have kept interest rates at all-time lows. Additionally, the continuation of the sovereign debt crisis affecting some European countries has also created further uncertainty amongst investors.

In this situation, the defensive nature of the Terna share has allowed it to record a positive performance of 5.3%, going well against the trend of negative performances recorded by the Italian Blue Chips (FTSE-MIB -13.2%) and the average posted for shares of the European sector (DJ Stoxx Utilities -8.8%). We would point out that Terna was the only European utility to have reached a record high in 2010, notably on 19 November of € 3.3925/share. During the year, the share volumes traded on the market amounted to 12.7 million shares, a rise on 2009 (10.9 million). In terms of Total Shareholder Return (TSR), namely the return inclusive of both the share trend and dividends paid during the period, Terna has guaranteed its shareholders a return of 12.2%, whilst the returns of the Italian Blue Chips index and sector were both negative (FTSE-MIB -9.8% and DJ Stoxx Utilities -3.5%).

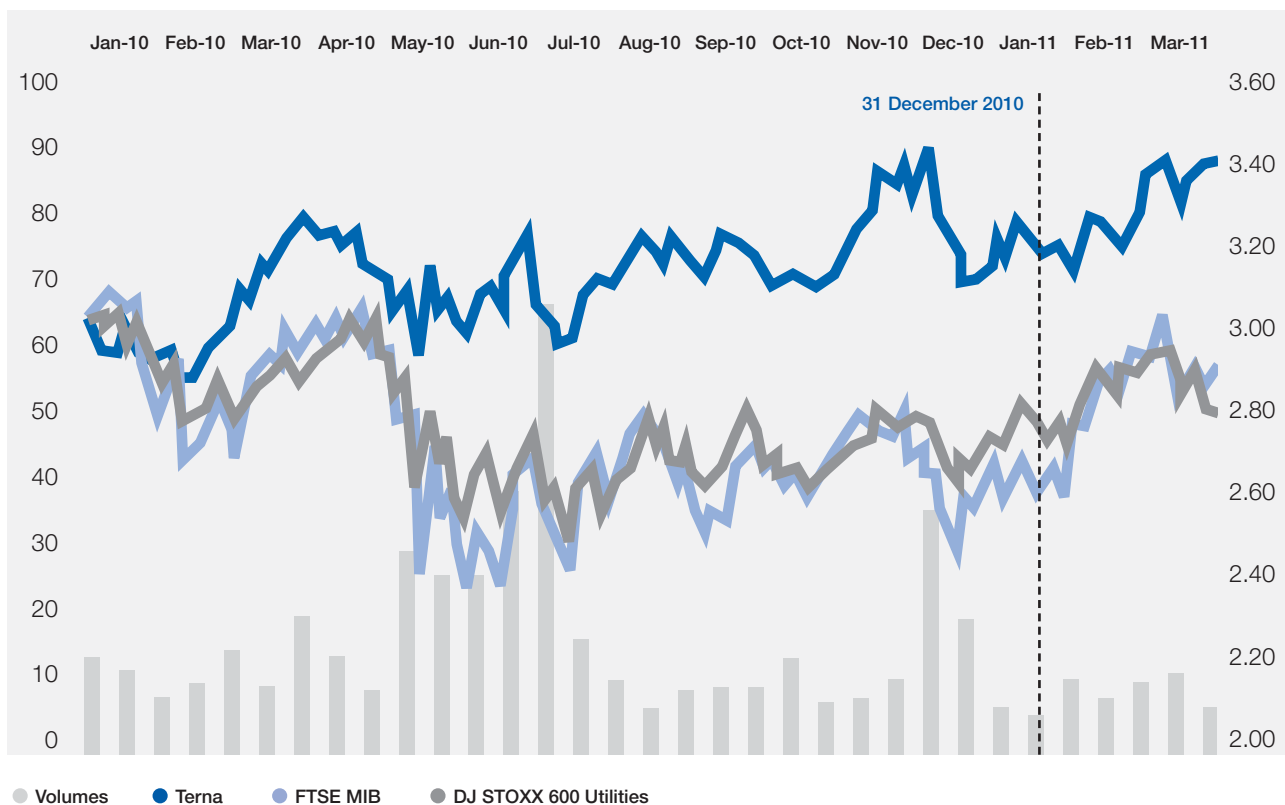
In the first few months of 2011<sup>(2)</sup>, the share gained 6.5%, whilst the sector index grew by 1.4% and the Italian market by 8.4%. From its listing (23 June 2004) until end 2010, Terna has over-performed both on the Italian market and on the sector, with appreciation of 85.9% (vs. FTSE-MIB 27.7% and DJ Stoxx Utilities +28.1%), booking a Total Return of 171.8% (vs. FTSE-MIB -7% and DJ Stoxx Utilities +73.7%).

(2) Amounts at 11 March 2011.

## PERFORMANCE OF TERNA SHARES AND THE FTSE MIB AND DJ STOXX 600 UTILITIES INDEXES

Volumes (mln)

Price



Source: Bloomberg.

## Shareholders

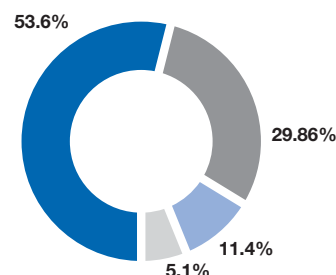
At the date on which these financial statements are prepared, the share capital of Terna S.p.A. amounts to € 442,088,020, represented by 2,009,491,000 ordinary shares, par value € 0.22 each.

Based on the register of shareholders and other information available as of the date of preparation of this report, the ownership of Terna S.p.A. is analysed as follows:

- Cassa Depositi e Prestiti S.p.A. (CdP) 29.86%
- Enel S.p.A. 5.1%
- Other Major Shareholders <sup>(3)</sup> 11.4% of which:
  - Romano Minozzi 4.4%
  - Pictet Funds (Europe) S.A. 2.8%
  - BlackRock Inc. 2.2%
  - Assicurazioni Generali 2%
- Other Institutional and Retail Investors 53.6%

### SHAREHOLDING STRUCTURE BY TYPE

- Other Institutional Investors + retail
- CdP
- Other Major Shareholders <sup>(3)</sup>
- Enel



**Total 100%**

Based on periodic surveys carried out by the Company, it is believed that 67% of the shares of Terna S.p.A. are held by Italian investors (CDP and Enel 35%, Italian Institutional Investors 5.9% and Retail Investors 26.3%), with the remaining 33% being held by foreign Institutional Investors, primarily within Europe and North America.

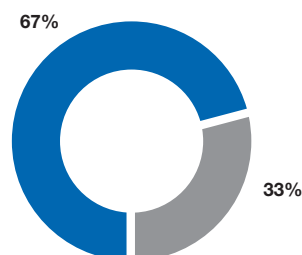
### SHAREHOLDING STRUCTURE BY GEOGRAPHIC AREA

#### Italian Investors

|                         |        |
|-------------------------|--------|
| CdP                     | 29.86% |
| Enel                    | 5.1%   |
| Retail                  | 26.3%  |
| Institutional Investors | 5.9%   |

#### Foreign Institutional Investors

|                |       |
|----------------|-------|
| UK             | 6.7%  |
| Usa/Canada     | 5.6%  |
| Europa (ex UK) | 14.3% |
| Others         | 6.2%  |

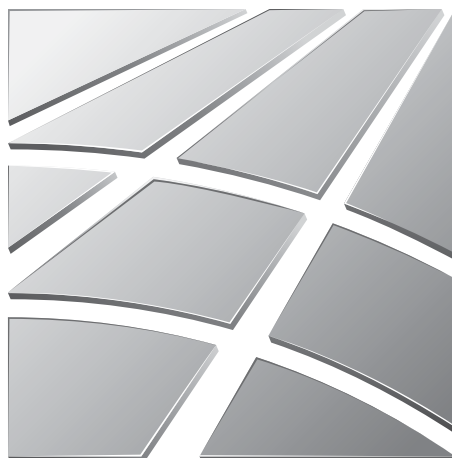


**Total 100%**

(3) The term "Major Shareholders" is used to refer to shareholders in possession of an interest of more than 2% in the share capital of Terna S.p.A., on the basis of the information available and communications received in accordance with CONSOB Resolution no. 11971/99.



2010



## Directors' Report

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## Directors' Report

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# Performance and financial position

## Highlights

2010 was a year that stood out not only for the reliability of the national power transmission grid and the continued investments forecast by the grid development plan, but also for the action taken to increase the efficiency of dispatching. It was these latter efforts in particular that have allowed us to achieve the high target for incentives, which was measured in consolidated and financial statements at fair value, in view of the three-year duration of the incentives mechanism.

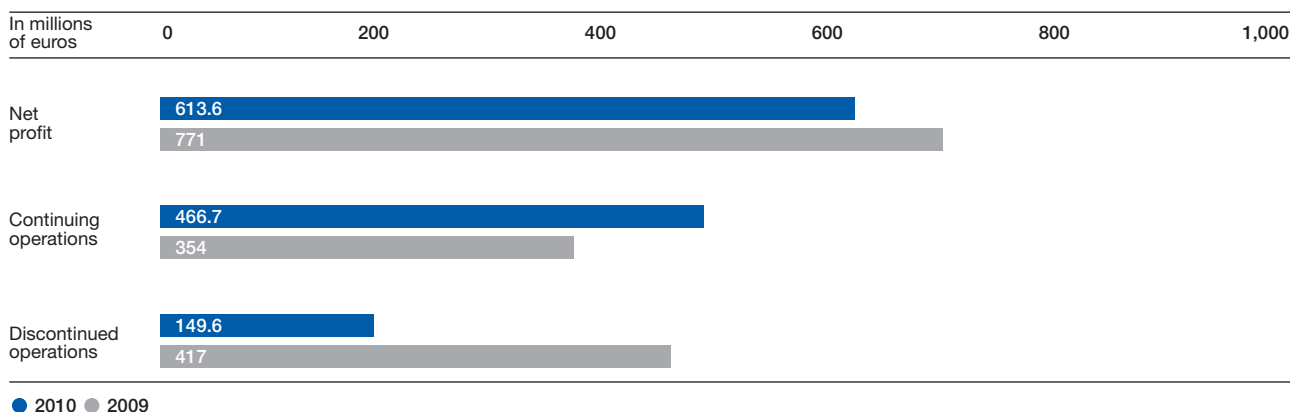
The Group has also been involved in developing the photovoltaic project, which culminated in the signing of a preliminary sales contract between Terna, SunTergrid and Terra Firma Investments (GP) 3 Limited, whereby the entire share capital of Rete Rinnovabile S.r.l. was transferred. The effect on the 2010 consolidated income statement, booked as the contract margin in terms as compared with total costs sustained during the year, on the basis of works progress, amounts to €147 million.

This event entailed the classification of the balances relating to the company RTR S.r.l. and its subsidiary Valmontone Energia S.r.l. into the item "Discontinued Operations and Assets Held for Sale" of the consolidated Statement of financial position and to item "Profit from discontinued operations and assets held for sale" of the consolidated income statement. We should also point out the acquisition of the portion of the NTG of Reti Trasmissione Energia Elettrica ASM S.r.l. ("Retrasm") by A2A S.p.A., which further strengthened the property of Terna in terms of kilometres of grid (NTG) and related remuneration.

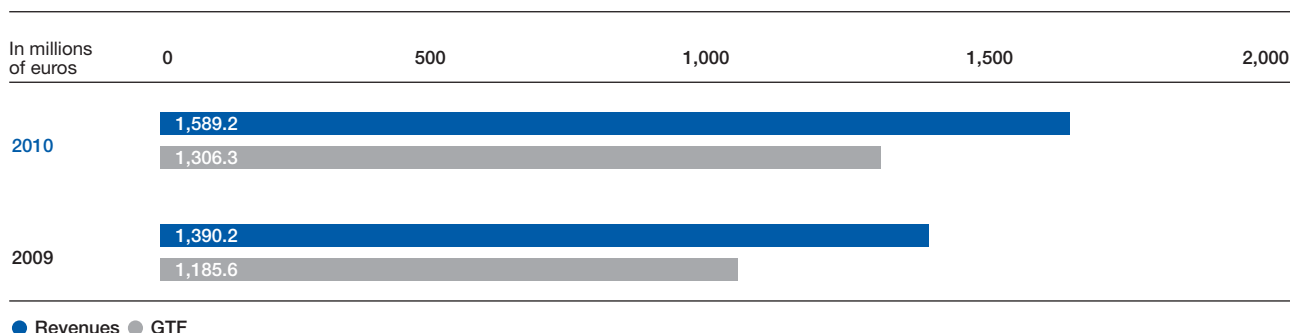
The figures discussed below have been drawn from the reclassified statements included in the section "Group performance and financial position" of this report, taken from the consolidated financial statements as described in the notes to the reclassified statements.

## Consolidated Group results

The consolidated financial statements as at and for the year ended 31 December 2010 show **a profit for the year** of €613.6 million, **entirely attributable to the owners of the Parent**. It includes €466.7 million relating to the profit from **continuing operations** and €149.6 million to the profit from **discontinued operations and assets held for sale**.



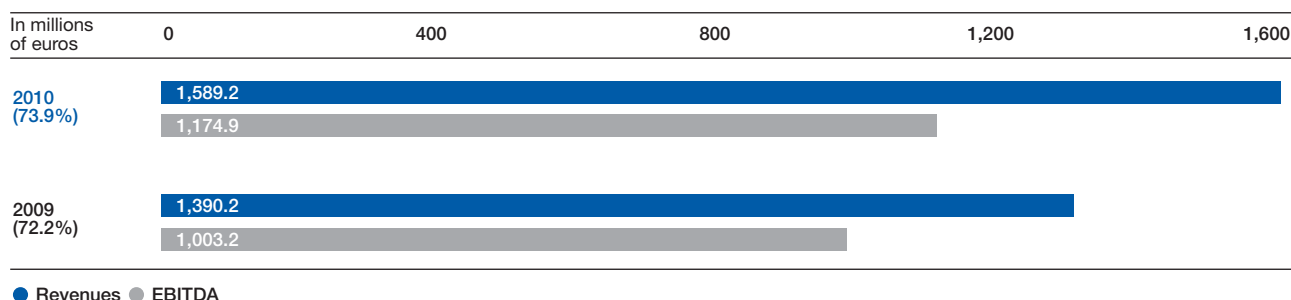
**Revenue** amounts to approximately €1,589.2 million, of which €1,306.3 million relates to the transmission payment and note an increase of €199 million (+14.3%) on 2009. More specifically, the transmission fee refers to the Parent for a total of around €1,173 million and to the subsidiary TELAT for approximately €133.3 million.



**Operating expenses** amounted to about €414.3 million, of which €212.2 million relating to personnel expense and €152.2 million to services. **EBITDA** (gross operating profit) stands at €1,174.9 million, showing an increase of €171.7 million (+17.1%) on the €1,003.2 million recorded for 2009. The subsidiary TELAT contributes for €137 million.

The **EBITDA margin** goes from 72.2% for 2009 (70.2% without considering the effects of the release of the energy discount fund) to 73.9% for 2010.

#### EBITDA MARGIN



**EBIT** (operating profit) amounted to about €814.4 million, after **depreciation and amortisation** charges of €360.5 million, of which €318.8 million recorded by the Parent and €41.7 million by the subsidiary TELAT.

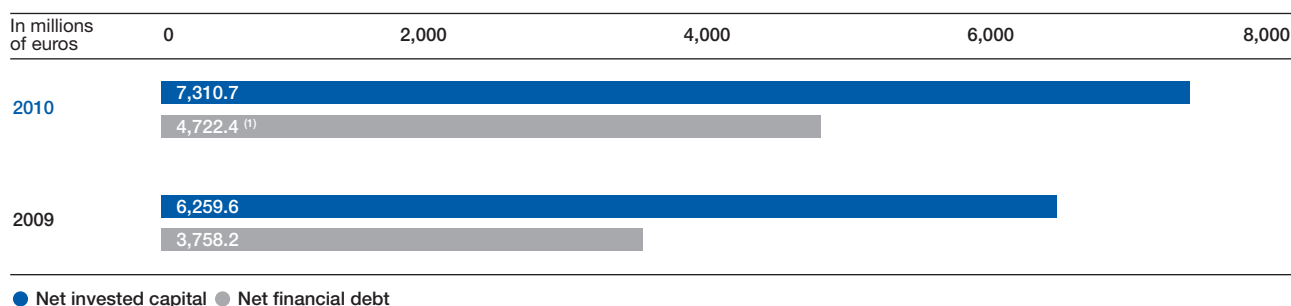
**Financial expense** for the period, with a negative balance of €102.5 million, almost entirely attributed to the Parent, records a reduction of €45.8 million (-30.9%) on 2009.

**Income taxes** for the year totalled €245.2 million, of which €230.5 million attributable to the Parent, for an effective tax rate of 34.4%.

**Profit from continuing operations** stands at €466.7 million, up €112.7 million (+31.8%) on the €354 million recorded for 2009.

**Total net invested capital**, amounting to €7,709.5 million, is covered by equity for €2,760.8 million and by **total net financial debt** for €4,948.7 million.

**Net invested capital in continuing operations** amounts to €7,310.7 million as compared with **effective net financial debt** of €4,722.4 <sup>(1)</sup> million.



The **debt/equity ratio** (effective net financial debt of continuing operations/equity) settles at 1.71.

**Total investments made in core business** by the Group during the year amount to €1,161.7 million (of which €1,103.4 million refer to property, plants and machinery), up 29.8% on the €894.7 million recorded for 2009.

(1) This includes the positive net financial position of Terna S.p.A. with regards to RTR, amounting to €254.6 million.

### Profit from discontinued operations and assets held for sale

**Profit from discontinued operations and assets held for sale** settles at €146.9 million and mainly refers to the optimisation of the margin on photovoltaic plants operating and under construction at 31 December 2010, net of the tax effect, on the basis of contractual conditions defined in the preliminary sales agreement for the subsidiary RTR, and with specific reference to the enterprise value.

Last year instead included the result achieved with the sale of the Brazilian subsidiaries, totalling €417 million.

**Discontinued operations and assets held for sale** include **net invested capital** of €398.8 and **effective financial debt** of €226.3 million, including the net financial liability of RTR to Terna S.p.A.

## Significant events

### Core business

#### TELAT-Terna plant transfer for NTG development and upgrade purposes

On **11 March 2010**, TELAT transferred certain transmission plant to the parent Terna in order to complete the development and renewal of the NTG in the Operational Territories of Milan, Padua, Florence and Naples.

In particular, pursuant to art. 6 of Presidential Decree 327/2001, the Ministry of Economic Development only delegates expropriation powers to Terna, as the concession holder for transmission and dispatching services.

The total consideration, equal to the market value of the plant transferred, was about €21 million.

#### The new “electricity bridge” across the Strait of Messina<sup>(2)</sup>

On **7 July 2010**, the last segment of the “Sorgente-Rizziconi” line between the Regions of Sicily and Calabria received the final approval from the Ministry for Economic Development. The planned investment for the “electricity bridge” across the Strait of Messina amounts to over €700 million. The new line will allow for significant savings on the electrical system, strengthening the connection between Sicily and Calabria and solving the congestion issues between the two regions. It will prevent the risk of electrical isolation of Sicily, improving the reliability, safety and quality of the Sicilian electrical system. Also important are the environmental benefits: the new line will allow avoiding about 670 million tons of CO<sub>2</sub> emissions a year and approximately 179 km of old and obsolete electricity lines will be removed.

#### Acquisition of Reti Trasmissione Energia Elettrica S.r.l. (Retrasm) and merger by incorporation into TELAT S.r.l.

On **5 August 2010**, according to the purchase contract signed on 22 December 2009 and as a result of the approval by the Antitrust Authorities, the subsidiary TELAT S.r.l. finalised the purchase of the entire quota capital of Reti Trasmissione Energia Elettrica ASM S.r.l. (“Retrasm”) from A2A S.p.A.

The price amounted to approximately €28 million.

The stipulation of the agreement occurred after the transfer to Retrasm – by way of the partial demerger of A2A Reti Elettriche S.p.A. (A2A Reti Elettriche), a company entirely controlled by A2A – of the high-voltage lines owned by A2A Reti Elettriche S.p.A. The assets transferred included 108 kilometres of power lines (at 132 kilovolts) and the bays related to these lines which were inserted within the NTG by means of the Decree of the Minister of Economic Development on 26 April 2010.

Retrasm – renamed “Rete Trasmissione Brescia S.r.l.”, electricity transmission company, managed and owned a portion of the Rete di Trasmissione Nazionale (NTG) totalling approximately 288 km of lines and relative bays, and a 220/130 kV power station.

In **November 2010** the incorporation of Rete di Trasmissione Brescia S.r.l. into TELAT S.r.l. took effect, in accordance with that envisaged by the merger project (approved on 22 September 2010 by the board of directors of the companies involved by the merger) with the cancellation of all shares of the incorporating company and with no share exchange ration nor any cash compensation.

The merger aims to improve operations of the Terna Group, increasing synergies for the pursuit of greater efficiency and a reduction in administrative costs.

#### Terna joins the DESERTEC Industrial Initiative

On **30 September 2010**, Terna S.p.A. subscribed, through a capital increase, the entrance into the ownership structure of DESERTEC Industrial Initiative (“DII”), a company incorporated under the laws of Germany and with registered office in Munich, with equal shares of 5.6%, as for the other shareholders. The subscription price was €130,000 (of which €10,000 for the nominal value and €120,000 allocated as equity-related reserve).

The DESERTEC project aims to study and facilitate the production and transmission of solar and wind power in the areas of the Middle East and North Africa (MENA), both to fulfil local demand and to be destined, in large part, to the European market.

(2) “The project is co-financed by the EU within the scope of the European Energy Programme for Recovery. Terna S.p.A. is the only responsible party for the information contained in it. The EU is not responsible of any use that could be made of the information contained in it”.

#### **Terna subscribes a capital increase to join the ownership structure of CASC**

On **10 November 2010**, Terna subscribed, together with the grid operators of Switzerland (Swissgrid), Austria (Verbund-APG), Slovenia (Eles) and Greece (HTSO), a capital increase of the company CASC (Capacity Allocation Service Company CWE S.A.) in equal shares with the founder members (which include TSO RTE, Tennet, Elia, EnBW and Amprion). CASC is a service company that was founded in 2008 and has its registered office in Luxembourg. In 2011, through a single platform, it will manage and implement the auctions for the allocation of cross border transport capacity between 12 European countries, including Italy. The operation will benefit both the power system concerned and the market operators involved in the auctions, facilitating access procedures to the individual markets.

The subscription price for the 8.3% share in the share capital of CASC was €285,000.

#### **Terna joins the ownership structure of CORESO**

On **26 November 2010**, Terna joined the ownership structure of CORESO, a service company incorporated under the laws of Belgium and with registered office in Brussels, holding a 22.485% share. The ownership structure of the company includes the operators of France (RTE), Belgium (Elia) and Great Britain (National Grid), each holding an equal share to that of Terna, and the German operator, 50Hertz Transmission, with 10%. More specifically, CORESO prepares daily forecasts and analyses in real time of energy flows in Central-Western Europe, identifying possible critical issues and duly informing the TSOs concerned in a timely manner. The total value of the transaction was €281,082.

The share held by Terna in CORESO represents an investment in an associate for the Group.

#### **Terna constitutes MEDGRID with 19 partners**

On **9 December 2010** Terna made an initial payment of € 100,000 toward the constitution of the service company MEDGRID, to be incorporated under French law with registered office in Paris. The company was incorporated on 7 January 2011, together with another 19 partners, all holding equal 5% shares in the share capital. MEDGRID aims to develop and market, in France and abroad, studies and analyses aimed at the establishing and transport of an objective of 20 Giga watts by 2020 of electricity generated from renewable sources, mainly solar, under the scope of the Plan Solaire Méditerranéen (PSM) launched in July 2008 by the Union Pour la Méditerranéen (UPM). Also through its investment in DESERTEC, Terna thus becomes one of the major European industrial operators involved in the study of the production of electricity from renewable sources in the area, and in their integration with European transport grids.

#### **Purchase of additional shares in the associate CESI S.p.A.**

On **20 December 2010** Terna finalised the acquisition from Ansaldo Trasmissione & Distribuzione S.p.A. of the 9% share in the capital of CESI S.p.A. (307,800 shares). As a result of this transaction, Terna's equity interest in CESI reached 39.906%, which, for the Terna Group, represents an investment in an associate.

CESI S.p.A. develops and manages plants and laboratories for tests, studies and experimental research.

### **Finance**

#### **Agreement with EIB to finance the SA.PE.I. project**

On **18 March 2010**, Terna S.p.A. signed an agreement with the European Investment Bank (EIB) for a further loan of €73 million to finance the project connecting Sardinia with the Italian Peninsula ("SA.PE.I.") via a 500 kV d.c., HV submarine cable. This financing, issued on 25 March 2010, is in addition to the €300 million agreed on 5 May 2008. The second financing also has a 20-year term and is repayable in half-yearly instalments from the fifth year. The economic conditions are very competitive, since the annual cost of the loan is 6-month Euribor uplifted by 40 basis points.

#### **Renewal and expansion of EMTN programme and new bond issues**

On **25 May 2010**, Terna S.p.A. renewed its Euro Medium-Term Note Programme (EMTN), increasing the amount from €2 to €4 billion as approved by the Board of Directors on **17 February 2010**, which authorised the private or public issue, on one or more occasions by 31 March 2011, of bonds totalling €1.5 billion to finance the 2010-2014 business plan. The issues, denominated in euro or other currencies, will have a maximum term of 30 years. Deutsche Bank and Citigroup were the Joint Arrangers for the programme, which has obtained ratings of A+ from Standard & Poors, A2 from Moody's and A+ from Fitch.

#### Agreement with the European Investment Bank for a loan of 300 million to fund a four-year investment plan for 2010-2013

On **24 November 2010**, Terna signed an agreement with the European Investment Bank (EIB) for a loan of €300 million aimed at strengthening and enhancing the Italian electricity transport system in order to guarantee the safety and efficiency standards required of the transmission service.

The loan will have a term of 20 years and shall be repaid in half-yearly instalments starting from the fifth year. The economic conditions are very competitive, since the annual cost of the loan is 6-month Euribor uplifted by 39 basis points.

#### Sustainability index

##### Terna enters for the first time in the Dow Jones Sustainability Index Europe

On **4 November 2010**, for the first time Terna joined the single independent grid manager in the selective European index Dow Jones Sustainability Europe, which only numbers 11 Italian enterprises out of a total of 163. Additionally, it is also confirmed in the Dow Jones Sustainability World index, which admits 12 Italian companies out of a total of 323 companies with the best sustainability performance, of the 2,500 most important companies worldwide in terms of capitalisation. With a score of 79 (an increase of 5 compared to 2009), Terna improves its position within the prestigious international sustainability index.

#### Photovoltaic project

##### Rete Rinnovabile S.r.l. (Discontinued operations)

###### Sale of business unit and capital injection to RTR

On **29 January 2010**, in order to implement the ongoing solar energy project, the Board of Directors of SunTergrid authorised the sale to RTR, a subsidiary, of the Company's line of business comprising the generators of electricity from renewable energy sources for self-consumption or sale, together with all activities and the design, construction, management, development and maintenance contracts relating to the above plant. Payment for the transaction, which took effect as from 1 February 2010, amounted to €3.2 million, in line with the market value of the branch sold, as resulting from the expert opinion prepared by independent professionals. Additionally, on the same date, the Board of Directors of SunTergrid resolved to inject capital of €5.0 million to the subsidiary. This injection was made in February.

##### Acquisition of the company Reno Solar S.r.l. and merger into RTR

On **22 July 2010**, Rete Rinnovabile S.r.l. completed the purchase of the entire share capital of Reno Solar S.r.l. ("Reno Solar"), incorporated on 25 January 2010 by Tre S.p.A. Tozzi Renewable Energy. The price paid amounted to approximately €9 million.

Reno Solar was the owner of the project relative to constructing and running a solar energy plant of approximately 35 MWp and relative concessions to the NTG in the Alfonsine Municipality (RA).

The ordinary and extraordinary Quota holders' Meeting of the acquired company, on the same date, appointed the new Sole Director and deliberated to amend the by-laws and, amongst other things, moving the company registered offices to Rome.

On **23 December 2010** the deed was stipulated for the merger by incorporation of Reno Solar S.r.l. into RTR S.r.l., with effect as from 28 December 2010, in accordance with that established by the merger project approved on 2 August 2010 by the Board of Directors of RTR and the Sole Director of Reno Solar. The merger project involved cancelling all shares of the merged company, with no change to be made to the quota capital of the merger company and with no share exchange ratio nor any cash compensation.

##### Intercompany Terna and RTR loan

On **8 September 2010**, in implementation of the resolution taken by the Board of Directors on 17 February 2010, Terna provided a loan of €500 million. The loan was stipulated for an initial duration of more than 5 years and is interest-bearing, with interest to be calculated at the EURIBOR six month rate increased by a spread of 1.70%. More specifically, compulsory early repayment is envisaged should the control structure change. On the matter, considering the company sales agreement, and as better explained in the paragraph entitled "Events after the reporting period" to which we would refer you, on **28 January 2011**, the company RTR stipulated a refinancing agreement with a pool of 7 banks, for an 18-year term and a total maximum amount of €593.8 million. This has the main aim of refinancing the investments sustained to develop the photovoltaic plant portfolio held by Rete Rinnovabile, on the basis of project financing non recourse.



#### Agreement for the disposal of RTR

On **18 October 2010** Terna, SunTergrid and Terra Firma Investments (GP) 3 Limited (wholly-owned by Terra Firma Capital Partners III, L.P.) undersigned a preliminary agreement to transfer 100% of the share capital of Rete Rinnovabile S.r.l. (and of the latter's subsidiaries).

The compensation for the operation was agreed in a modular fashion (in terms of enterprise value) on the basis of the plants which, on the closing date (31 March 2011), alternatively benefited from the incentives of the 2010 Energy Account or the Energy Account of the first months of 2011. For details of the transaction, please refer to the paragraph entitled "Events after the reporting date".

#### Acquisition of shares in the company Valmontone Energia S.r.l. and capital injection

On **25 October 2010**, the company RTR completed the acquisition of shares accounting for a total of 98.5% of the share capital (equating to €1,118,106.99) in Valmontone Energia S.r.l. from Troiani & Ciarrocchi S.r.l. and C.I.EL. S.p.A. Payment for the sale was made to the sellers for €279,526.75, corresponding to 98.5% of the share capital already paid-in (25% of the share capital) and €838,580.24 was paid directly to the company for payments of share capital subscribed by RTR and still outstanding. On 8 November 2010, the shareholders Troiani & Ciarrocchi S.r.l. and C.I.EL. also made payments of outstanding capital (totalling 1.5% of the capital).

Troiani & Ciarrocchi and C.I.EL. granted RTR the irrevocable right to purchase the entire residual interest held by them in the company's capital, which can be exercised after commissioning and testing of the solar power plants.

The sellers, as consortium winners of the tender for the building lease to realise solar power plants on land owned by the Valmontone Municipality, founded the company Valmontone Energia S.r.l., as set out by the relative licensing agreement. The business objects of the company is to design, install and manage a solar power network. Valmontone Energia S.r.l. is the owner of the project relative to constructing and running a solar energy plant of approximately 7 MWp and relative licenses to the NTG in the Valmontone Municipality (RM).

On the same date of 25 October 2010, the ordinary Meeting of the shareholders of the company acquired also appointed the new Sole Director, a new board of auditors and resolved to amend the company's Bylaws, amongst other changes moving the company's registered office to Rome.

On **8 November 2010** the Board of Directors of RTR resolved to finance the company Valmontone Energia for an amount of up to €25 million, to be delivered by making payments on capital account and/or in accordance with the terms and conditions deemed to be most appropriate and useful.

To this end, on the same date, RTR injected capital of €10 million to Valmontone Energia S.r.l.

#### Acquisition of business units from Eva Solare

On **19 November 2010**, with reference to the photovoltaic plant under construction in Brindisi 1, of authorised power of 8.4672 MWp and the photovoltaic plant under construction in Brindisi 2 of authorised power of 10.080 MWp, RTR acquired the following from Eva Solare S.r.l.:

- a) land rental contracts;
- b) the projects for the design, development and operation of photovoltaic plants and the related intellectual property rights, economic exploitation rights and rights for use, reproduction and processing, of the drawings, designs, layouts, specifications and other documents relating to the photovoltaic plants;
- c) the consolidated authorisations, which RTR successfully took over on 25 November 2010.

The price of the above transaction amounted to approximately €2.4 million for the Brindisi 1 photovoltaic plant and €0.6 million for the Brindisi 2 photovoltaic plant.





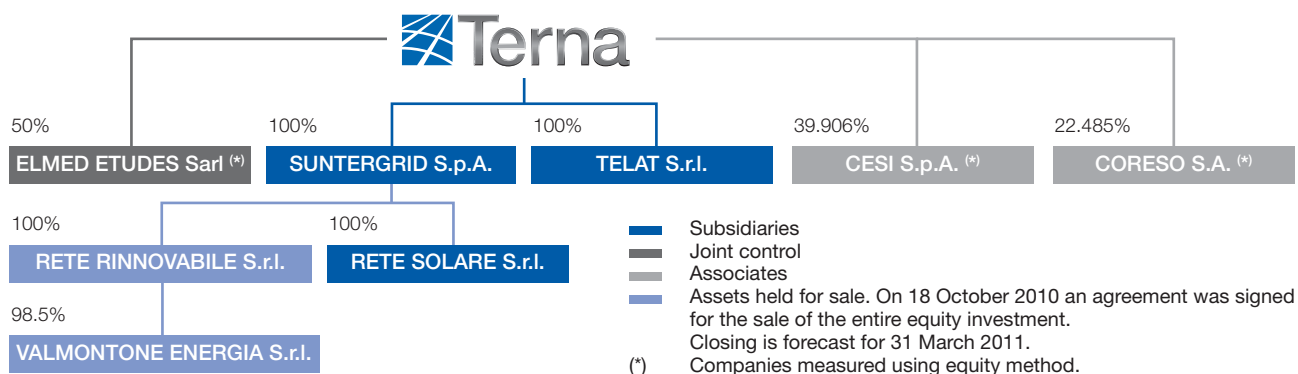
## Group performance and financial position

### Foreword

The 2010 Annual Report for the Terna Group has been prepared in accordance with art. 154-ter of Legislative Decree no. 58/98 as introduced by Legislative Decree no. 195 of 6 November 2007 (the "Transparency Decree"). In implementation of the provision of Italian Legislative Decree no. 38 of 28 February 2005 and EEC Regulation no. 1606/2002, the Terna Group prepares the consolidated financial statements as at and for the year ended 31 December 2010 in compliance with the international financial reporting standards (IFRS) issued by the International Accounting Standards Board and endorsed by the European Commission (hereinafter "IFRS-EU"). The 2010 Annual Report has been prepared on a historic cost basis, modified where necessary for certain financial instruments, as well as on a going concern basis.

### Scope of consolidation

As of the end of the financial year, the Group was organised as follows:



The change in the scope of consolidation since 31 December 2009, relates to:

### Continuing operations:

- on 18 May 2010, the subsidiary SunTergrid S.p.A. formed **Rete Solare S.r.l.** ("RTS S.r.l.") with a quota capital of €10,000. The business objects of RTS are to design, install, manage, develop and maintain grids and other infrastructure connected to such grids, as well as plant and equipment for the transmission and dispatching services of electricity, and for other segments of the energy sector and similar, related or connected sectors, together with plant for the generation of electricity from renewable or other sources, for self consumption or for sale.

It is also specified that on 5 August 2010, through the subsidiary TELAT S.r.l., the Terna Group acquired the entire share capital of "**Rete di Trasmissione Brescia S.r.l.**" (ex Reti Trasmissione Energia Elettrica ASM S.r.l. - "Retrasm") from A2A S.p.A. The company was incorporated during the year by the subsidiary TELAT.

With reference to associates, we note the following:

- the acquisition by Terna on 26 November 2010 of a 22.485% share in **CORESO S.A.**, a service company incorporated under the laws of Belgium, with registered office in Brussels, with an ownership structure that includes operators of France (RTE), Belgium (Elija) and Great Britain (National Grid) - each of which with a share equal to that held by Terna - and the German operator (50Hertz Transmission) with approximately 10%. CORESO prepares daily forecasts and analyses in real time of energy flows in Central-Western Europe, identifying possible critical issues and duly informing the TSOs concerned in a timely manner.
- On 20 December 2010, following the acquisition of a further 9% share in the share capital of the associate **CESI S.p.A.**, Terna increased its interest from 30.906% to 39.906%.

### Discontinued operations and assets held for sale:

- to the acquisition on **25 October 2010**, by RTR of the shares representing a total of 98.5%<sup>(3)</sup> of the share capital of Valmontone Energia S.r.l. from Troiani & Ciarrocchi S.r.l. and C.I.EL. S.p.A.

It is also specified that on 22 July 2010, through Rete Rinnovabile S.r.l. (RTR), the Terna Group acquired the entire share capital of **Reno Solar S.r.l.** ("**Reno Solar**") from Tre S.p.A. Tozzi Renewable Energy.

The company was incorporated during the year by the subsidiary RTR.

<sup>(3)</sup> Please note that RTR has the irrevocable right to purchase the residual shares held by the sellers, and that this right can be exercised once the photovoltaic plants have been tested and started-up.

## Basis of presentation

The criteria for reporting and measurement applied in this annual report comply with that used in the Consolidated financial statements as at and for the year ended 31 December 2009, with the exception of the application of IFRIC 12 - Service concession agreements, which came into effect on 1 January 2010. The Parent's analysis of the adoption of this interpretation identified that it applies solely to Terna's concession for the provision of dispatching services; accordingly, the property, plant and equipment and intangible assets associated with the dispatching activities identified pursuant to IFRIC 12 have been reclassified to the "Infrastructure rights" caption of intangible assets. In addition, the costs and revenue associated with the investment in dispatching activities have been reclassified as construction costs and revenue. Revenue recognised during the construction phase is limited to the amount of the internal and external construction costs incurred, considering that the fair value of the construction services is equivalent to the construction cost recognised to third-party contractors plus the internal cost of the technical personnel employed on such construction activities. By contrast, tariff revenue continues to be recognised in accordance with IAS 18 and borrowing costs continue to be capitalised pursuant to IAS 23R. The amortisation process of assets, in relation to the concession service agreements, has remained unchanged and continues to be applied considering the methods forecast for obtaining future economic benefits deriving from the use and residual value of the infrastructure, as established by the reference regulatory framework.

Following the application of the interpretation in question, with reference to the comparative balances of 2009, the balance referring to property, plant and equipment infrastructures relative to concession arrangements ex IFRIC 12 (carrying amount of €85.4 million) was reclassified from the caption "Property, plant and equipment" to "Intangible assets" and the balances capitalised in relation to construction and upgrading of infrastructure, which have been recognised to the extent of the related costs, were reclassified as construction revenue and costs (€29.5 million) without any effects on the results of the Group. The EBITDA margin of 2009 has therefore been changed, going from 73.7% to 72.2%.

With reference to the interpretation IFRIC 18 - Transfer of assets from customers, endorsed by the European Commission on 27 November 2009 and applied as from 1 January 2010 in relation to the booking of connection agreements, it is specified that the equity, financial and economic position of 31 December 2010, the Terna Group was not significantly affected.

We should note that following the signing of the sales agreement for the subsidiary RTR, as has been explained in depth in the paragraph entitled "Significant events", to which we would refer you, the balances in relation to the operations of the companies RTR and Valmontone Energia have been reclassified in accordance with that established by accounting standard IFRS 5 - Non-current assets held for sale and discontinued operations. It is also specified that on the basis of the content of the preliminary sales agreement in question, the transaction falls under the scope of agreements for the realisation of assets, for which the technical specifications and development terms for PV plants agreed with the Buyer prove to be key elements in negotiation, and can therefore be traced to the type of construction contracts regulated by IAS 11. It therefore follows that the transaction was booked on the consolidated financial statements of the Terna Group, noting the margin accrued as of 31 December 2010 on the progress made in the development of photovoltaic plants to be transferred to the Buyer, on the basis of the relevant sales price.

## Reclassified consolidated income statement

The reclassified consolidated income statement of the Terna Group for 2010 and 2009 is shown below.

| In millions of euros   | 2010           | 2009           | Change        | %             |
|--|----------------|----------------|---------------|---------------|
| <b>Revenue</b>   |                |                |               |               |
| Grid transmission fees <sup>(1)</sup>                        | 1,306.3        | 1,185.6        | 120.7         | 10.2%         |
| Other energy items <sup>(1)</sup>                            | 169.8          | 121.0          | 48.8          | 40.3%         |
| Other revenue from sales and services <sup>(1)</sup>         | 57.0           | 40.2           | 16.8          | 41.8%         |
| Other revenue and income                                     | 56.1           | 43.4           | 12.7          | 29.3%         |
| <b>Total revenue</b>   | <b>1,589.2</b> | <b>1,390.2</b> | <b>199.0</b>  | <b>14.3%</b>  |
| <b>Operating expenses</b>                                    |                |                |               |               |
| Personnel expense  | 212.2          | 185.5          | 26.7          | 14.4%         |
| Services, leases and rentals                                 | 152.2          | 149.7          | 2.5           | 1.7%          |
| Materials  | 28.2           | 12.4           | 15.8          | 127.4%        |
| Other expenses <sup>(2)</sup>                                | 21.7           | 39.4           | -17.7         | -44.9%        |
| <b>Total operating expenses</b>                              | <b>414.3</b>   | <b>387.0</b>   | <b>27.3</b>   | <b>7.1%</b>   |
| <b>Gross operating profit (EBITDA)</b>                       | <b>1,174.9</b> | <b>1,003.2</b> | <b>171.7</b>  | <b>17.1%</b>  |
| <b>Amortisation and depreciation <sup>(3)</sup></b>          | <b>360.5</b>   | <b>308.8</b>   | <b>51.7</b>   | <b>16.7%</b>  |
| <b>Operating profit (EBIT)</b>                               | <b>814.4</b>   | <b>694.4</b>   | <b>120.0</b>  | <b>17.3%</b>  |
| Net financial expense <sup>(4)</sup>                         | -102.5         | -148.3         | 45.8          | -30.9%        |
| <b>Pre-Tax profit</b>  | <b>711.9</b>   | <b>546.1</b>   | <b>165.8</b>  | <b>30.4%</b>  |
| Income taxes   | 245.2          | 192.1          | 53.1          | 27.6%         |
| <b>Profit from continuing operations</b>                     | <b>466.7</b>   | <b>354.0</b>   | <b>112.7</b>  | <b>31.8%</b>  |
| Profit from discontinued operations and assets held for sale | 146.9          | 417.0          | -270.1        | -64.8%        |
| <b>Profit for the year</b>                                   | <b>613.6</b>   | <b>771.0</b>   | <b>-157.4</b> | <b>-20.4%</b> |
| <i>Attributable to owners of the Parent</i>                  | <i>613.6</i>   | <i>771.0</i>   | <i>-157.4</i> | <i>-20.4%</i> |
| <i>Attributable to non-controlling interests</i>             | <i>0.0</i>     | <i>0.0</i>     | <i>0.0</i>    | <i>0%</i>     |

In the consolidated income statement:

(1) this amount is included in the "Revenue from sales and services" caption;

(2) it corresponds to the item "Other operating expenses" and "Amortisation, depreciation and impairment losses" for the value of the asset impairment (€0.2 million);

(3) it corresponds to "Amortisation, depreciation and impairment losses" net of the impairment of the assets (€0.2 million);

(4) total of the captions presented in points 1, 2 and 3 of letter C-"Net financial expense".

In 2010 the Terna Group achieved **revenue** of €1,589.2 million, attributed to owners of the Parent for approximately €1,444.9 million and to the subsidiary TELAT for approximately €144.3 million, up €199.0 million on last year (+14.3%) due to:

- **payment of grid transmission fees**, up +€120.7 and referring to:
  - the Parent, +€85.1 million, largely due to:
    - revision of the transmission service tariffs (+€55.0 million);
    - grid transmission fees related to the Defence plan (+€15.5 million);
    - incentive for the remuneration of strategic works pursuant to ARG/elt Resolution 87/10 (+€16.8 million);
  - to the subsidiary TELAT for the share of NTG owned, for +€35.6 million (as compared with the €97.7 million reported for April/December 2009), which also include remuneration of the grid acquired with Retrasam (+€2.8 million booked in August/December 2010);



- **other energy items, recording an increase of €48.8 million, mainly originating from greater revenue due to:**
  - optimisation of the competence of the incentives mechanism associated with the reduction in volumes procured from the Ancillary Services Market, made available under AEEG Resolution 213/09 (€77 million, being +€37 million compared with €40.0 million incentives reported in 2009 on the basis of Resolution ARG/elt 206/08). More specifically, the result achieved in 2010 has been stated at fair value in view of the three-year nature of the incentives mechanism; the greater investments in the construction and strengthening of the dispatching infrastructures, booked in application of IFRIC 12 (+€8.8 million);
  - the increase of the DIS tariff component for +€3.5 million.
- **other sales and services** (+€16.8 million) for greater services provided by the Parent to third party clients, both for engineering and systems and for the development of new projects and orders relating to stations and connections;
- **greater other revenue and income** (+€12.7 million), mainly due to:
  - recording the gain from bargain purchase (€6.0 million) deriving from the process of allocation of the price paid for the acquisition of the shareholding in Trasmissione Brescia based on the fair value at the date of acquisition of the identifiable net assets acquired;
  - reimbursements for damage to primary plants (+€3.9 million), mainly occurring last year;
  - greater prior year income recorded by the Parent (+€2.5 million).

In 2010, **operating expenses** amounted to €414.3 million and mainly referred to the Parent (€406.5 million) and subsidiary TELAT (€7.3 million), recording an increase of approximately €27.3 million on last year (+7.1%), mainly by virtue of the combined effect of the following phenomena:

- **Personnel expense:** the increase of €26.7 million is mainly due to the impact of last year's release (for €26.8 million) of the energy discount fund, following the recalculation with Enel Servizio Elettrico of the number of retired recipients of this benefit for which Terna is responsible;
- **Costs of materials:** the increase of €15.8 million mainly refers to construction and investment in the dispatching infrastructures (+€7.1 million) and greater scheduled maintenance works particularly linked to the extension of the NTG;
- **Other expenses:** the item in question shows a significant reduction of €17.7 million, for the most part due to the greater impairment of assets (+€3.5 million) and accruals to the allowance for impairment losses on receivables (€14.1 million) made last year.

**EBITDA** (gross operating profit) for the year stands at around €1,174.9 million, up €171.7 million on the €1,003.2 million recorded for 2009 (+17.1%). TELAT contributes for €137.0 million (equal to approximately 12%).

The significant increase in revenues as compared with expense is reflected on the **EBITDA margin** which goes from 72.2% for 2009 (70.2%<sup>(4)</sup>) without considering the effects of the release of the energy discount fund) to 73.9%<sup>(5)</sup> for 2010.

**Amortisation and depreciation** for the year are up by €51.7 million on 2009, for +€39.4 million due to the Parent, basically for the start-up of new plants, and for +€12.3 million to the amortisation of the subsidiary TELAT.

As a result, **EBIT** (operating profit) amounted to about €814.4 million, up by €120.0 million (+17.3%) compared with 2009.

**Net financial expense**, €102.5 million, is mainly related to the Parent and was considerably lower than the €148.3 million reported for 2009. This reduction (-€45.8 million) was principally due to the effect of:

- lower financial expense deriving from medium and long-term debt and the related hedges (€26.4 million) due to the fall in market interest rates, as partially offset by an increase in borrowing;
- positive impact of the financial component of the uplift (+€14.1 million), mainly attributed to the related financial expense in 2009) and the greater capitalisation of financial expense (+€6.2 million) linked to the growth of investments during the period.

After the impact of net financial expense, the **pre-tax profit** of €711.9 million was €165.8 million higher than last year (+30.4%).

**Income taxes** for the period amounted to €245.2 million (including -€46.1 million in net deferred taxes), up by €53.1 million compared with 2009 due, in the main, to the rise in taxable income. The period tax rate settled at 34.4% as compared with 35.2% for 2009.

(4) Corresponding to 71.8% without considering the effects of IFRIC 12.

(5) Equal to 75.8% without considering the effects of IFRIC 12.

**Profit from continuing operations** stands at €466.7 million, up €112.7 million (+31.8%) on the €354.0 million recorded for 2009.

**Consolidated profit for the year** amounts to €613.6 million and includes the **profit from discontinued operations and assets held for sale** of €146.9 million, mainly relating to the margin, net of the tax effect, accrued on photovoltaic plants operating and under construction as of 31 December 2010, measured on the basis of the defined contractual conditions, with specific reference to the enterprise value, in the preliminary sales contract for the subsidiary RTR. Last year instead included the result achieved with the sale of the Brazilian subsidiaries, totalling €417 million.

### Reclassified consolidated financial position

Reclassified consolidated statements of financial position of the Terna Group at 31 December 2010 and 31 December 2009 are presented below.

| In millions of euros  | at 31 Dec. 2010 | at 31 Dec. 2009 | Change         |
|---|-----------------|-----------------|----------------|
| <b>Net non-current assets</b>   |                 |                 |                |
| Intangible assets and goodwill  | 470.6           | 457.6           | 13.0           |
| Property, plant and equipment   | 7,802.6         | 6,989.9         | 812.7          |
| Financial assets <sup>(1)</sup>   | 30.4            | 21.0            | 9.4            |
| <b>Total</b>  | <b>8,303.6</b>  | <b>7,468.5</b>  | <b>835.1</b>   |
| <b>Net working capital</b>  |                 |                 |                |
| Trade receivables <sup>(2)</sup>  | 511.5           | 371.8           | 139.7          |
| Inventories   | 11.4            | 11.7            | -0.3           |
| Other assets <sup>(3)</sup>   | 16.2            | 10.7            | 5.5            |
| Trade payables <sup>(4)</sup>   | 480.6           | 381.3           | 99.3           |
| Net payable for pass-through energy-related items <sup>(5)</sup>                        | 77.3            | 303.4           | -226.1         |
| Tax liabilities, net <sup>(6)</sup>   | 55.7            | 14.8            | 40.9           |
| Other liabilities <sup>(7)</sup>  | 294.2           | 265.3           | 28.9           |
| <b>Total</b>  | <b>-368.7</b>   | <b>-570.6</b>   | <b>201.9</b>   |
| <b>Gross invested capital</b>   | <b>7,934.9</b>  | <b>6,897.9</b>  | <b>1,037.0</b> |
| Other provisions <sup>(8)</sup>   | 624.2           | 638.3           | -14.1          |
| Net invested capital in continuing operations   | 7,310.7         | 6,259.6         | 1,051.1        |
| Net invested capital in discontinued operations and assets held for sale <sup>(9)</sup> | 398.8           | 0.1             | 398.7          |
| <b>Total net invested capital</b>   | <b>7,709.5</b>  | <b>6,259.7</b>  | <b>1,449.8</b> |
| Equity attributable to the owners of the Parent   | 2,760.5         | 2,501.5         | 259.1          |
| Equity attributable to non-controlling interests  | 0.2             | 0.0             | 0.2            |
| Net financial debt of continuing operations <sup>(10) (*)</sup>                         | 4,977.0         | 3,758.2         | 1,218.8        |
| Net financial debt of discontinued operations and assets held for sale <sup>(11)</sup>  | -28.3           | 0.0             | -28.3          |
| <b>Total net financial debt</b>   | <b>4,948.7</b>  | <b>3,758.2</b>  | <b>1,190.5</b> |
| <b>Total</b>  | <b>7,709.5</b>  | <b>6,259.7</b>  | <b>1,449.8</b> |

Reported in the consolidated statement of financial position as:

- (1) "Equity-accounted investees", "Other non-current assets" and "Non-current financial assets" for the carrying amount of the other interests (€0.5 million);
- (2) "Trade receivables" net of the receivables for energy-related pass-through revenue (€984.3 million);
- (3) "Other current assets" net of other tax assets (€4.6 million) and "Current financial assets";
- (4) "Trade payables" net of the payables for energy-related pass-through costs (€1,061.6 million);
- (5) the receivables for energy-related pass-through revenue (€984.3 million) element of "Trade receivables" and the payables for energy-related pass-through costs (€1,061.6 million) element of "Trade payables";
- (6) "Tax assets", the other tax assets element (€4.6 million) of "Other current assets", the other tax liabilities element (€7.5 million) of "Other current liabilities" and "Tax liabilities";
- (7) "Other non-current liabilities", "Current financial liabilities" and "Other current liabilities" net of other tax liabilities (€7.5 million);
- (8) "Employee benefits", "Provisions for contingencies and charges" and "Deferred tax liabilities";
- (9) "Invested capital in discontinued operations and assets held for sale" (€547.5 million) and "Debt from discontinued operations and assets held for sale";
- (10) "Long-term loans", "Current portion of long-term loans", "Short-term loans", "Non-current financial liabilities", "Cash and cash equivalents" and "Non-current financial assets" for the value of FVH derivatives (€200.3 million).
- (11) "Invested capital in discontinued operations and assets held for sale" (€28.3 million).

(\*) **Effective net financial debt** for continuing operations, if we consider the loan and net liability of the treasury current a/c of Terna S.p.A. with regards to RTR, amounts to €4,722.4 million.

The €835.1 million increase in net non-current assets since 31 December 2009, is attributable to:

- **Intangible assets and goodwill:** post an increase of €13.0 million, entirely attributed to intangible assets and mainly due to:
  - core investments in the year for €58.3 million (of which €38.6 million in dispatching infrastructures);
  - amortisation in the period (€45.1 million including, in particular, €23.7 million for the amortisation of dispatching infrastructures and €5.6 million for the amortisation of the concession).

As described earlier, this caption includes the carrying amount of the infrastructure used by the dispatching service totalling €131.5 million at 31 December 2010 (compared with €117.2 million at 31 December 2009).

- **Property, plant and equipment:** the increase, €812.7 million, is principally attributable to the combined effect of:
  - core investments for €1,103.4 million (of which €1,063.4 million for the Parent, €40.0 million for TELAT);
  - depreciation for the year of €315.4 million;
  - grants related to assets received in the year (€12.2 million);
  - supply of €43.4 million for the portion of NTG acquired with the Brescia Transmission Grid.

**Total investments in core business** made by the Group in 2010 amount to €1,161.7 million, up 29.8% on the same figure for 2009.

- **Financial assets:** these record an increase of €9.4 million, mainly deriving from the adjustments made to equity at period end and the acquisition of a further interest (+9%) in the investment of Terna in the company CESI (respectively +€3.2 million and +€5.3 million); these also include investments by the Parent in the companies CORESO, CASC, DESERTEC and MEDGRID, as described in the paragraph entitled "Significant events", for a total of €0.8 million.

**Net working capital** stands at -€368.7 million and has absorbed liquidity for €201.9 million, essentially due to the combined effect of:

- increase in trade receivables for €139.7 million, mainly due to the payment for dispatching, which suffers the booking of fees for the incentives linked to the reduction in volumes supplied to the Ancillary Services Market described above (+€77.0 million). These also include trade receivables for the greater diversified activities performed by the Group (€33.4 million) and the incentive to CCSE for the remuneration of strategic works (+€16.8 million);
- increase in trade payables (€99.3 million), mainly due to the start-up of Pole 2 SA.PE.I.;
- a decrease in net trade payables and receivables for electricity dispatching services of the Parent, which absorbed cash totalling €226.1 million due, in the main, to the combined effect of:
  - increase in net receivables in relation to the uplift component (approx. €134.8 million);
  - recognition of net payables for the virtual interconnection fees (€85.9 million);
  - reduction of payables ascribable to the lesser volumes supplied on the Ancillary Services Market (MSD) (about €22 million);
  - reduction of payables for available production capacity (€27.5 million) and capacity payment (€54.0 million);
  - recognition of receivables covering the costs of wind power pursuant to art. 44-bis of 111/06 (€19.5 million);
  - reduction of payables linked to the essential units for the safety of the electrical system (€32.7 million);
- increase of net tax liabilities (€40.9 million), mainly due to the payable due to the tax authorities for greater current tax (€25.6 million) and collection of previous receivables (€8.8 million) due from the Greek tax authority for indirect taxes relating to the activities of the Terna branch in Greece;
- increase in other liabilities (€28.9 million) for the recognition of on advance payments (€15.6 million) and guarantee deposits for contractual obligations (€17.4 million) mainly relative to the design of interconnection infrastructure with abroad.

**Gross invested capital** therefore amounts to €7,934.9 million, up by €1,037.0 million during the period.

Other provisions record a decrease of €14.1 million, mainly ascribable to use of the net deferred tax provision (-€33.5 million), essentially recognised on previous allocations made for accelerated depreciation, net of net accruals to the Provision for risks and charges (€20.8 million), mainly for "Environmental and town planning requalification projects" linked to the works of the Parent.

**Net invested capital in continuing operations** stands at €7,310.7 million, with an increase of €1,051.1 million on 31 December 2009, against a **net effective financial debt** of €4,722.4 million, including the positive net financial position of Terna S.p.A. with regards to RTR.

**Comprehensive net invested capital** amounts to €7,709.5 million and is covered by the equity for €2,760.8 million (of which €2,760.6 million as Group equity), against the €2,501.5 million as of 31 December 2009 and the **net financial debt** of €4,948.7 million (+€1,190.5 million on 31 December 2009).

The **debt/equity ratio** (effective net financial debt of continuing operations/equity) settles at 1.71.

#### Reconciliation of consolidated profit for the year and equity with the corresponding figures for the Parent

A reconciliation of consolidated equity and profit with the amounts reported by the Parent is provided below:

| In millions of euros   | Profit<br>2010 | Equity<br>at 31 Dec. 2010 | Profit<br>2009 | Equity<br>at 31 Dec. 2009 |
|--|----------------|---------------------------|----------------|---------------------------|
| <b>Financial statements of the Parent</b>                              | <b>433.7</b>   | <b>2,534.3</b>            | <b>790.0</b>   | <b>2,468.3</b>            |
| Profit and equity contributed by TELAT                                 | 33.2           | 59.3                      | 26.1           | 26.1                      |
| Loss and net deficit - SunTergrid                                      | -1.9           | -3.0                      | -0.8           | -1.1                      |
| Profit (loss) from discontinued operations<br>and assets held for sale | 145.3          | 161.3                     | -47.2          | 0.0                       |
| Equity-accounted investees   | 3.3            | 8.7                       | 2.9            | 8.2                       |
| <b>Consolidated figures</b>  | <b>613.6</b>   | <b>2,760.6</b>            | <b>771.0</b>   | <b>2,501.5</b>            |
| Non-controlling interests  | 0,0            | 0,0                       | 0,0            | 0,0                       |
| <b>Terna Group consolidated financial statements</b>                   | <b>613.6</b>   | <b>2,760.8</b>            | <b>771.0</b>   | <b>2,501.5</b>            |

## Cash flows

### Net financial debt

| In millions of euros  | 31 Dec. 2010   | 31 Dec. 2009   | Change         |
|---|----------------|----------------|----------------|
| <b>Net financial debt of continuing operations</b>                              |                |                |                |
| <b>A. Medium and long-term debt</b>   |                |                |                |
| Bonds <sup>(1)</sup>  | 2,728.2        | 2,643.5        | 84.7           |
| Floating-rate loans <sup>(1)</sup>  | 2,419.3        | 1,555.7        | 863.6          |
| Derivative financial instruments <sup>(2)</sup>                                 | -153.2         | -40.6          | -112.6         |
| <b>Total A</b>  | <b>4,994.3</b> | <b>4,158.6</b> | <b>835.7</b>   |
| <b>B. Short-term debt (liquidity):</b>  |                |                |                |
| Floating-rate loans (current portion) <sup>(3)</sup>                            | 59.7           | 59.7           | 0.0            |
| Short-term securities   | 0.0            | -500.0         | 500.0          |
| Short-term loans  | 73.1           | 40.0           | 33.1           |
| Cash and cash equivalents   | -150.1         | -0.1           | -150.0         |
| <b>Total B</b>  | <b>-17.3</b>   | <b>-400.4</b>  | <b>383.1</b>   |
| <b>Total financial debt of continuing operations <sup>(*)</sup></b>             | <b>4,977.0</b> | <b>3,758.2</b> | <b>1,218.8</b> |
| <b>Total financial debt of discontinued operations and assets held for sale</b> | <b>-28.3</b>   | <b>0.0</b>     | <b>-28.3</b>   |
| <b>Total</b>  | <b>4,948.7</b> | <b>3,758.2</b> | <b>1,190.5</b> |

Reported in the consolidated statement of financial position as:

(1) this balance corresponds to the "Long-term loans" caption;

(2) this balance corresponds to the "Non-current financial liabilities" and "Non-current financial assets" caption for the value of FVH derivatives (€200.3 million);

(3) this balance corresponds to the "Current portion of long-term loans" caption.

(\*) **Effective net financial debt** for continuing operations, if we consider the loan and net liability of the treasury current a/c of Terna S.p.A. with regards to RTR, amounts to €4,722.4 million.

Net financial debt increased by €1,190.5 million, mainly ascribable to:

- an increase in the fair value of **bonds** (€84.7 million);
- an increase in **variable rate loans** for €863.6 million, mainly due to the use in September of the revolving credit facility of 2006 (€550 million) and the supply of new loans by the European Investment Bank (totalling €373 million). The change also incorporates the repayment of the portions due of loans in place (€59.7 million);
- an increase in the net asset balance of **derivative instruments** (+€112.6 million) as a result of:
  - change in fair value hedges of bonds for €77.1 million, ascribable to the decrease in interest rates in 2010;
  - a reduction in the cash flow hedges that cover floating-rate loans by €35.5 million;
- realisation of the investment in short-term securities issued by UBS and MPS (€500 million);
- taking out of a short-term loan for €50 million and lesser net use of cash elasticity (-€16.9 million);
- increase in the Group's cash and cash equivalents (€150.0 million).

The financial debt of discontinued operations and assets held for sale amounts to -€28.3 million and is represented by the derivative asset of CFH of the company RTR (€22.1 million) covering the loan stipulated in January 2011 – as better explained in "Events after the reporting period", to which we would refer you - in addition to bank deposits of the company Valmontone Energia (€6.2 million).

Effective financial debt of discontinued operations and assets held for sale amounts to €226.3 million if we consider the net financial liability of RTR to Terna S.p.A.

## Cash flows

| In millions of euros  | 2010<br>Cashflow | Reconciled<br>financial statements | 2009<br>Cashflow | Reconciled<br>financial statements |
|---|------------------|------------------------------------|------------------|------------------------------------|
| <b>Opening cash and cash equivalents</b>  | <b>0.1</b>       |                                    | <b>779.7</b>     |                                    |
| of which Cash and cash equivalents included<br>in discontinued operations and held for sale   | 0.0              |                                    | 90.5             |                                    |
| Profit for the year<br><i>of which Profit from continuing operations</i>  | 613.6            | 466.7                              | 771.0            | 354.0                              |
| Depreciation, amortisation  | 360.5            |                                    | 308.8            |                                    |
| Net change in provisions  | -14.1            |                                    | 213.3            |                                    |
| <i>Deferred tax assets</i>  |                  | 0.0                                |                  | 127.0                              |
| <i>Employee benefits</i>  |                  | -2.8                               |                  | -28.8                              |
| <i>Provisions for risks and charges</i>   |                  | 22.2                               |                  | 67.8                               |
| <i>Deferred tax liabilities</i>   |                  | -33.5                              |                  | 47.3                               |
| Net losses (gains) on asset disposals <sup>(1)</sup>  | -3.1             |                                    | -1.3             |                                    |
| <b>Self-financing</b>   | <b>956.9</b>     |                                    | <b>1,291.8</b>   |                                    |
| Change in net working capital:  | -201.9           |                                    | -37.6            |                                    |
| <i>Inventories</i>  |                  | 0.3                                |                  | 6.0                                |
| <i>Trade receivables</i>  |                  | -326.7                             |                  | 561.3                              |
| <i>Current financial assets</i>   |                  | 0.5                                |                  | 5.7                                |
| <i>Tax assets</i>   |                  | 1.6                                |                  | 7.5                                |
| <i>Other current assets</i>   |                  | 7.3                                |                  | 1.3                                |
| <i>Trade payables</i>   |                  | 60.2                               |                  | -398.6                             |
| <i>Tax liabilities</i>  |                  | 25.6                               |                  | 42.2                               |
| <i>Current financial liabilities</i>  |                  | -1.3                               |                  | -8.5                               |
| <i>Other liabilities</i>  |                  | 30.6                               |                  | -254.5                             |
| <b>Cash flows from operating activities</b>   | <b>755.0</b>     |                                    | <b>1,254.2</b>   |                                    |
| <b>Investment</b>   |                  |                                    |                  |                                    |
| Property, plant and equipment <sup>(2)</sup>  | -1,104.4         |                                    | -849.4           |                                    |
| Intangible assets <sup>(3)</sup>  | -58.3            |                                    | -51.0            |                                    |
| Other changes in non-current assets   | -29.7            |                                    | -309.6           |                                    |
| <i>Goodwill</i>   |                  | 0.0                                |                  | 13.7                               |
| <i>Intangible assets</i>  |                  | 0.2                                |                  | 106.4                              |
| <i>of which contribution of newly purchased companies</i>   |                  | 0.0                                |                  | -6.3                               |
| <i>Property plant and equipment</i>   |                  | -20.6                              |                  | -455.7                             |
| <i>of which contribution of newly purchased companies</i>   |                  | -43.4                              |                  | -1,101.4                           |
| <i>Non-current financial assets</i>   |                  | -0.5                               |                  | 0.0                                |
| <i>Other non-current assets</i>   |                  | -0.8                               |                  | 0.0                                |
| <i>Equity-accounted investees</i>   |                  | -8.1                               |                  | 22.7                               |
| <i>Exchange rate differences from translation of financial<br/>statements in currencies other than euro (Equity) <sup>(4)</sup></i> |                  | 0.0                                |                  | 3.4                                |
| <i>Assets of discontinued operations</i>  |                  | 0.1                                |                  | -0.1                               |
| <b>Total cash flows used in investing activities</b>  | <b>-1,192.4</b>  |                                    | <b>-1,210.0</b>  |                                    |
| <b>NIC Assets held for sale</b>   | <b>-398.8</b>    |                                    | <b>0.0</b>       |                                    |
| Change in loans   | 1,346.7          |                                    | -387.2           |                                    |
| <i>Non-current financial assets</i>   |                  | -77.1                              |                  | -7.7                               |
| <i>Current financial assets</i>   |                  | 500.0                              |                  | -499.8                             |
| <i>Non-current financial liabilities</i>  |                  | -35.5                              |                  | 15.9                               |
| <i>Long-term loans</i>  |                  | 948.3                              |                  | 243.9                              |
| <i>Current portion of long-term loans</i>   |                  | 0.0                                |                  | -19.3                              |
| <i>Short-term loans</i>   |                  | 33.1                               |                  | -120.2                             |
| <i>Discontinued operations and assets held for sale</i>   |                  | -22.1                              |                  | 0.0                                |
| Other changes in equity attributable to the owners of the Parent  | 46.3             |                                    | -11.9            |                                    |
| <i>Equity attributable to the owners of the Parent</i>  |                  |                                    |                  |                                    |
| - <i>Share capital, other reserves and retained earnings <sup>(4)</sup></i>   |                  | 46.3                               |                  | -11.9                              |
| Dividends   | -400.8           |                                    | -337.8           |                                    |
| Non-controlling interests in discontinued operations<br>and assets held for sale  | 0.2              |                                    | -86.9            |                                    |
| <b>Total cash flows from financing activities</b>   | <b>992.4</b>     |                                    | <b>-823.8</b>    |                                    |
| <b>Total cash flows for the year</b>  | <b>156.2</b>     |                                    | <b>-779.6</b>    |                                    |
| <b>Closing cash and cash equivalents</b>  | <b>156.3</b>     |                                    | <b>0.1</b>       |                                    |
| of which Cash and cash equivalents included<br>in discontinued operations and assets held for sale                                  | 6.2              |                                    | 0.0              |                                    |

(1) included in the "Other revenue and income" and "Other operating expenses" captions of the consolidated income statement;

(2) see note 13 to the financial statements;

(3) see note 15 to the financial statements;

(4) see the statement of changes in consolidated equity.



### Change in net financial position

In order to more clearly present the actual cash flows for the year, the table below shows the contribution of continuing operations to the generation or use of cash by operating activities, in investment activities, and in the remuneration of capital.

| In millions of euros   | 31 Dec.2010       | 31 Dec. 2009    |
|--|-------------------|-----------------|
| <b>Opening net financial debt</b>                                | <b>-3,758.2</b>   | <b>-3,365.8</b> |
| <b>Self-financing</b>  | <b>956.9</b>      | <b>1,291.8</b>  |
| <i>of which attributable to continuing operations</i>            | <i>810.0</i>      | <i>754.6</i>    |
| <b>Change in net working capital</b>                             | <b>-201.9</b>     | <b>-37.6</b>    |
| <b>Cash flows generated from operating activities</b>            | <b>755.0</b>      | <b>1,254.2</b>  |
| Investments in property, plant and equipment                     | -1,104.4          | -849.4          |
| Investments in intangible assets                                 | -58.3             | -51.0           |
| Other changes in non-current assets                              | -21.1             | -332.3          |
| Change in equity investments                                     | -8.6              | 22.7            |
| <b>Cash flows used in investing activities</b>                   | <b>-1,192.4</b>   | <b>-1,210.0</b> |
| <b>NIC Assets held for sale</b>                                  | <b>-398.8</b>     | <b>0.0</b>      |
| Dividends  | -400.8            | -337.8          |
| Other changes in equity attributable to the owners of the Parent | 46.3              | -11.9           |
| Equity attributable to non-controlling interests                 | 0.2               | -86.9           |
| <b>Self-financing flows</b>                                      | <b>-354.3</b>     | <b>-436.6</b>   |
| Change in financial debt   | -1,190.5          | -392.4          |
| <i>of which attributable to continuing operations</i>            | <i>-964.2 (*)</i> | <i>-804.6</i>   |
| <b>Closing net financial debt</b>                                | <b>-4,948.7</b>   | <b>-3,758.2</b> |

(\*) Including net financial position towards RTR.

The cash flows generated from operating activities for the Group during the year came to about €755 million and relate to self-financing for the year (€956.9 million, of which €810 million refer to continuing operations) and other financial resources used by net working capital (€201.9 million).

Under the scope of **self-financing**, we have a profit for the year of €613.6 million (of which €466.7 million refer to continuing operations), amortisation for €360.5 million and a net decrease in provisions amounting to €14.1 million, mainly ascribable to the use of the net deferred tax liabilities recorded on previous allocations for accelerated depreciation net of net accruals to the provision for risks and charges, as described previously.

The change in **net working capital**, equal to -€201.9 million, is for the most part due to the net balance of energy payables and receivables referring to temporary economic items.

**Investing activities** used financial resources for approximately €1,192.4 million, for the most part relating to core investments made during the period in property, plants and machinery (€1,103.4 million) and in intangible assets (€58.3 million) - ascribable to the Parent for a total of €1,120.4 million - and to the value of the NTG portion acquired with the Brescia Transmission Grid (€43.4 million) net of grants related to plants recorded during the period (€12.4 million). Under this scope, we would also mention the increased value of the investment held in the associate CESI (+€8.5 million).

**Discontinued operations and assets held for sale** have used cash flows of €398.8 million during the year, basically by virtue of the investments made for the construction and development of photovoltaic plants (€345.8 million), measured considering the margin of competence (€149 million) determined on the basis of contractual conditions defined in the preliminary sales agreement for the company RTR, net of net trade payables (€128.9 million) relating to this.

**Cash flows** used in self-financing are essentially the result of the distribution of the balance on the 2009 dividend to the owners of the Parent (€240.4 million) and the interim dividend for 2010 (€160.4 million).

**Other changes in equity** for the Group refer to the fair value measurement of derivative instruments held to hedge the variable rate debt - CFH, net of the relevant tax effect, of the Parent (€25.9 million) and the company RTR (€16 million), in addition to the effects of Stock Options exercised during the year (€7.2 million) and the acquisition of the further 9% interest in the share capital of CESI (-€2.8 million).

Financial resources used by the Group in investment, considering the extraordinary transactions implemented during the period, and the changes to equity, have resulted in total requirements of **continuing operations** of €1,562.9 million, covered by means of recourse to a new debt for €964.2 million and partly with the liquidity generated by operating activities.

## Terna S.p.A. performance and financial position

### Foreword

The 2010 annual report of Terna S.p.A. has been prepared in accordance with art. 154-ter of Legislative Decree no. 58/98 as introduced by Legislative Decree no. 195 of 6 November 2007 (the "Transparency-Decree").

In implementation of the provision of Italian Legislative Decree no. 38 of 28 February 2005 and EEC Regulation no. 1606/2002, Terna S.p.A. prepares the separate financial statements as at and for the year ended 31 December 2010 in compliance with the international financial reporting standards (IFRS) issued by the International Accounting Standards Board and endorsed by the European Commission (hereinafter "IFRS-EU").

The 2010 annual report has been prepared on a historic cost basis, modified where necessary for certain financial instruments, as well as on a going concern basis.

In compliance with the provisions of art. 2364 of the Italian Civil Code and art. 9.2 of the Company's Bylaws, the Board of Directors has resolved to call the Shareholders to meet within one hundred and eighty days of the financial year end, in view of the complexity and time required in relation to the extraordinary transactions.

### Basis of presentation

The criteria for reporting and measurement applied in this annual financial report comply with that used in the separate financial statements as of 31 December 2009, with the exception of the application of IFRIC 12 - Service concession agreements, which came into effect on 1 January 2010. The Company's analysis of the adoption of this interpretation identified that it applies solely to Terna's concession for the provision of dispatching services; accordingly, the property, plant and equipment and intangible assets associated with the dispatching activities identified pursuant to IFRIC 12 have been reclassified to the "Infrastructure rights" caption of intangible assets. In addition, the costs and revenue associated with the investment in dispatching activities have been reclassified as construction costs and revenue. Revenue recognised during the construction phase is limited to the amount of the internal and external construction costs incurred, considering that the fair value of the construction services is equivalent to the construction cost recognised to third-party contractors plus the internal cost of the technical personnel employed on such construction activities. By contrast, tariff revenue continues to be recognised in accordance with IAS 18 and borrowing costs continue to be capitalised pursuant to IAS 23R. The amortisation process of assets, in relation to the concession service agreements, has remained unchanged and continues to be applied considering the methods forecast for obtaining future economic benefits deriving from the use and residual value of the infrastructure, as established by the reference regulatory framework.

Following the application of the interpretation in question, with reference to the comparative balances of 2009, the balance referring to property, plant and equipment infrastructures relative to concession arrangements ex IFRIC 12 (net carrying amount of €85.4 million) was reclassified from the caption "Property, plant and equipment" to "Intangible assets" and the balances capitalised in relation to construction and upgrading of infrastructure, which have been recognised to the extent of the related costs, were reclassified as construction revenue and costs (€29.5 million) without any effects on the results of the Company. The EBITDA margin of 2009 has therefore been changed, going from 72.1% to 70.5%.

With reference to the interpretation IFRIC 18 - Transfer of assets from customers, endorsed by the European Commission on 27 November 2009 and applied as from 1 January 2010 in relation to the booking of connection agreements, it is specified that the equity, financial and economic position of 31 December 2010, Terna was not significantly affected.

We should note that following the signing of the sales agreement for the subsidiary RTR, as has been explained in depth in the paragraph entitled "Significant events", to which we would refer you, the balances in relation to the financial expense of the companies RTR and Valmontone Energia have been reclassified in accordance with that established by accounting standard IFRS 5 - Non-current assets held for sale and discontinued operations.

## Reclassified income statement of Terna S.p.A.

The reclassified income statement of Terna S.p.A. for 2010 and 2009 is shown below.

| In millions of euros   | 2010           | 2009           | Change        | %             |
|--|----------------|----------------|---------------|---------------|
| <b>Revenue</b>   |                |                |               |               |
| Grid transmission fees <sup>(1)</sup>                        | 1,173.0        | 1,087.9        | 85.1          | 7.8%          |
| Other energy items <sup>(1)</sup>                            | 169.8          | 121.0          | 48.8          | 40.3%         |
| Other revenue from sales and services <sup>(1)</sup>         | 116.3          | 73.8           | 42.5          | 57.6%         |
| Other revenue and income                                     | 46.0           | 42.0           | 4.0           | 9.5%          |
| <b>Total revenue</b>   | <b>1,505.1</b> | <b>1,324.7</b> | <b>180.4</b>  | <b>13.6%</b>  |
| <b>Operating expenses</b>                                    |                |                |               |               |
| Personnel expense  | 214.8          | 186.2          | 28.6          | 15.4%         |
| Services, leases and rentals                                 | 166.5          | 148.0          | 18.5          | 12.5%         |
| Materials  | 36.7           | 19.9           | 16.8          | 84.4%         |
| Other expenses   | 17.8           | 36.8           | -19.0         | -51.6%        |
| <b>Total operating expenses</b>                              | <b>435.8</b>   | <b>390.9</b>   | <b>44.9</b>   | <b>11.5%</b>  |
| <b>Gross operating profit (EBITDA)</b>                       | <b>1,069.3</b> | <b>933.8</b>   | <b>135.5</b>  | <b>14.5%</b>  |
| <b>Amortisation and depreciation</b>                         | <b>318.8</b>   | <b>279.4</b>   | <b>39.4</b>   | <b>14.1%</b>  |
| <b>Operating profit (EBIT)</b>                               | <b>750.5</b>   | <b>654.4</b>   | <b>96.1</b>   | <b>14.7%</b>  |
| Net financial expense <sup>(2)</sup>                         | -87.7          | -149.1         | 61.4          | -41.2%        |
| <b>Pre-Tax profit</b>  | <b>662.8</b>   | <b>505.3</b>   | <b>157.5</b>  | <b>31.2%</b>  |
| Income taxes   | 230.5          | 179.5          | 51.0          | 28.4%         |
| <b>Profit from continuing operations</b>                     | <b>432.3</b>   | <b>325.8</b>   | <b>106.5</b>  | <b>32.7%</b>  |
| Profit from discontinued operations and assets held for sale | 1.4            | 464.2          | -462.8        | -99.7%        |
| <b>Profit for the year</b>                                   | <b>433.7</b>   | <b>790.0</b>   | <b>-356.3</b> | <b>-45.1%</b> |

In the income statement:

(1) This amount is included in the "Revenue from sales and services" caption;

(2) Corresponds to the balance of the items described under points 1 and 2 of "C.Net financial expense".

2010 **Revenue**, amounting to €1,505.1 million, shows an increase of €180.4 million (+13.6% on the €1,324.7 million of 2009), which derives from:

- the increase of €85.1 million (+7.8%) for NTG fees, essentially as a result of the following factors:
  - revision of the transmission service tariffs (+€55.0 million);
  - grid transmission fees related to the Defence plan (+€15.5 million);
  - incentive for the remuneration of strategic works pursuant to ARG/elt Resolution 87/10 (+€16.8 million);
- the item Other energy items (+€48.8 million or +40.3%) mainly due to:
  - optimisation of the competence of the incentives mechanism associated with the reduction in volumes procured from the Ancillary Services Market, made available under AEEG Resolution 213/09 (€77 million, being +€37 million compared with €40.0 million incentives reported in 2009 on the basis of Resolution ARG/elt 206/08). More specifically, the result achieved in 2010 has been stated at fair value in view of the three-year nature of the incentives mechanism;
  - the greater investments in the construction and strengthening of the dispatching infrastructures, booked in application of IFRIC 12 (+€8.8 million);
  - the increase of the DIS tariff component for +€3.5 million.

- the item Other sales and services, which is up by €42.5 million (+57.6%), mainly due to the greater revenue deriving from non-regulated activities performed for the subsidiary TELAT (+€30.5 million, mainly ascribable to greater investments and maintenance works on the grid owned by the subsidiary) and for the implementation of new projects and orders for third party clients concerning stations and connections;
- increased other revenue and income (+€4.0 million), mainly ascribable to repayments for damages to primary plants (+€2.5 million), which mainly occurred last year, and increased prior year income recorded (+€2.5 million).

**Operating expenses** totalled €435.8 million, increasing by €44.9 million (+11.5%) from 2009 due mainly to the combined effect of the following factors:

- "Personnel expense": the increase of €28.6 million is mainly due to the impact of last year's release (for €26.8 million) of the energy discount fund, following the recalculation with Enel Servizio Elettrico of the number of retired recipients of this benefit for which Terna is responsible;
- "Services and use of third-party assets": in the amount of €166.5 million, increased by €18.5 million (+12.5 %) over the previous year due essentially to the increase in technical services and contracts for plants of the subsidiary TELAT;
- "Materials": the increase of €16.8 million is mainly to be attributed to construction and investment in dispatching infrastructures (+€7.1 million) and increased supplies of materials for lines and stations of the subsidiary TELAT;
- "Other expenses": the significant reduction, of €19.0 million for the most part refers to the increased recognition on 2009 of allocations to the allowance for impairment losses on receivables (€14.1 million), impairment of fixed assets (€2.8 million) and of the construction and investment in dispatching infrastructures (€1.9 million).

**EBITDA** (gross operating profit) reached €1,069.3 million, equal to 71% of revenue (up 0.5 percentage points from 2009), rising by €135.5 million over the €933.8 million of 2009 (+14.5%).

**Amortisation and depreciation** for the year settles at €318.8 million and is up by €39.4 million on 2009 (+14.1%), mainly due to the start-up of new plants.

**EBIT** (operating profit) came to €750.5 million, for an increase of 14.7% (+€96.1 million) from 2009.

**Net financial expense** for the year is €87.7 million and was considerably lower than the €149.1 million reported for 2009. This reduction (-€61.4 million) was principally due to the effect of:

- lower financial expense deriving from medium and long-term debt and the related hedges (€26.5 million) due to the fall in market interest rates, as partially offset by an increase in borrowing;
- positive impact of the financial component of the uplift (+€14.1 million), mainly attributed to the related financial expense in 2009) and the greater capitalisation of financial expense (+€6.2 million) linked to the growth of investments during the period;
- increased net financial income from subsidiaries (€15.9 million), mainly ascribable to the loan granted to the subsidiary TELAT.

**Income taxes** for the year came to €230.5 million (of which a negative -€37.2 million was for net deferred taxes). The incidence on the pre-tax result of continuing operation settles at 34.8% (35.5% as of 31 December 2009).

**Profit from continuing operations** stands at €432.3 million, up €106.5 million (+32.7%) on the €325.8 million recorded for 2009.

**Profit for the year**, including profit from discontinued operations and assets held for sale, stands at €433.7 million, as compared with the €790.0 million for last year, which included the gain on the sale of the share package in the Brazilian subsidiary Terna Participações (€464.2 million).

## Reclassified financial position of Terna S.p.A.

The reclassified statement of financial position of Terna S.p.A. at 31 December 2010 and 31 December 2009 is shown below.

| In millions of euros  | at 31 Dec. 2010 | at 31 Dec. 2009 | Change         |
|---|-----------------|-----------------|----------------|
| <b>Net non-current assets</b>   |                 |                 |                |
| Intangible assets and goodwill  | 362.6           | 350.2           | 12.4           |
| Property, plant and equipment   | 6,687.7         | 5,890.9         | 796.8          |
| Financial assets <sup>(1)</sup>   | 590.0           | 581.2           | 8.8            |
| <b>Total</b>  | <b>7,640.3</b>  | <b>6,822.3</b>  | <b>818.0</b>   |
| <b>Net working capital</b>  |                 |                 |                |
| Trade receivables <sup>(2)</sup>  | 511.3           | 379.8           | 131.5          |
| Inventories   | 11.4            | 11.7            | -0.3           |
| Other assets <sup>(3)</sup>   | 17.6            | 12.1            | 5.5            |
| Trade payables <sup>(4)</sup>   | 491.2           | 386.9           | 104.3          |
| Net payable for pass-through energy-related items <sup>(5)</sup>                        | 77.3            | 303.4           | -226.1         |
| Tax liabilities, net <sup>(6)</sup>   | 54.4            | -8.2            | 62.6           |
| Other liabilities <sup>(7)</sup>  | 287.9           | 265.4           | 22.5           |
| <b>Total</b>  | <b>-370.5</b>   | <b>-543.9</b>   | <b>173.4</b>   |
| <b>Gross invested capital</b>   | <b>7,269.8</b>  | <b>6,278.4</b>  | <b>991.4</b>   |
| Other provisions <sup>(8)</sup>   | 536.3           | 549.3           | -13.0          |
| Net invested capital in continuing operations   | 6,733.5         | 5,729.1         | 1,004.4        |
| Net invested capital in discontinued operations and assets held for sale <sup>(9)</sup> | 4.6             | 0.1             | 4.5            |
| <b>Total net invested capital</b>   | <b>6,738.1</b>  | <b>5,729.2</b>  | <b>1,008.9</b> |
| Equity  | 2,534.3         | 2,468.3         | 66.0           |
| Net financial debt of continuing operations <sup>(10)</sup>                             | 4,458.4         | 3,260.9         | 1,197.5        |
| Net financial debt of discontinued operations and assets held for sale <sup>(11)</sup>  | -254.6          | 0.0             | -254.6         |
| <b>Total net financial debt</b>   | <b>4,203.8</b>  | <b>3,260.9</b>  | <b>942.9</b>   |
| <b>Total</b>  | <b>6,738.1</b>  | <b>5,729.2</b>  | <b>1,008.9</b> |

In the statement of financial position these correspond to:

- (1) "Other non-current assets" and "Non-current financial assets" for the value of equity investments (€583.8 million);
- (2) "Trade receivables" net of the receivables for energy-related pass-through revenue (€984.3 million);
- (3) "Other current assets" net of other tax assets (€3.9 million) and "Current financial assets";
- (4) "Trade payables" net of the payables for energy-related pass-through costs (€1,061.6 million);
- (5) the receivables for energy-related pass-through revenue (€984.3 million) element of "Trade receivables" and the payables for energy-related pass-through costs (€1,061.6 million) element of "Trade payables";
- (6) "Tax assets", the other tax assets element (€3.9 million) of "Other current assets", the other tax liabilities element (€6.0 million) of "Other current liabilities" and "Tax liabilities";
- (7) "Other non-current liabilities", "Current financial liabilities" and "Other current liabilities" net of other tax liabilities (€6.0 million);
- (8) "Employee benefits", "Provisions for contingencies and charges" and "Deferred tax liabilities";
- (9) "Invested capital in discontinued operations and assets held for sale" (€4.6 million);
- (10) "Long-term loans", "Current portion of long-term loans", "Short-term loans", "Non-current financial liabilities", "Cash and cash equivalents" and "Non-current financial assets" for the value of the loan to TELAT and FVH derivatives (respectively €500.0 and €200.3 million).
- (11) "Invested capital in discontinued operations and assets held for sale" (€500 million) and "Debt from discontinued operations and assets held for sale" (€245.4 million).

The €818.0 million increase in net non-current assets over the figures at 31 December 2009, is attributable to the following:

- **intangible assets and goodwill**, which posted an increase of +€12.4 million, exclusively ascribable to intangible assets and due mainly to the combined effect of:
  - investments for +€57.0 million (of which +€38.6 million for infrastructure rights) in particular with reference to the development and evolution of an application software for the remote control dispatching system (€12.7 million) for the power exchange (€9.5 million) and for the protection of the electrical system (€0.6 million), in addition to general applications and software licenses (€17.8 million);

- amortisation of the year of €44.4 million (of which €23.7 million relating to dispatching infrastructures and €5.6 million relating to the amortisation of the concession for transmission and dispatching activities in Italy).
- **property, plant and equipment**, which increased by €796.8 million.

The following is a breakdown of the changes in property, plant and equipment for the year:

In millions of euros

2010

#### Investment

|                             |                |
|-----------------------------|----------------|
| Transmission lines          | 471.0          |
| Transformation stations     | 468.0          |
| Other                       | 124.4          |
| <b>Total investments</b>    | <b>1,063.4</b> |
| Depreciation                | -274.4         |
| Disposals and other changes | -13.4          |
| Intra-group purchases       | 21.2           |
| <b>Total</b>                | <b>796.8</b>   |

Therefore, the increase (€796.8 million) is the net effect of new capital expenditures (€1,063.4 million), depreciation (-€274.4 million) and disposals, impairment and other net reductions (-€13.4 million) during the year. It also reflects the acquisition of some HV transmission plants from the subsidiary TELAT (€21.2 million) for a series of urgent interventions for the development and renewal of the NTG in the Territorial Operative Areas of Milan, Padua, Florence and Naples.

**Total investments** made by the Company during the year came to €1,120.4 million (€1,063.4 million of which in property, plant and equipment and €57 in million intangible assets), up 28.5% from the €872.1 million of 2009:

- **financial assets**, which change by +€8.8 million, basically due to the acquisition (+€8 million) of the additional share in the associate CESI (+9% of the share capital), in addition to the investments in the companies CORESO, CASC, DESERTEC and MEDGRID, described in the paragraph "Significant events" (+€0.8 million).

**Net working capital** came to -€370.5 million and absorbed €173.4 million in liquidity during the year related essentially to the following:

- **Trade receivables:** increase in trade receivables for €131.5 million, mainly due to the payment for dispatching, which suffers the incentives mechanism linked to the reduction in volumes supplied to the Ancillary Services Market described above (+€77.0 million). These also include trade receivables for the greater diversified activities (+€25.7 million) and the incentive to CCSE for the remuneration of investments in strategic transmission infrastructures (+€16.8 million).
- **Trade payables:** the increased trade payables (+€104.3 million) are ascribable to the purchases and supplies for the increased investments made during the latter part of the year and mainly linked to Pole 2 of SA.PE.I. They also include the greater payable due to the subsidiary TELAT (€6.7 million), mainly ascribable to the mitigation mechanism established by ARG/elt Resolution 188/08.
- **Net payables for pass-through energy items:** the decrease (€226.1 million) is to a large extent due to the combined effect of:
  - increase in net receivables in relation to the uplift component (approx. €134.8 million);
  - reduction of payables ascribable to the lesser volumes supplied on the Ancillary Services Market (MSD) (about €22 million);
  - recognition of net payables for the virtual interconnection fees (€85.9 million);
  - reduction of payables for available production capacity (€27.5 million) and capacity payment (€54.0 million);
  - recognition of receivables covering the costs of wind power pursuant to art. 44-bis of 111/06 (€19.5 million);
  - reduction of payables linked to the essential units for the safety of the electrical system (€32.7 million).
- **Net tax liabilities:** the increase of €62.6 million mainly originates from the greater debt due to the tax authorities for the estimate of period taxes, net of advances paid (+€48.3 million; 2009 benefits from the recovery of previous receivables) and the collection of the receivable (€8.8 million) from the Greek tax authority for indirect taxes relating to the activities of the Terna branch in Greece.
- **Other liabilities:** these are up by +€22.5 million due to the recognition of advances paid for the design of the interconnection infrastructures with abroad (€15.6 million) and related caution deposits as a guarantee of contractual commitments (€17.4 million), net of the release of grant shares, in relation to the depreciation of the year of the plants for which they were recognised (€6.2 million).





The **gross invested capital** therefore settles at €7,269.8 million, recording an increase of €991.4 million as compared with 31 December 2009.

**Other provisions**, amounting to €536.3 million, record a change of -€13 million, mainly ascribable to use of the deferred tax liabilities (-€36.1 million), to a large extent for the release of previous allocations for accelerated depreciation, partially offset by net accruals to the Provision for risks and charges (€15.6 million), mainly for "Environmental and town planning requalification projects" linked to works developed by the Company.

**Net invested capital** stands at €6,783.1 million and is covered by the equity for €2,534.3 million (as compared with €2,468.3 million as of 31 December 2009) and by net financial debt for €4,203.8 million (+€942.9 million as compared with 31 December 2009).

The **debt/equity ratio** (net financial debt/equity) settles at 1.66.

The **Net financial debt of discontinued operations and assets held for sale** refers in particular to the positive net financial position of Terna vs. RTR (equal to €254.6 million), whilst the **net invested capital in discontinued operations and assets held for sale**, amounting to €4.6 million, relates to the financial asset for interest accrued and not yet collection in relation to the loan supplied to the subsidiary RTR.

The following is a breakdown of net financial debt:

| In millions of euro   | at 31 Dec. 2010 | at 31 Dec. 2009 | Change       |
|---|-----------------|-----------------|--------------|
| Long-term debt and related hedges, including the short-term portion | 5,054.0         | 4,218.3         | 835.7        |
| Short-term loans  | 73.1            | -460.0          | 533.1        |
| Cash and cash equivalents   | -150.1          | -0.1            | -150.0       |
| Financial transactions with subsidiaries                            |                 |                 |              |
| - TELAT loan  | -500.0          | -500.0          | 0.0          |
| - Net current a/c position of intercompany treasury                 | -18.6           | 2.7             | -21.3        |
| Net financial debt of continuing operations                         | 4,458.4         | 3,260.9         | 1,197.5      |
| Financial debt of continued operations and assets held for sale     | -254.6          | 0.0             | -254.6       |
| <b>Total financial debt</b>   | <b>4,203.8</b>  | <b>3,260.9</b>  | <b>942.9</b> |

For a breakdown of the individual components of this net debt at 31 December 2010, see "Cash flows" below.

## Cash flows

### Net financial debt

Net financial debt of the Company (€4,203.8 million) as of 31 December 2010 can be broken-down as follows:

| In millions of euros  | 31 Dec. 2010   | 31 Dec. 2009   | Change         |
|---|----------------|----------------|----------------|
| <b>A. Medium- and long-term debt</b>  |                |                |                |
| Bonds <sup>(1)</sup>  | 2,728.2        | 2,643.5        | 84.7           |
| Floating-rate loans <sup>(1)</sup>  | 2,419.3        | 1,555.7        | 863.6          |
| Derivative financial instruments <sup>(2)</sup>                                 | -153.2         | -40.6          | -112.6         |
| Loan to TELAT <sup>(3)</sup>  | -500.0         | -500.0         | 0.0            |
| <b>Total A</b>  | <b>4,494.3</b> | <b>3,658.6</b> | <b>835.7</b>   |
| <b>B. Short-term debt (liquidity)</b>   |                |                |                |
| Floating-rate loans (current portion) <sup>(4)</sup>                            | 59.7           | 59.7           | 0.0            |
| Short-term loans  | 73.1           | 40.0           | 33.1           |
| Short-term securities   | 0.0            | -500.0         | 500.0          |
| Net current a/c position of intercompany treasury <sup>(5)</sup>                | -18.6          | 2.7            | -21.3          |
| Cash and cash equivalent <sup>(5)</sup>   | -150.1         | -0.1           | -150.0         |
| <b>Total B</b>  | <b>-35.9</b>   | <b>-397.7</b>  | <b>361.8</b>   |
| <b>Total financial debt of continuing operations</b>                            | <b>4,458.4</b> | <b>3,260.9</b> | <b>1,197.5</b> |
| <b>Total financial debt of discontinued operations and assets held for sale</b> | <b>-254.6</b>  | <b>0.0</b>     | <b>-254.6</b>  |
| <b>Total</b>  | <b>4,203.8</b> | <b>3,260.9</b> | <b>942.9</b>   |

In the statement of financial position:

- (1) this balance corresponds to the "Long-term loans" caption;
- (2) this balance corresponds to the "Non-current financial liabilities" and "Non-current financial assets" caption for the value of FVH derivatives (€200.3 million);
- (3) this figure is included under "Non-current financial assets";
- (4) this balance corresponds to the "Current portion of long-term loans" caption;
- (5) the balance is included in "Cash and cash equivalents".

Net financial debt increased by €942.9 million. This change is due primarily to the following:

- an increase in the fair value of **bond loans** (€84.7 million);
- an increase in **variable rate loans** for €863.6 million, mainly due to the use in September of the revolving credit facility of 2006 (€550 million) and the supply of new loans by the European Investment Bank (totalling €373 million). The change also incorporates the repayment of the portions due of loans in place (€59.7 million);
- an increase in the net asset balance of **derivative instruments** (+€112.6 million) as a result of:
  - change in fair value hedges of bonds for €77.1 million, mainly ascribable to the decrease in interest rates in 2010;
  - a reduction in the cash flow hedges that cover floating-rate loans by €35.5 million;
- taking out of a short-term loan for €50 million and lesser net use of cash elasticity (-€16.9 million);
- realisation of the investment made in 2009 in short-term securities issued by UBS and MPS (€500 million);
- a €21.3 million decrease in the net position on the intercompany current accounts held with TELAT, SunTergrid and RTS for the purposes of centralised treasury management;
- a €150.0 million increase in the Company's **cash and cash equivalents**.

The debt of **discontinued operations and assets held for sale**, amounting to -€254.6 euro is represented by the loan of Terna to RTR (€500 million), granted during the period and net of the liability of the treasury current a/c (€254.4 million).

## Cash Flow

| In millions of euros   | 2010<br>Cashflow | Reconciled<br>financial statements | 2009<br>Cashflow | Reconciled<br>financial statements |
|--|------------------|------------------------------------|------------------|------------------------------------|
| <b>Opening cash and cash equivalents<br/>&amp; intercompany current accounts</b> | <b>0.1</b>       |                                    | <b>689.2</b>     |                                    |
| Profit for the year  | 433.7            |                                    | 790.0            |                                    |
| Depreciation, amortisation   | 318.8            |                                    | 279.4            |                                    |
| Net change in provisions   | -13.0            |                                    | 3.0              |                                    |
| <i>Employee benefits</i>   |                  | -2.8                               |                  | -28.8                              |
| <i>Provisions for risks and charges</i>  |                  | 17.2                               |                  | 66.3                               |
| <i>Deferred tax liabilities</i>  |                  | -27.4                              |                  | -34.5                              |
| Net losses (gains) on asset disposals <sup>(1)</sup>                             | -3.1             |                                    | -1.9             |                                    |
| <b>Self-financing</b>  | <b>736.4</b>     |                                    | <b>1,070.5</b>   |                                    |
| Change in net working capital:   | -178.0           |                                    | 180.2            |                                    |
| <i>Inventories</i>   |                  | 0.3                                |                  | 4.9                                |
| <i>Trade receivables</i>   |                  | -318.5                             |                  | 528.9                              |
| <i>Current financial assets</i>  |                  | 0.4                                |                  | 3.4                                |
| <i>Tax assets</i>  |                  | 1.6                                |                  | 7.5                                |
| <i>Other current assets</i>  |                  | 7.9                                |                  | -5.4                               |
| <i>Trade payables</i>  |                  | 65.2                               |                  | -386.8                             |
| <i>Tax liabilities</i>   |                  | 48.3                               |                  | 20.8                               |
| <i>Current financial liabilities</i>   |                  | -1.3                               |                  | -7.0                               |
| <i>Other liabilities</i>   |                  | 22.7                               |                  | 13.9                               |
| <i>Discontinued operations and assets held for sale</i>                          |                  | -4.6                               |                  | 0.0                                |
| <b>Cash flows from operating activities</b>                                      | <b>558.4</b>     |                                    | <b>1,250.7</b>   |                                    |
| <b>Investment</b>  |                  |                                    |                  |                                    |
| Property, plant and equipment <sup>(2)</sup>                                     | -1,063.4         |                                    | -821.1           |                                    |
| Intangible assets <sup>(3)</sup>   | -57.0            |                                    | -51.0            |                                    |
| Other changes in non-current assets  | -13.2            |                                    | -335.7           |                                    |
| <i>Property plant and equipment</i>  |                  | -4.7                               |                  | 24.3                               |
| <i>Intangible assets</i> <sup>(3)</sup>  |                  | 0.2                                |                  | 0.6                                |
| <i>Goodwill</i>  |                  | 0.0                                |                  | 0.0                                |
| <i>Non-current financial assets</i>  |                  | -8.1                               |                  | -359.6                             |
| <i>Other non-current assets</i>  |                  | -0.7                               |                  | -0.9                               |
| <i>Discontinued operations and assets held for sale</i>                          |                  | 0.1                                |                  | -0.1                               |
| <b>Total cash flows used in investing activities</b>                             | <b>-1,133.6</b>  |                                    | <b>-1,207.8</b>  |                                    |
| Change in loans  | 1,111.5          |                                    | -382.3           |                                    |
| <i>Current financial assets</i>  |                  | 500.0                              |                  | -500.0                             |
| <i>Non-current financial assets</i>  |                  | -77.1                              |                  | -507.7                             |
| <i>Non-current financial liabilities</i>   |                  | -35.5                              |                  | 15.9                               |
| <i>Long-term loans</i>   |                  | 948.3                              |                  | 552.2                              |
| <i>Current portion of long-term loans</i>  |                  | 0.0                                |                  | 15.1                               |
| <i>Short-term loans</i>  |                  | 30.4                               |                  | 42.2                               |
| <i>Discontinued operations and assets held for sale</i>                          |                  | -500.0                             |                  |                                    |
| <i>Liabilities of discontinued operations held for sale</i>                      |                  | 245.4                              |                  |                                    |
| Other changes in equity  | 33.1             |                                    | -11.9            |                                    |
| <i>Equity - Share capital and other reserves</i> <sup>(4)</sup>                  |                  | 33.1                               |                  | -11.9                              |
| <i>Equity - Retained earnings</i> <sup>(4)</sup>                                 |                  | 0.0                                |                  | 0.0                                |
| Dividends <sup>(4)</sup>   | -400.8           |                                    | -337.8           |                                    |
| <b>Total cash flows from financing activities</b>                                | <b>743.8</b>     |                                    | <b>-732.0</b>    |                                    |
| <b>Total cash flows for the year</b>   | <b>168.6</b>     |                                    | <b>-689.1</b>    |                                    |
| <b>Closing cash and cash equivalents<br/>&amp; intercompany current accounts</b> | <b>168.7</b>     |                                    | <b>0.1</b>       |                                    |

(1) Included in the balances of "Other revenue and income" and "Other operating expenses" of the income statement;

(2) see note 11 to the financial statements;

(3) see note 13 to the financial statements;

(4) see statement of changes in equity.

## Change in net financial position

| In millions of euros                                  | 2010            | 2009            |
|---|-----------------|-----------------|
| <b>Opening net financial debt</b>                     | <b>-3,260.9</b> | <b>-2,954.1</b> |
| <b>Self-financing</b>                                 | <b>736.4</b>    | <b>1,070.5</b>  |
| <b>Change in net working capital</b>                  | <b>-178.0</b>   | <b>180.2</b>    |
| <b>Cash flows generated from operating activities</b> | <b>558.4</b>    | <b>1,250.7</b>  |
| Investments in property, plant and equipment          | -1,063.4        | -821.1          |
| Infra-group disposals (acquisitions) of fixed assets  | -21.2           | 0.0             |
| Investments in intangible assets                      | -57.0           | -51             |
| Disposals (acquisitions) of equity investments        | -8.1            | -359.6          |
| Other changes in non-current assets                   | 16.1            | 23.9            |
| <b>Cash flows used in investing activities</b>        | <b>-1,133.6</b> | <b>-1,207.8</b> |
| Dividends distributed                                 | -400.8          | -337.8          |
| Other changes in equity                               | 33.1            | -11.9           |
| <b>Equity movements</b>                               | <b>-367.7</b>   | <b>-349.7</b>   |
| Change in financial debt                              | -942.9          | -306.8          |
| <b>Closing net financial debt</b>                     | <b>-4,203.8</b> | <b>-3,260.9</b> |

The liquidity generated by operating activities during the year, amounting to €558.4 can be ascribed to self-financing (€763.4 million) and to changes in net working capital (-€178.0). More specifically, **self-financing** includes the profit for the year for €433.7 million, amortisations for €318.8 million and the net decrease in funds for €13.0 million. **NWC management** has used net financial resources for €178.0 million, for the most part ascribable to the net balance of energy receivables and payables referring to pass-through economic items, the increase of trade receivables mainly with reference to the incentive mechanism linked to the reduction of volumes supplied to the Ancillary Services Market and to the greater diversified activities implemented by the Company. Said change is partially offset by the payables due to suppliers for the greater investments made and the increase in net payables due to the tax authority, mainly for current taxes.

**Investing activities** led to a net use of cash of about €1,133.6 million. These cash flows mainly concerned investments in property, plant and equipment (€1,063.4 million) and intangible assets (€57.0 million) for the year, net of plant grants recognised during the year (€12.3 million). The flow also reflects the acquisition from the subsidiary TELAT of some transmission plants subject to development and renewal (€21.2 million) in addition to the further investment share acquired in the associate CESI (€8.0 million).

**Cash flows** in respect of equity movements are essentially the result of the distribution of the balance for the 2009 dividend (€240.4 million) and the interim dividend for 2010 (€160.4 million). Other changes to equity refer to the adjustment to fair value of derivative instruments hedging variable rate payables - net of the related tax effect (€25.9 million) and the effects of the exercise of Stock Options during the year (€7.2 million).

Therefore, cash flows absorbed by investing activities and equity movements for the year resulted in total uses of liquidity in the amount of €1,501.3 million, which was funded in part by cash flows generated from operating activities (€558.4 million) and the remaining €942.9 million through new debt.

# The business

## National Transmission Grid

The following table provides greater detail about the number of Terna Group transmission plants at 31 December 2010:

|                     | Terna Group            |                        |                        |
|---------------------|------------------------|------------------------|------------------------|
|                     | 31 Dec. 2010           | 31 Dec. 2009           | Change                 |
| Stations            | no. 431                | no. 383                | + no. 48               |
| Transformers        | no. 634<br>125,571 MVA | no. 620<br>121,501 MVA | + no. 14<br>+4,070 MVA |
| Bays                | no. 4,825              | no. 4,537              | + no. 288              |
| Lines               | 57,638 km              | 56,691 km              | +947 km                |
| 3-phase power lines | no. 3,981<br>63,578 km | no. 3,891<br>62,503 km | + no. 90<br>+1,075 km  |

### Number of plants - Terna

The number of plants belonging to Terna at 31 December 2010, and 31 December 2009, is shown in the following table:

|                     | Terna                  |                        |                        |
|---------------------|------------------------|------------------------|------------------------|
|                     | 31 Dec. 2010           | 31 Dec. 2009           | Change                 |
| Stations            | no. 412                | no. 383                | + no. 29               |
| Transformers        | no. 632<br>125,251 MVA | no. 620<br>121,501 MVA | + no. 12<br>+3,750 MVA |
| Bays                | no. 4,706              | no. 4,537              | + no. 169              |
| Lines               | 40,805 km              | 39,819 km              | +986 km                |
| 3-phase power lines | no. 2,247<br>45,707 km | no. 2,167<br>44,560 km | + no. 80<br>+1,147 km  |

### Stations

In relation to the stations, in particular, the start-up of 29 plants is noted:

- 3 new transformation stations: Castegnero, Maida and Bisaccia;
- 13 new switching stations: Turano, San Severo, Ittiri, Sambuca, Cattolica Eraclea, Castelnuovo, Castel di Lucio, Cianfurro, Scampitella, Licodia Eubea e Villafrati, San Bellino and Fenis;
- 12 132 kV stations acquired from SET Distribuzione;

### Transformers

An additional 12 transformers went into operation compared with 31 December 2009, corresponding to a 3,750 MVA increase in transformation capacity. Specifically, there were 6 new 380 / 207 / 207 kV single-phase machines introduced at the Latina and Fumesanto conversion stations, operations began at pole 2 of the SA.PE.I. connection, and 6 new 380 / 150 kV machines at the stations of Maida, Bisaccia 380, Brindisi Pignicelle and Santa Sofia were added.

### Long distance power lines

In relation to power lines, the total length of three-phase lines has increased by 1,147 km as compared with 31 December 2009, whilst those of lines has increased by 986 km. More specifically, we note the start-up of pole 2 of the underwater 500 kV connection of SA.PE.I. between the stations of Latina and Fumesanto for a total of 458.8 km and the acquisition



from SET Distribuzione of 15 lines for a total of 171.7 km (of which: 4 at 132 kV, equal to 32.8 km; 11 at 60 kV, equal to 138.9 km).

We would also point out that as of 31 December 2010, the lines and three-phase lines owned by the Parent also included those (32 lines for a total of 381 km) of some plants subject to urgent development and renewal works in the territorial operative areas of Milan, Padua, Florence and Naples, transferred from the subsidiary TELAT in March.

### Number of plants - TELAT

The number of plants belonging to TELAT at 31 December 2010, and 31 December 2009, is shown in the following table:

|                     | TELAT        |              |           |
|---------------------|--------------|--------------|-----------|
|                     | 31 Dec. 2010 | 31 Dec. 2009 | Change    |
| Stations            | no. 19       | -            | + no. 19  |
| Transformers        | no. 2        | -            | + no. 2   |
|                     | 320 MVA      | -            | +320 MVA  |
| Bays                | no. 119      | -            | + no. 119 |
| Lines               | 16,833 km    | 16,872 km    | -39 km    |
| 3-phase power lines | no. 1,734    | no. 1,724    | + no. 10  |
|                     | 17,871 km    | 17,943 km    | -72 km    |

### Stations and transformers

In relation to stations and transformers, the changes recorded are all ascribable to the assets achieved with the merger of the Brescia Transmission Network.

### Long distance power lines

As of 31 December 2010, the extent of the lines and three-phase lines derives basically from the combined effect of the following factors:

- 32 lines for a total of 381.0 km concerned by the above sale to Terna;
- 25 lines for a total of 287.9 km acquired with the merger of Brescia Transmission Network;
- 2 lines acquired by Enel Distribuzione for a total of 72.8 km;
- 8 new lines activated for a total of 41.2 km: Baronissi - Mercatello 150 kV (6.3 km), Aversa - Aversa RFI 150 kV (2.2 km), Gricignano - Aversa RFI 150 kV (6.5 km), Torre Nord - Torre Sud 60 kV (3.7 km), Mulini - Quattroventi 150 kV (4.8 km), Siracusa Nord - Siracusa Est 150 kV (6.6 km), cp Monselice - cp Este Nuova 132 kV (9.9 km), Fano Z.I. - Profilglass 132 kV (1.2 km).

### Development Plan for the NTG

On 29 January 2010, in compliance with the Ministerial Decree of 20 April 2005, the Development Plan for 2010 was submitted to the relevant authorities for approval.

The 2010 Development Plan was approved by the Terna Board of Directors on 16 December 2009, having already been favourably received by the Users' Consultative Committee<sup>(6)</sup> (which on 31 October 2009 approved the new developments initiatives included in the Plan and on 25 November 2009 approved the Plan in its entirety).

The latest version of the Development Plan takes account of the instructions that the Ministry for Economic Development attached to its Final Approval of the 2009 Development Plan<sup>(7)</sup>.

These conditions regarded:

- "accelerating activities for a further reduction in congestion, while fostering planned interconnections with new energy markets in the north-eastern and southern quadrants, in particular regarding completion of the Adriatic backbone and the 380 kV ring in Sicily";
- "ensuring the development of renewable energy resources in compliance with targets agreed at the European level" by resolving "in particular in the southern areas of the country, issues associated with grid plants arising out of a boom in this type of non-programmable energy";
- monitoring the "implementation of new regulations that provide for the return of nuclear power generation to Italy with regard to the repercussions this will have on the national electricity grid";

(6) The Users' Consultative Committee, established by Prime Minister Decree dated 11 May 2004, expresses a non-binding opinion on the Development Plan as required by Competition Authority Decision no. 14542 dated 4 August 2005.

(7) On 23 December 2009, the Ministry for Economic Development (MED) approved the 2009 Development Plan through the publication of its final ruling, which came out in the Official Journal of 20 January 2010, no. 15.



- bearing in mind “development of distributed generation and new developments in bidirectional grid use associated with this type of plant, which must be taken into consideration, and coordination with local distributors in order to adopt and develop the required technological upgrades”;
- as soon as is feasible, beginning the authorisation process for work to connect the islands situated off the Campania region to the national electricity grid in order to resolve the repeated critical issues affecting the electricity system during the tourist season.

The 2010 Development Plan adopts the structure of the previous year's version and is divided into two sections. *2010 Development Plan - Section I*, describing the reference framework and the new needs for development, as were seen in 2009 (in accordance with Italian Legislative Decree n. 152/06, this section is subject to *Strategic Environmental Assessment procedures*, which took place on 2 October 2009). *Progress of previous plans – Section II* where the progress made on the interventions envisaged by previous Development Plans, already approved and confirmed in this Plan, is explained. Specifically, the plan highlights the development of the European transmission network. In fact, the European Commission notes the need for network operators to work together to develop a European network in order to ensure that transmission capacity keeps pace with demand and that national electricity markets are integrated.

The European Development Plan (2010 version) was prepared as part of the ENTSO-E<sup>(8)</sup> project in which Terna is directly involved in the following regional forums: Terna is both a member and the coordinator of the Continental Central South Regional Forum, and is a member of the Continental South East Forum. Terna has supported its community-interest projects, giving particular precedence to new interconnections and resolving internal NTG congestion. The 2010 Development Plan envisages investments of around €3.14 billion in the period 2010-2014 (an increase compared with the 2009 version of the Plan) and €3.77 billion in the five years thereafter. The implementation of the Development Plan will increase the size of the national transmission grid by adding around 4,800 km of new lines and 140 new stations with a transformation capacity of around 32,500 MVA.

#### SEA procedure for the 2010 Development Plan

On 2 October 2009, the preliminary stage of the Strategic Environmental Assessment procedure for the 2010 Development Plan (scoping) was initiated, pursuant to the Consolidated Environmental Law (Legislative Decree no. 4/2008), following publication of the 2010 Preliminary Report (PR) “on potential significant environmental impacts of Plan implementation”. The PR is intended to define the extent and level of detail of information to be included in the 2010 Environmental Report (ER). This preliminary stage will be completed once an opinion (and, where applicable, observations) is received from the Ministry for the Environment (METPS) - EIA-SEA Technical Commission, which gathers and collates observations made during the consultative phase, including comments issued by the Ministry for Cultural Heritage.

#### Status of authorisation applications

In 2009, pursuant to Law no. 239/04, 29 authorisation application procedures were initiated regarding NTG Development Plan development work. During 2009, 15 decrees received authorisation pursuant to Law no. 239/04 regarding Development Plan works.

#### Work carried out in the year

In 2010, the most important work involved activities to reduce network congestion, to connect new generating plants (especially those fuelled by renewable resources), and to increase the reliability of the grid with ever greater attention to environmental and safety issues. The following is a summary of the main sites on which work was performed in 2010:

- 500 kV d.c. “Sardinia-Continent” (SA.PE.I.) underwater cable: work was completed in 2008 on underwater cabling of the first pole (a total of 425 km). In 2009, civil engineering works were completed along with the construction of the buildings designed to hold the highly technological electrical equipment. Work had been completed by end 2010 on underwater cabling of the second pole (a total of 425 km).
- 380 kV stations to connect renewable-resource fuelled plants: in 2009, site work began on 380 kV stations suited to reducing congestion and connection to new renewable fuel generating plants located in the areas of Turano, Maida, Bisaccia, S. Severo, Deliceto, Troia and Brindisi South. During the first four months, work was completed in the stations of Turano and S. Severo; during the second four months, the first stage of the Brindisi South station was activated; during the last four months of 2010, works were completed in the stations of Maida and Bisaccia.
- 380 kV rationalisation in the province of Lodi: site work has begun with the construction of two new 380 kV power stations in the municipalities of Chignolo Po and Maleo; work has also begun on building a new 380 kV double three-phase power line connection along the “La Casella-Caorso” line;
- new 380 kV “SORGENTE – RIZZICONI” underwater connection: site work has begun and the civil works involved for the stations of Scilla (Calabria) and Sorgente (Sicily) are at an advanced stage; site work has begun and the site is being organised for the station of Villafranca (Sicily). Preparation of materials for the three 380 kV stations described above is

(8) ENTSO-E (European Network of Grid Operators for the Transmission of Electricity) is the body for strengthening cooperation between network operators at community level.

at an advanced stage. For Scilla in particular, electro-mechanical and electrical assembly has begun at the 380 kV power station of Rizziconi, where works are underway to expand and install the 2 bays necessary for building the new long-distance line. Final design is still in progress, in preparation for executing the manufacture and laying of the 380 kV double three-phase underwater and overland cable; in the second half of 2010, sites began in relation to the preliminary works prior to developing the Favazzina tunnel and the sites for the 380 kV power lines (overhead part) on the Calabria side. Studies have been performed using the real time simulator of the protection systems used in the grid.

- 380 kV “Ittiri-Codrongianos” long-distance line: at end 2010, the construction of the new 380 kV power line and the new Ittiri power station had been completed.
- 132 kV “Val d’Ossola” rationalisation: the works, which had begun in 2008, were completed during the last quarter of 2010. The development of the new line has allowed for the demolition of around 90 km of old power lines. Painted tubular pylons have been installed along this line to reduce environmental impact.
- 380 kV “Casellina-Tavarnuzze-S. Barbara” long-distance line: during the last quarter of 2010, the works envisaged for the 380 kV were completed. More specifically, the following parts have been completed:
  - the new 380 kV section of the Casellina power station, as were the new 380 kV “Casellina-Poggio a Caiano” and “Casellina-Calenzano” connections;
  - the new 380 kV “Tavarnuzze-Casellina” connection, including the assembly of a number of Foster pylons;
  - the new 380 kV connection at S.Barbara-Tavarnuzze with the first three-phase line of cables entering the station of Tavarnuzze (approx. 5 km).
- Replacement of conductors along the “Piossasco-Venaus-Villarodin” line: The first 2 stages of activity have been concluded for the replacement of conductors on the line.

## Energy overview

### Energy demand in Italy

In 2010, the demand for electricity amounted to 326,165 (\*) GWh, up by 5,897 GWh or +1.8% on 2009.

Comparison of the results for 2010 with the data for the prior year, leaving constant the number of days and the temperature, involves considering a number of factors. First of all, there is the variation in the calendar. 2010 had one more working day than 2009 (255 days vs. 254). Secondly, the climatic conditions were different: 2010 had a total of four summer months that were cooler than 2009 and winter months that were at the same temperature levels as 2009, apart from February, which was warmer. Therefore, adjusting for both number of days and temperature, the change in electricity demand came to +2.0%.

### ENERGY BALANCE IN ITALY

| GWh                 | Balance        |                | Change       | %          |
|---------------------|----------------|----------------|--------------|------------|
|                     | 2010 (*)       | 2009           |              |            |
| Net production      | 286,531        | 281,107        | 5,424        | 1.9        |
| Imports             | 45,761         | 47,070         | -1,309       | -2.8       |
| Exports             | 1,817          | 2,111          | -294         | -13.9      |
| Pumping             | 4,310          | 5,798          | -1,488       | -25.7      |
| <b>Total demand</b> | <b>326,165</b> | <b>320,268</b> | <b>5,897</b> | <b>1.8</b> |

(\*) Provisional figures as of 10 January 2011.

### Power generation

According to initial estimates, in 2010 net domestic power generation (see table below) increased by +1.9% year on year. Analysing the data for production, net of dispatching services, by the sources reveals a +1.1% rise in thermoelectric generation compared with 2009.

In 2010, hydroelectric production records a change of +0.6% on 2009, net of consumptions for auxiliary services.

Wind and photovoltaic generation once again rose dramatically compared with the previous year, posting a +39.3% overall rise compared with 2009, spurred by growth in wind assessed at around +29.1%, and +136.5% growth in photovoltaic energy compared with the preceding year.

Geothermal energy production, finally, was more or less stationary, at +0.3% on last year.

## DOMESTIC POWER GENERATION

| GWh                         | Production     |                | Change       |            |
|-----------------------------|----------------|----------------|--------------|------------|
|                             | 2010 (*)       | 2009           | Delta        | %          |
| Net hydro generation        | 53,169         | 52,843         | 326          | 0.6        |
| Net thermal generation      | 218,357        | 216,087        | 2,270        | 1.1        |
| Net geothermal generation   | 5,031          | 5,016          | 15           | 0.3        |
| Net wind generation         | 8,374          | 6,485          | 1,889        | 29.1       |
| Net photovoltaic generation | 1,600          | 676            | 924          | 136.5      |
| <b>Total net generation</b> | <b>286,531</b> | <b>281,107</b> | <b>5,424</b> | <b>1.9</b> |

(\*) Provisional figures as of 11 March 2011.

## Dispatching and trade

### Electricity business

Based on preliminary figures, Italian electricity demand for 2010 came to 326,165 GWh, a rise of 1.8% on the previous year (see table below).

During the year, 86.5% of the demand for electricity on the network was met by domestic power generation (86.0% in 2009), for a total of 282,221 GWh, net of consumption by dispatching services and pumping, for an increase of 2.5% on 2009. The remaining portion of demand (13.5%) was covered by imports, for a total of 43,944 GWh in 2010, compared with 44,959 GWh for the previous year (-2.3%). Export trade was calculated as the difference between energy received from supplies and that sold to foreign customers.

With regards to energy imported from abroad, a value of 45,761 GWh was recorded, showing a decline of 2.8% as compared with the 47,070 GWh of 2009. Exports, on the other hand, went from 2,111 GWh for 2009 to 1,817 GWh in 2010, showing a drop of 13.9%.

### ENERGY BALANCE IN ITALY

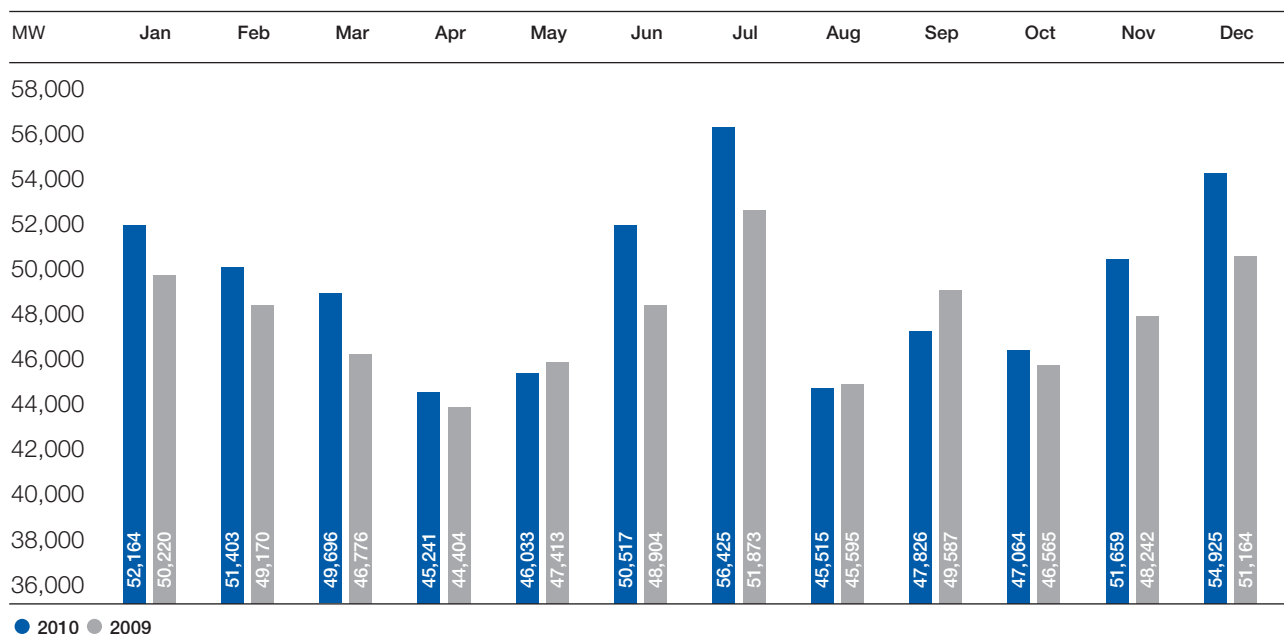
| GWh                           | Jan-Dec 2010 (*) | Jan-Dec 2009   | Change       | %          |
|-------------------------------|------------------|----------------|--------------|------------|
| Net production                | 286,531          | 281,107        | 5,424        | 1.9        |
| Imports                       | 45,761           | 47,070         | -1,309       | -2.8       |
| Exports                       | 1,817            | 2,111          | -294         | -13.9      |
| Pumping                       | 4,310            | 5,798          | -1,488       | -25.7      |
| <b>Total demand for Italy</b> | <b>326,165</b>   | <b>320,268</b> | <b>5,897</b> | <b>1.8</b> |

(\*) Provisional figures.

The trend of maximum demands in power terms per month for 2010 is shown in the figure below, compared with the respective data for 2009. We note that in 2010, monthly peak values remained for almost all months above those of the respective months the previous year, with significant growth points seen in the first and last quarters.

The highest level of demand for power registered at any time in 2010 was at midday on 16 July when demand reached 56,425 MW. The 2009 peak was at midday on 17 July when demand reached 51,873 MW. The highest load in 2010 was up 8.8% compared with the corresponding peak the preceding year.

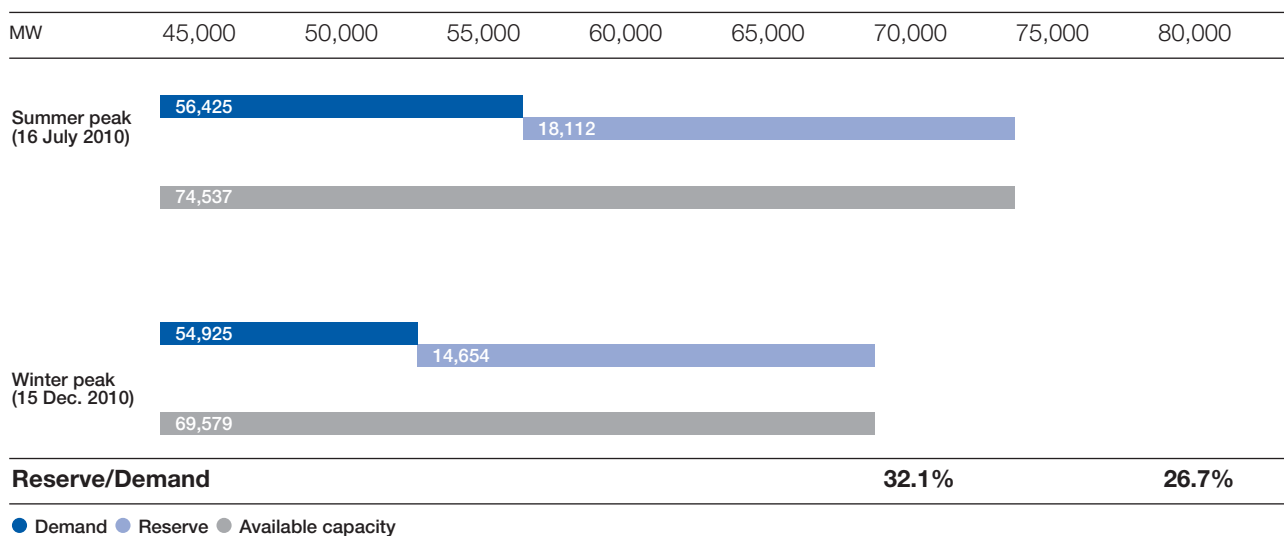
## MAXIMUM POWER DEMAND (MW)



## Coverage of demand

The high margins available at the peak recorded in 2010 are attributable to maintenance forecasting and coordination by Terna. The year also saw the start-up of a number of new generating plants.

## PEAK RESERVE MARGINS

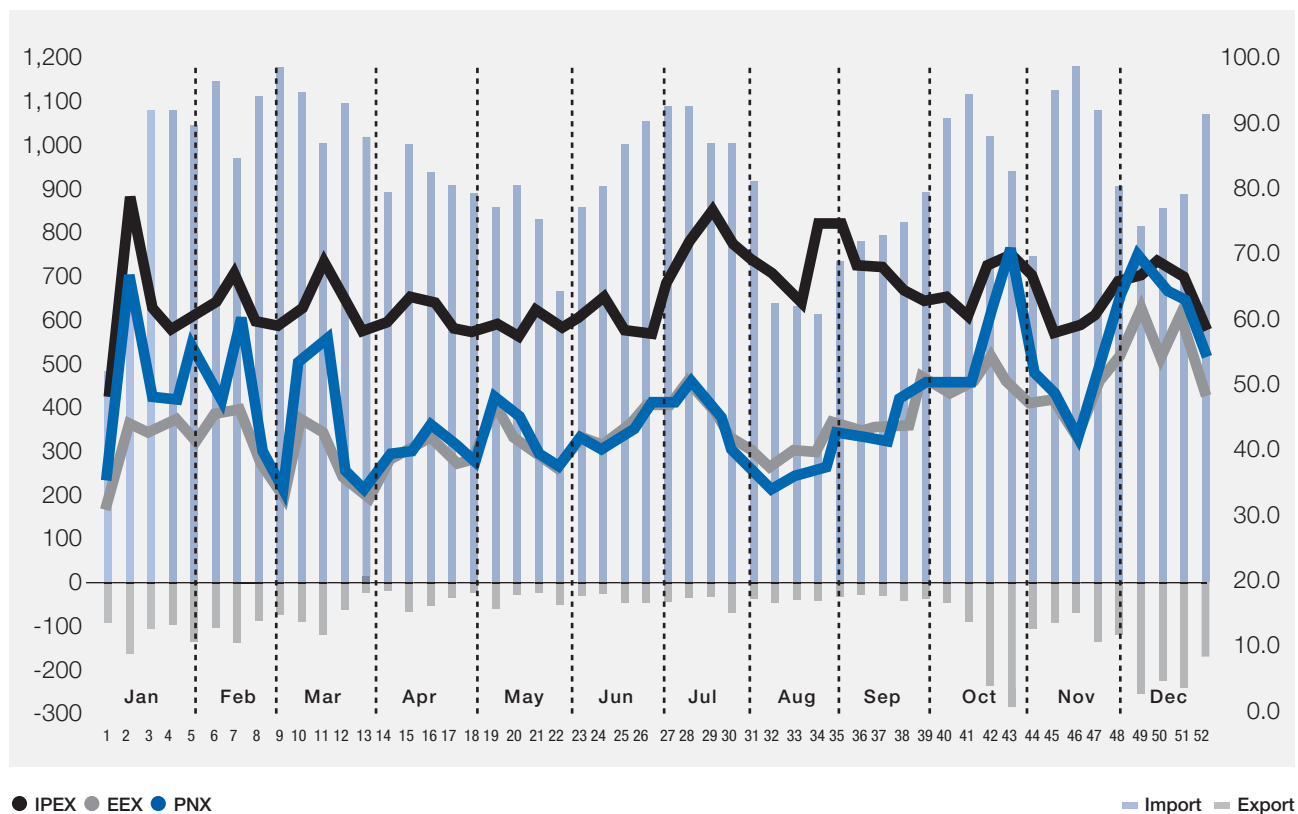


In Sicily, margins for covering demand were adjusted, also thanks to the use of the Termini Imerese 4 plant, for approximately 2,300 hours during the year. On this, we would recall that the production plant in question should be considered as generally not functional, and its availability for production can only be requested by Terna in relation to the forecast or occurrence of conditions risking the safety of the grid in Sicily. In Sardinia, an improvement was seen to margins in the periods of availability of SA.PE.I. connection, despite an accidental rate of production plants that was significantly greater than that recorded for mainland.

As concerns export trade, the difference in the average hourly price of the Italian power market and the French and German power markets recorded a value that was about 20% below that of last year (18 €/MWh vs. 23 €/MWh). This pricing



dynamic resulted in a decrease in the net balance of export trade as compared with the same period last year, for approximately 1.0 TWh less energy imported.



### Provisioning of dispatching resources

On 31 December 2009, the Ancillary Services Market reform came into force. This new reform innovates some aspects relating to the process and means for presenting bids by operators.

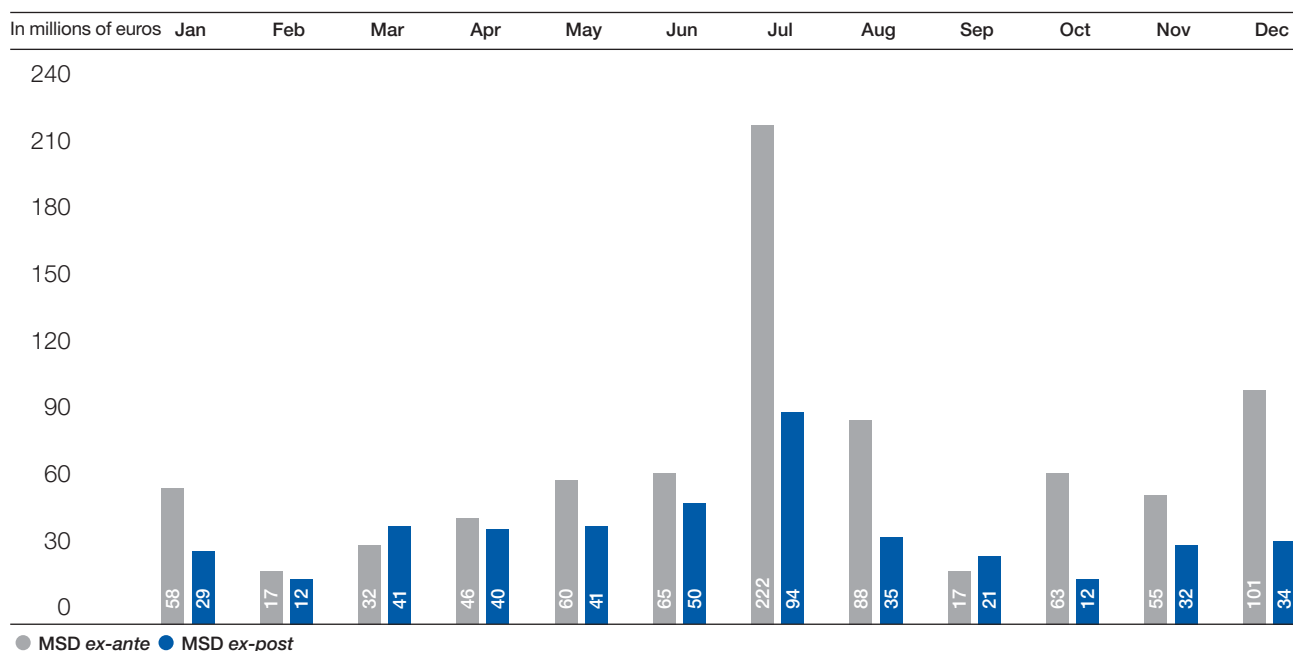
The most important new feature, however, is linked to the producer bid dynamic. In the past, operators could present 6 bids throughout the day (a purchase offer and a sales offer for each of the three time-bands into which the day was divided). These would apply both during the programming stage of the Ancillary Services Market and during the real time phase.

Two new features have been included in the new Ancillary Services Market:

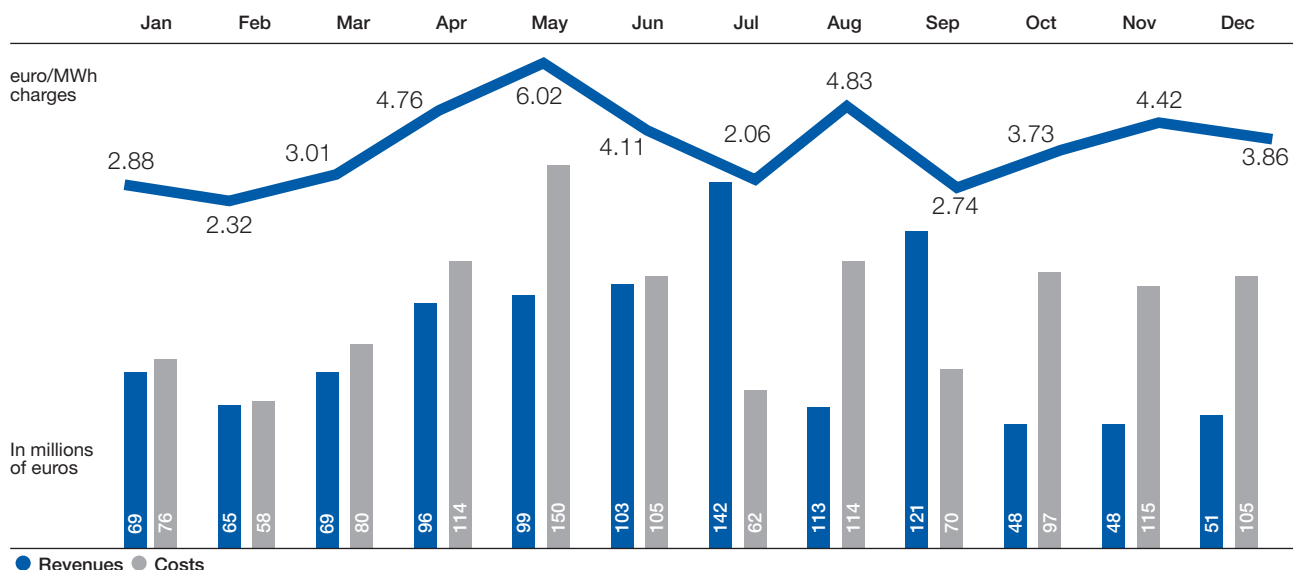
- a bid structure that is differentiated according to time, power steps (up to 3 steps in purchasing and 3 steps in selling with specific offers for switching off and the minimum production plant) and type of service (use of secondary reserve, provisioning and use of other dispatching services);
- an infra-day balancing market articulated into 5 sessions, in four of which operators can update their offers.

Operators thus enjoy greater flexibility in their bid strategies. In particular, the possibility of a better reflection of the cost incurred associated with the service.

Following the new Ancillary Services Market mechanism, during the scheduling phase, which is held on the day prior to that of the actual flow, Terna bought and sold energy respectively for about 7.0 TWh and 14.8 TWh (respectively 12.5 TWh and 14.8 TWh in 2009), corresponding to a net outlay of €823 million (€1,385 million in 2009, down 41%). Volumes bought and sold in relation to the balancing stage in real time came in respectively as 7.0 TWh (in the same period of 2009, equal to 7.8 TWh, -10%) and 8.1 TWh (in 2009 10.5 TWh, -22%), corresponding to a net expense of €440 million (in 2009, €429 million, +3%).



After the real-time phase, Terna verifies the proper execution of commercial obligations by the market participants, both in terms of generation and demand. To that end, the measurements at each point of input and withdrawal are taken, with the help of the distribution firms, and the differences from the schedules are calculated. These differences (imbalances) are measured using algorithms established by the regulatory framework. The net charge resulting from the measurement of these imbalances and of the buying and selling transactions executed by Terna on the Ancillary Services Markets are billed on a pro rata basis to each consumer with the uplift fee.



As established in AEEG Decisions 111/06 and 314/06, commencing from January 2007 this fee is determined by Terna during the first month of each quarter, based on the forecast charges and withdrawals for the quarter concerned. This calculation includes the differences between estimate and actual for the previous quarter, as well as the balance deriving from the settlement of the transport capacity usage fee (CCT), the hedges against volatility in the transport capacity usage fee, the transport capacity interconnection fee and the virtual importation service.



### Interruptibility service

By Resolution ARG/elt 201/09 of 30 December 2009, in accordance with articles 30, paragraphs 18 and 32, paragraphs 8 and 9, the AEEG defined the procedures for provisioning by Terna for 2010 of resources that can be immediately interrupted:

1. available following release of power that can be interrupted by parties financing interconnectors and by assignees of the instant withdrawal reduction service for the major islands (Legislative Decree no. 3 of 25 January 2010 converted with amendments into Law no. 41 of 22 March 2010);
2. concerned by temporary release for quantities in line with the average annual values forecast and not, therefore, associated with a termination of contract;
3. available by virtue of potential demands by Terna for an increase of interruptible resources, supplied overall to guarantee the safety of the system.

By virtue of this resolution, in March 2010, Terna assigned 552 MW instantly interruptible power, with validity from 1 March 2010 to 31 December 2010, against a total supply of 1,077 MW. The residual quantity, exclusively relating to shares forecast as the forecast average annual value of monthly temporary releases, has not been subsequently assigned.

Additionally, during the subsequent assignment procedures, the following were allocated:

- 18 MW for instant interruptible service in May 2010, for the period 1 October 2010 – 31 December 2010;
- 48 MW for instant interruptible service in September 2010, for the period 1 October 2010 - 31 December 2010.

The table attached shows the evolution of the power contracted throughout 2010 for the interruptible service, not considering the power made available for reassignment on a monthly basis, and partially reassigned.

|               | Interruptible<br>customers at<br>1 January 2010 | Interruptible<br>customers at<br>31 December 2010 | Power<br>assigned at<br>1 January 2010 | Power<br>assigned at<br>31 December 2010 |
|---------------|---|---|--|--|
| Instantaneous | 130   | 145   | 3,361                                  | 3,302                                    |
| Emergency     | 5   | 4   | 37                                     | 36                                       |
| <b>Total</b>  | <b>135</b>                                      | <b>153</b>  | <b>3,398</b>                           | <b>3,338</b>                             |

### Instant reduction service in withdrawals on the major islands

Law Decree no. 3 of 25 January 2010, converted with amendments into Law no. 41 of 22 March 2010 instituted the instant reduction service in withdrawals of electricity in order to guarantee the safety of supplies of electricity to the major islands for the three-year period 2010-2012. This service, which is only supplied to Sicily and Sardinia, aims to guarantee the possibility of reducing the electricity demand on said islands, with absolute availability, reliability and continuity.

By Resolution ARG/elt 15/10 (subsequently amended with Resolution ARG/elt 75/10), the AEEG defined the technical/commercial methods by which to assign and manage this service.

In February 2010, Terna defined the procedures for the assignment of 500 MW for Sicily and 500 MW for Sardinia for the period 1 March 2010 – 31 December 2012 and requests only came from Sardinia, for a total of 296 MW, from 4 parties.

Resolution ARG/elt 15/10 also provides for the quarterly reassignment of any residual quantities and, therefore, in May, August and November, a further total of 79 MW were assigned to Sardinia and 24 MW to Sicily, with effect as from 31 December 2012.

### Interconnectors and shippers

In implementation of the provisions of Law no. 99/2009 and Resolution ARG/elt 179/09, on which basis Terna selects the parties available for financing the interconnection infrastructures with abroad in the form of interconnectors and allows, as from 1 January 2010, for the use, by means of the assignment of the virtual import service ("shipping"), of the economic benefit deriving from the import of energy supplied from abroad, in December 2009, two selection procedures were organised, the first to select the parties to finance interconnectors and the second to identify shippers.

The interconnector procedure ended on 15 December 2009, with the assignment of 2,000 MW across the various borders:

- 500 MW France – 35 parties selected;
- 700 MW Switzerland – 24 parties selected;
- 500 MW Slovenia – 11 parties selected;
- 300 MW Austria – 4 parties selected.

The shipper selection procedure came to an end on 28 December 2009. This took place according to Resolution 179/09, whereby the Authority defined the measures and payments aiming to allow for the implementation of any provisioning contracts from abroad of electricity for the supply to withdrawal points of selected end clients, pursuant to article 32, paragraph 6 of Law 99/09. These measures provide for the introduction of a virtual import service to be carried out by one or more shippers, identified each year by Terna through auctions. The shippers thus identified commit to making a quantity of energy corresponding to that made available to them from abroad by the selected parties and, in any case, no greater

than that corresponding to the transport capacity pursuant to the appointment for programming and planning stipulated with Terna by said selected parties, available to the parties with interconnectors on the Italian market.

Subsequently, Decree Law 3 dated 25 January 2010, converted with modifications into Law 41 dated 22 March 2010, envisaged an extension up to 500 MW of the capacity to be assigned as an interconnector. Terna set the new interconnection capacity at 500 MW with reference to a project for connection with Austria. In April 2010, Terna commenced the procedures for assigning these blocks of financing, giving priority - as established in the above Decree - to those parties who make binding commitments to make available incremental resources, by 31 March 2011, for the instantaneous reduction of their drawings from the grid. Consequent to the publication of Resolution ARG/elt 65/10 and subsequent amendments, this procedure was concluded in January 2011, as a consequence of the assignment of the interruptible service for 2011-2013.

### **Service quality, unsupplied energy and other service issues**

Service quality in 2010 recorded decidedly positive figures for Regulated Energy Not Supplied (RENS) and the Number of Supply Failures per User (NSFU), falling below the averages seen in recent years: RENS of 1005 MWh vs. quality target of 1241 MWh and NSFU of 0.179 vs. quality target of 0.214.

In 2010, a major incident was recorded in the 150 kV grid in the area of Naples. The forest fires had a limited effect on the availability of the transmission system. This situation meant that low values of energy were not served, albeit slightly above the predefined target.

Critical issues generated by causes not attributable to Terna included storms, strong wind and, in some cases, significant snowfall in the areas of Turin, Naples and Palermo, which led to an increase in the number of supply failures per user, although performance on a national level was above the predefined target.

No gas and water availability-related critical issues were recorded.

Although in line with the positive service quality generally, the larger islands continued to face their particular challenges connected with the structure of the transmission system.

In conclusion, the following are the four key indices of service quality and performance for Terna's NTG systems, which are calculated in accordance with Resolution no. 250/04 of the Authority for Electricity and Gas and Terna's Grid Code and which all show positive results:

- AIT (Average Interrupt Time attributable to Terna) = 0.99 min/period; Annual national target = 1.00 min/year;
- SAIFI + MAIFI (System and Momentary Average Interruption Frequency indexes per user directly connected to the Terna NTG, attributable to Terna) = 0.15; Annual national target = 0.22;
- ENS (Energy Not Supplied attributable to Terna) = 613 MWh; Annual national target = 550 MWh;
- ASA (Average System Availability of Terna network elements) = 99.225%; Annual national target = 99.05%.

## **Terna and the photovoltaic energy**

In order to use and safeguard as best possible its resources and maximise the profitability of its assets, in 2009 Terna embarked on the "Photovoltaic project". This entailed the construction and management of small photovoltaic generation plants in the areas of the owned power stations which are currently free from plants and not used.

With this aim in mind, Terna has incorporated the company SunTergid. This corporate organisation both meets the needs of functional and accounting separation of the Parent and ensures compatibility with the bylaws and the concession of Terna S.p.A., as well as with the provisions of Legislative Decree no. 79/99 (i.e. the "Bersani Decree").

On 23 December 2009, under the scope of an internal reorganisation process looking to optimise resources and potential for the new production from photovoltaic source, SunTergid incorporated the new company Rete Rinnovabile S.r.l., also referred to as "RTR S.r.l.", with share capital of e 50,000.00, which has been identified as a special purpose entity into which all projects that became operative in 2010 and the early months of 2011 have been transferred.

On 18 October 2010 Terna, SunTergid and Terra Firma Investments (GP) 3 Limited (wholly-owned by Terra Firma Capital Partners III, L.P.) undersigned a preliminary agreement to transfer 100% of the share capital of Rete Rinnovabile S.r.l. The compensation for the operation was agreed in a modular fashion (in terms of enterprise value) on the basis of the plants which, on the closing date (31 March 2011), alternatively benefited from the incentives of the 2010 Energy Account or the Energy Account of the first quarter of 2011.

After the Rete Rinnovabile transaction, which saw the creation, development and sale of more than 140 MWp in such a short space of time, the photovoltaic project continues to be a priority for Terna, which is committed to developing a second tranche of projects in 2011, through the subsidiary Nuova Rete Solare.

# Risks, organisation and corporate social responsibility

## Risks and uncertainties to which Terna and the Group are exposed

Terna has always paid careful attention to the prevention of risks of all natures that could affect or limit the company's results. This paragraph aims to provide a clearer, more complete representation of these, by summarising the risks and uncertainties to which the company is exposed, as indeed known to the market and shareholders, considering their exposure in the financial statements and informative prospectuses published in the past.

### Regulatory risk

About 96% of the Group's consolidated revenue comes from annual fees paid for the provision of services regulated by the Italian Energy Authority. Within the scope of such regulations, there are a number of variables that could have an impact on performance.

### Volume effect

The revenue of Terna and TELAT attributable to the operation, functioning and development of the NTG, and to the management of dispatching activities, is regulated by tariffs set by the AEEG. The unit tariffs are applied to the overall volume of energy transmitted using the NTG. These volumes depend on factors that are beyond the control of the Group.

In view of the current economic conditions and the consequent contraction in electricity consumption, and to protect transmission revenue from marked volatility, Resolution no. ARG/elt 188/08 adopted by the AEEG has established a revenue guarantee mechanism that limits within a range of +/- 0.5% the effect of annual changes in the volume of energy transmitted. Resolution no. ARG/elt 204/09 also confirmed the use of this mechanism for the DIS component.

As from 2009, Terna has opted to adopt the mechanism that shall remain effective for the whole of this regulatory period (until end 2011).

In 2011, the rules for the new regulatory period (2012-2015) will be discussed with the Authority. At this point, Terna will suggest a regulation to the Authority, which, in view of the experience of these last three years, can ensure a tariff revenue in line with the costs recognised.

### Bonuses and penalties

At present, various different bonus and penalty calculation mechanisms are provided for, on the quality of transmission service and on dispatching.

More specifically, in relation to the incentives mechanism linked to the reduction of quantities supplied for services to the Ancillary Services Market, we note that by Resolution ARG/elt 213/09, a bonus/penalty system has been introduced that is applicable for 2010-2012. By this measure, the Authority intends to continue encouraging Terna to increase the efficiency of its provisions of the resources required to ensure a safe management of the system, using incentive schemes that span several years. The mechanism entails a unitary incentive of € 11/MWh for 2010, set to decrease for subsequent years (respectively € 7 and € 3.5/MWh).

In view of the three-year duration of the incentives mechanism, against a service that allowed it to reach incentive targets totalling about € 160 ml in 2010, Terna has recognised revenue of € 77 million, as the measurement of the related fair value, considering the risks mainly linked to the trend of the electrical market and regulations.

### Domestic legislative risk

#### Laws on environmental protection

The activities of the Group are conditioned by the Italian and European environmental legislation governing electromagnetic fields. The Group may incur additional costs to implement environmental regulations requiring preventive measures to be taken or reparations to be made. At present, the government is working, with the involvement of operators including Terna, on the definition of the relevant regulations established by current legislation.

#### Laws on employment

More onerous regulations governing health and safety in the workplace might have an adverse effect on the economic/financial performance of the Group. At this time, no significant new measures are expected from the competent Institutions that might have a significant impact.



### **Laws on the consolidated energy market**

The implementation in Italy of the Community directive on the matter of the consolidated electricity market 2009/72, on which the government is currently working with the preparation of the related implementation Decree, envisages the adoption of provisions of interest with reference to the separation of production and import, transmission, distribution and sales of electricity.

### **Operational risks: risks connected with NTG malfunction**

The Terna Group's operations are exposed to the risk of unexpected service interruptions caused by external events that are beyond Terna's control, such as accidents, defects or breakdowns involving control systems or other equipment, deteriorating plant performance, natural disasters, terrorist attacks and other extraordinary events of this kind. Repairs to the sections of the NTG owned by the Group and any claims for compensation by third parties as a result of such events could, in principle, give rise to charges if the Group is found to be responsible. Specific insurance cover has been arranged to mitigate the effect of operational risks.

### **Litigation risk: legal disputes**

The Terna Group is involved, as both claimant and respondent, in a number of legal proceedings involving contracts, employees, the environment, regulatory matters, and public safety issues arising from normal business operations. In addition, the Group may be involved in new litigation and/or out-of-court disputes raised by interested/entitled parties of various types (by mere and incomplete way of example: suppliers, public bodies etc.). See the section "Commitments and risks" of the notes to the separate financial statements of Terna and the consolidated financial statements of the Group for more information.

### **Market and financial risks**

In the conduct of its operations, the Group is exposed to various financial risks: market risk (interest-rate risk and inflation risk), liquidity risk and credit risk.

As part of the policies approved by the Board of Directors, the Terna Group has defined responsibilities and operational procedures for the management of financial risk, making specific reference to the tools considered acceptable and setting clear operating limits for their use.

The risk management policies adopted by Terna seek to identify, analyse and monitor the risks to which the Company is exposed, establishing appropriate limits and controls, and checking compliance with such limits. These policies and related systems are reviewed on a regular basis in order to reflect any changes in market conditions and the activities of the Group. For more information, see the section "Risk management - Terna S.p.A." in Section "A. Accounting policies" of the notes to the 2010 financial statements.

### **Risks connected with financing needs**

Even in current market conditions, the Group expects to maintain sufficient capacity to generate financial resources from its operating activities. Implementation of the investment plan is however expected to result in greater borrowing. Although the Group continues to enjoy the support of its banking partners for the financing of its debt, it may become necessary to arrange additional loans that, under less favourable market conditions, could result in an increase in financial expense.

## **Security**

Terna has always tackled the vulnerabilities of the electrical system and critical infrastructure by applying the latest solutions and a high level of technical and organisational skill, which are reflected in the internal processes and systems, as well as in the procedures and instructions applicable to all operators participating in Italy's national electrical system.

In order to meet the increasing need for security, Terna set itself the goal of significantly enhancing the organisation's security mechanisms and defining a broad-based system for identifying, analysing and monitoring Company risks.

In particular, security efforts are aimed at protecting the Company's physical and technological infrastructures, in part through efforts aimed at preventing and handling corporate fraud. For the real-time monitoring and management of critical issues affecting key infrastructure, Terna has created a Security Operations Centre (SOC) that is able to tackle and manage critical situations.

Terna's security unit adopts the latest best practices in the areas of critical infrastructure protection and security, which are also in line with the current regulatory framework recently introduced in Europe.

### **Security Operations Centre (SOC)**

In 2010, the number of operative company sites monitored for break-ins and by video-surveillance systems increased significantly, thus now covering most of the most sensitive sites as specified in the agreement with the Ministry of Interior. In addition to these, we also have the areas involved by sites, which are monitored by systems that can be relocated.

In particular, jointly with the Carabinieri Police Force, the portal "Terna – Control Centre Carabinieri" has been developed to allow for the complete integration of the Terna Control Centre and that of the Carabinieri.

Through this portal, information, images and videos can be exchanged in real time between the control room and the Carabinieri patrols, equipped with "EVA" devices, sending the records from the monitoring room of the control centre, or the data collected on field by the patrols, thereby allowing for a rapid exchange of information in the event of a break-in. A similar integration has been started-up with the operative rooms of the National Police Force.

With regards to the monitoring of information security, in 2010 company ICT resources were integrated (servers, management platforms, etc.) onto the Security Information and Event Management system devoted to monitoring and relating security events on ICT resources.

The office of company Registration Authority was also established, through which security services are supplied such as the issue of electronic signature digital certificates via the company platform, digital signature services and certified e-mail, with the use of systems external to the company (Infocert) in addition to services managing applicative qualifications.

These services are in addition to the now consolidated monitoring of spam and viruses on company resources.

## **Risk Management**

### **Electricity market risk management**

With its Resolution no. 115/08 ("TIMM") regarding the monitoring of the Wholesale Energy and Ancillary Services Markets, the Authority for Electricity and Gas defined the general principles and criteria of market monitoring for the companies Terna, GME and GSE, calling for each of these companies to establish a specific monitoring office.

Electricity Market Risk Management is Terna's monitoring unit, which is responsible for the TIMM data warehouse and sees to the acquisition, organisation and storage of data in order to monitor the volumes and indicators related to the Ancillary Services Market.

The activity in question is particularly important under the scope of the Terna incentives scheme envisaged by Authority Resolution no. 213/09 in relation to the provisioning of resources for the dispatching service.

In order to analyse the main risks relating to the electricity market in 2010 the SIMM (Security Index Market Monitor) was started-up. This is a managerial "dashboard" devoted to monitoring the electricity market.

A dynamic graph included represents the key performance indicators (KPIs) that allow us to have an overview of the high level of the trend of the electricity market and to readily identify any differences from the threshold limits established in order to analyse potential critical issues and risks.

### **Electricity system risk management**

Terna is responsible for coordinating the functioning of the entire electrical system, although the Company only directly manages the part that concerns the transmission grid. As such, the correct function of the plants connected must be protected by conduct outside the scope and management of Terna, which can represent an additional threat. This is a component of operational risk that must be monitored and for which mitigating actions must be taken, actions which generally work towards limiting external events, such as malfunctions or failures to comply with the Grid Code. At times, systems with certain innovative characteristics, such as wind and photovoltaic farms, or other events that have not been foreseen require analyses and studies that may lead to changes or additions to said Code.

## **Fraud Management**

In 2010, the Fraud Management Unit continued with its prevention of company fraud, taking all actions needed to discourage its occurrence. Under this scope, the company proceeded to implement specific procedures for certain critical processes. These aim to define the criteria and means by which to ensure management at maximum efficiency and effective prevention of unlawful conduct. The Operative Instruction defining the flows of information needed to implement the Memorandum of Understanding signed with the General Command of the Tax Police force in 2009 is particularly important, for the prevention of the risk of crime and the development of the related computer portal to allow the Tax Police access to the relevant information, in order to guarantee the timeliness, confidentiality, traceability and integrity of data.

Together with the activities involved in preventing crime, the Fraud Management Unit also carried out:

- activities to support the Company's other units, such as in the analysis and assessment of counterparties, so as to limit the risks deriving from transactions with others;
- compliance activities focusing on cooperating with and supporting the Company's management and its various offices, aimed at ensuring compliance with laws, regulations, procedures, codes of conduct, and best practices, as well as at reducing and/or preventing the risk of sanctions and safeguarding the Company's image.

### **Organisational Model under Legislative Decree no. 231 of 8 June 2001**

The Company Security Department, in collaboration with the Legal and Corporate Affairs Department, is engaged in implementing and updating the Organisational Model under Legislative Decree no. 231/01.

For more details on the content and changes made in 2010, please refer to the Corporate Governance Report published with the 2010 Annual report.

In order to disclose and ensure the effective implementation of the principles and rules established in the model, in 2010 a capillary, differentiated training campaign was organised at all transmission areas.

### **Control of Management Systems**

In 2010, through an audit by the Certifying Body (IMQ), Terna obtained certifications UNI EN ISO 9001:2008, UNI EN ISO 14001:2004 and BS OHSAS 18001:2007.

The method of environmental data collection and analysis has been improved and the first stage of the "Context analysis and identification of stimuli to encouraging safe conduct in the workplace" has been completed, aiming to improve the safety culture within the company, mainly in the operative structures of the Parent.

### **Physical Security**

Terna has established new surveillance and protection systems that are in line with their importance to the functioning of the electrical system and suited to the number and type of actual or potential threats they are designed to face.

With this goal, and for the first time in Italy, Terna has adopted risk assessment methodology for each of the stations concerned in order to analyse the related physical risk – concerning both actual and potential attacks – and electrical risk.

Based on the "role" that each system plays in the functioning of the national electrical system, determined by assigning a risk index to each station based on their respective critical importance, a long-term action plan has been developed.

In 2010, the programme that had been started-up in 2009 was continued, aiming to protect the entire electrical asset, comprising more than 400 stations, by means of the use of technology calibrated on the real electrical and environmental risk. During the year, a further 20 anti break-in systems were developed.

### **Information Security**

In 2010, the multi-year programme continued aiming to gradually "improve the security of data and company systems" and, in a parallel fashion, the constant, ongoing compliance with applicable regulatory framework obligations and requirements.

The main initiatives concerned on the one hand, the consolidation of the governance model for information security, with new specific policies and supporting tools for the design of secure applications, and on the other hand an increase in the diffused culture on the matter at all company levels, through a multi-level training plan focussing specifically on increasing sensitivity and awareness. Additionally, technical initiatives have also been launched towards the computer structures, in order to facilitate the guided introduction of tools and methods established in the company for the analysis and treatment of the risk to the computer assets.

In 2010, the matter of security checks and audits on the operating platform gained ground through various Information Security Assessments of important ICT infrastructures and systems with the multiple objective of measuring potential risk level, verifying compliance with the model established in Terna and launching any action plans (compliance plans) aimed at eliminating the vulnerabilities detected.

Thanks to the programme contents and the preparation of new technological and organisational tools by which to assess safety level, the level of application of the governance model has grown, at the same time also causing the level of protection to rise for data and company technological infrastructures against the most common physical and "cyberspace" threats.

The same programme also guaranteed, as indeed had been forecast, a timely compliance of the company with the applicable, and constantly evolving, regulatory framework, according to the importance that the asset of "data" is now acquiring in the business processes of companies and other organisations of high technological content.

Finally, under the scope of the initiatives aiming to improve security processes, in the second half of 2010 the path began towards certification to standard ISO/IEC 27001:2005 in relation to a specific information technology environment of Terna. This is represented by the TIMM (Market Monitoring Integrated Text) applications and has the aim of achieving this certification in 2011. This decision has been shared with the AEEG and aims to make Terna even more efficient in terms of the governance of data security and to improve trust between the company and its stakeholders.

Certification of the compliance of Terna with the stated standard ISO/IEC, and, therefore with the criteria of the standard for a Information Security Management System (ISMS), albeit applied to a limited business case, allows for the achievement of high standards of management/organisation, that go well beyond the technical/operative standard of the computer and technological aspects.



## Corporate social responsibility

One of Terna's defining characteristics is the adoption of a sustainability-led approach which has been integrated into its business policies, processes and management systems. The goal of this approach is to generate value from and enhance the asset base of management best practice, and to assist in drafting the Company's ethical, environmental and social policies and objectives. The Parent publishes its results in this field in an annual sustainability report, which is available for viewing on the corporate website at [www.terna.it](http://www.terna.it).

Terna's commitment to corporate social responsibility won the Company a number of awards in 2010 from specialised non-financial performance (environmental, social and governance) rating agencies. In November 2010, Terna was confirmed as part of the Dow Jones Sustainability World Index, on which the world's 300 top performing companies in sustainability are listed (of which just 12 are Italian enterprises). Additionally, again in November, Terna was included in the Dow Jones Sustainability Index Europe and in the new FTSE ECPI Italia SRI indexes, the first sustainability indexes consisting of only companies listed on the Italian Stock Exchange: Terna is present both in the Benchmark index and the Leaders index.

Terna's approach to corporate social responsibility embraces a number of key areas:

### Electrical service

Terna has taken to heart the goals defined in the concession agreement and assumes responsibility towards the public at large. The Company pledges to constantly ensure the security, quality and cost-effectiveness of electricity transmission over time, and to provide equal access conditions to all network users. Terna furthermore pledges to maintain the transmission system's efficiency and to upgrade it as a corporate asset that is also a key infrastructure for society.

### Environment

The most evident sign of Terna's operations is the physical, visible presence of power lines and stations across the country. To minimise this, Terna has developed a management system for monitoring and limiting the environmental impact of its operations. The Company has placed special emphasis on transmission infrastructure development activities. In this field, Terna has chosen to work with local institutions and harness Strategic Environmental Assessments (SEAs) to take environmental requirements into account right from the earliest stage of new line planning.

This makes it possible to identify optimal solutions that combine the needs of developing the electricity grid with the need for protecting the environment and local cultural heritage.

In 2010, Terna continued with many **initiatives for reducing the environmental impact** of its plants. In particular:

- it celebrated the International Year of Biodiversity, implementing interventions of environmental restoration, mitigation and offsetting in the two WWF oases of Tuscany of Padule-Orti Bottagone (LI) and Stagni di Focognano (FI), and in the Sicily oasis of Torre Salsa (AG), envisaged by the three-year agreement signed with WWF Italy in January 2009. In December 2010, a new Terna-WWF convention was signed for the development of the first Action Plan for the Sustainability of the Development of the National Transmission Grid in the areas of high environmental value within the national park of Pollino (Region of Calabria and Region of Basilicata) and the National Park of Gran Sasso - Laga (Region of Abruzzo).
- In November 2010, the first single-shaft tubular pylons were assembled for the new Chignolo Po-Maleo 380 kV power line in the provinces of Lodi and Pavia. The tubular supports are an important innovation in the development of high and very high voltage lines. The compact structure guarantees that minimum dimensions are required and provides a valid alternative, in given landscape conditions, to conventional pyramid-truncated supports. The prevalent use on the new line of single-shaft pylons in lieu of the traditional pyramid-truncated versions reduces the area of the territory taken up by the lines 5 times and the area covered on the ground by the supports, going from 250 to 50 m<sup>2</sup>.
- Terna's attention to CO<sub>2</sub> emissions continues. According to the "Carbon Disclosure Project - Italy Report 2010", prepared on the basis of a survey carried out amongst the top 60 Italian companies in terms of Stock Exchange capitalisation, Terna came in second place in the classification of the Italian businesses most aware and involved in climate change and most transparent in communicating the measurement of its emissions, thereby entering the Italian Carbon Disclosure Leadership Index. Terna's performance is even more significant, as it is not an electricity production company and therefore adopts containment policies on an entirely voluntary basis.

### Social Responsibility: human and community resources

Terna's highly specialised and often unique technical skills in the electricity industry allow the Company to operate with complete professional excellence. Terna's attentiveness to keeping this skill current is a key component of how Terna manages its human resources. Equally important is the Company's focus to workplace safety, in view of the risks associated with many of the Company's operations, such as, for example, working on live power lines.

The corporate responsibility of Terna extends to the social context through the definition and implementation of initiatives of solidarity and support to the development of the civil society. In 2010, the technical skills of Terna staff were put to the service of a sustainable development project to the benefit of an Andes community in Bolivia. The initiative, which started from the commitment as volunteers by some employees, concerned the design and development of a 37 km power line.

The most significant initiatives include the Terna Prize for contemporary art, which reached its third edition in 2010. The Prize objective falls under the scope of a Memorandum of Understanding signed with the Ministry for cultural heritage and assets, and takes the form of the creation of a new virtuous relationship between companies, the world of art and institutions, through an interconnection that optimises the production of Italian artists on the art market.

Detailed information on Terna's environmental and social impact can be found in the Sustainability Report that Terna has published every year since 2005 following the adoption of its annual financial statements. To provide increasingly full and complete disclosure of Corporate Governance-related achievements, below is a preview of key environmental and workforce indicators:

- no fatal accidents were recorded in the workplace, nor were there any fatal or serious accidents in previous years for which the Company's liability was ascertained in a final ruling during the year;
- no allegations were recorded regarding workplace bullying or work-related illness – regarding current or former employees – for which Terna was held liable in a final ruling;
- no cases of environmental damage were registered for which Terna was held culpable in a final ruling;
- no final penalties or sanctions were levied against the Parent for environmental damage.

Terna is not subject to the greenhouse gas reduction obligations arising out of the Kyoto Protocol, nor is it a participant in emissions trading schemes.

## Information Technology

Significant benefits were achieved in 2010 as a result of information and communication technology projects and innovation at Terna. The following objectives were achieved:

1. Benefits for the business deriving from the completion of important initiatives;
2. Enhancement of the telecommunications infrastructure as a key asset for National Transmission Grid management.

### 1. Benefits for business deriving from the completion of important initiatives

- **Enhancement of National Electricity System security** – National Electricity System security was enhanced through a series of interventions to improve the effectiveness of the control and operation system as regards the observed grid perimeter (extended to around 2,000 distribution stations) and real-time output plants (with more than 3,000 MW added).

Defence system effectiveness was also improved through the extension of disconnectable loads to distribution stations through the new emergency control panel (ECP) system, and extension of monitoring to additional events at hubs limited to the Calabro ring and the northeast-northwest backbone.

- **Dispatching incentives** – Following AEEG Resolution no. 206/08, which encouraged Terna to reduce the volume of energy procured on the Ancillary Services Market, significant work was undertaken to improve IT support instruments used for real-time planning and dispatch operations. Specific tools have been consolidated for the optimised use of strategic storage and Optimal Power Flow tools in the process of the tertiary regulation of production plants. Additionally, NTC (Net Transfer Capacity) for 2010 has been redefined in order to improve the management of the interconnection, with specific reference to low load periods, and the basis for regulation services has been extended.
- **Regulatory adjustments** – The application platform supporting the Ancillary Services Market, both during the programming stage and in real time, has been reviewed following Resolution ARG/elt 211/10. On 31 December 2010, the computer systems were adjusted at the time of instituting the new intra-day markets both of energy and dispatching services. The adaptation of the systems, giving rise to an Authority obligation, has made the new market rules operative, allowing operators to adjust their input programme and Terna to refine programming of services delivered at several stages throughout the flow day.



The application platform for market settlement has been reviewed following said resolution. The systems going towards invoicing the amounts of the Ancillary Services Market have been adapted in time for the first invoicing of the new market structure. Finally, the issue during the period of the GAUDI system is worthy of note: a consolidated record of plants in production of all sizes and on all voltage levels. As per the Authority guidelines, the system represents the consolidated record of the production system, allowing for its services to be supplied to the benefit of all sector operators.

## 2. Enhancement of the telecommunications infrastructure as a key asset for National Transmission Grid management

- **TLC infrastructure** – In 2010, the optic fibre telecommunications grid infrastructure services owned by Terna have been consolidated. The services activated relate to the control and operation system and the video-surveillance of the power stations.

The migration of the Defence Systems grid to the new owned infrastructure has also been completed, with significant benefits in terms of reliability and performance.

- **Perimeter security** – The efficiency of the firewall security systems has been further improved, thanks to the completion of the installation of the firewall systems at the power stations. The redundancy of intrusion prevention tools on the management grid for the identification of potentially dangerous traffic.

### Managerial information technology and services to people

In 2010, the technologies at the calculation rooms of the 8 territorial operative areas of the Parent, now obsolete, were consolidated and renewed. Again with a view to renewal, the new calculation room was created at the Pero (MI) Terna office, technology was introduced to monitor the technological infrastructures with a view to guaranteeing continued availability of the services supplied and there was proactive identification of failures to infrastructures.

## Research and Development

The Parent's research and development activities were focused on developing environmental monitoring and control technologies, enhancing the efficiency and reliability of plant, maximising service quality and optimising the management of corporate processes.

A group of experts is constantly studying the technological innovations to be used to improve Terna's core processes. The team is able to make use of specialised information systems (MBI etc.) for the close monitoring of equipment.

A number of activities were identified and implemented in 2010. The main activities, some of which are still at the implementation stage, are described briefly below:

- anti-deflagration terminals; new cable terminals are available, equipped with anti-deflagration systems;
- single-shaft supports for 380 kV lines: the feasibility study has been performed for single-shaft supports with high mechanical performance;
- emergency supports: quick-installation supports have been made available for maintenance for 150 and 220 kV;
- high Transport Capacity conductors: the following have been completed:
  - the installation of a new type of conductor featuring high thermal limit and reduced length; the experience of the INVAR-ZTAL conductors has been consolidated;
  - the study of further solutions using supports in ceramic or carbon, featuring high electrical and mechanical performance, particularly suitable for redoing power lines without replacing pylons.
- International "Pylons of the Future" contest: the preliminary studies have been started for the engineering of the winning supports;
- automation of Bolano-Paradiso stations: a study is currently underway looking to ensure the automatic replacement of cables relating to the interconnection of Sicily and Calabria in the stations of Bolano and Paradiso, which will allow for significant reductions in the time required for replacing cables, where necessary;
- extremely reliable current transformers (HV): the installation has begun of the new HV characterised by high hermetic seal performance (low gas loss), silicon insulation (rather than ceramic), high resistance of the internal arch to extremely high external temperatures and an overcharge of 150%;
- new transportable SCRI 150 kV stations: a new type of station has been designed (the first started-up in December 2010), which can be transported by road and is quick to install. It consists of three bays on a line with a single-bar execution and can be used to connect "in-out" production plants on a 150 kV line;
- containment of SF6 emissions: initiatives are underway to reduce the emissions of SF6, such as the recording and computerised management of the use of SF6 gas, specification of new "low loss" equipment and experiments on the recovery of gas from plants to be disposed of;
- on-line monitoring system of HV equipment: in the Lacchiarella power plant, the on-line monitoring system of HV equipment has been activated, with data transmission to the PSE platform and MBI remote maintenance centre;

- direct current plants: an investigation has been performed on the state of the art and specification on dielectric extruded electrical cables for cable systems HVDC 320 kV isolated in XLPE for overland applications and on VSC conversion systems;
- specific technical update of autotransformers, with study for the specification of new machine 400 MVA 400 kV/155 kV, safety prescriptions (rise systems, flange holding systems) and technological update (resin polymer pass-throughs, dissolved gas sensors sensitive to 3 gases);
- study for the design and operation of PSTs (Phase Shifting Transformers): the following have been implemented:
  - the review of the PST project of Camporosso, Foggia and Villanova;
  - the study of transistors during installation of the PSTs in Foggia and the use of the by-pass;
  - the specifications for the test and protection system by means of RTDS.
- Study of possible solutions by which to optimise the design and construction of new power plants, aiming to seek compact installation solutions (reactors with toroidal neutral HV, combined equipment) and the identification of new civil design standardisation criteria;
- specification of HV/LV power transformers to power the power plants directly from the NTG.

These activities have been pursued using internal resources. The staff also operate in working groups, a method that facilitates the spread of knowledge to all branches of the Company. Terna also draws on the specialist support of developers, universities, the associate CESI S.p.A., and, where necessary, its main suppliers, which are also interested in the development of new technologies and operate under the supervision of project managers from within the Company. In particular, in 2010 the Terna Group incurred costs totalling € 22.5 million towards the associate CESI, of which € 19.9 million capitalised (of this latter amount, € 0.5 million relating to the subsidiary RTR).

The accounting treatment of Research and Development expenses is discussed in the "Intangible assets" paragraph of section "A. Accounting policies" of the notes to the financial statements of Terna S.p.A. at 31 December 2010.

## Human Resources and Organisation

### Organisational structure

There were no changes to the macrostructure of the business during 2010. However, we would point out the strengthening of ICT monitoring under the scope of corporate security management, through the move of the departments 'Managerial Information Technology and Services to People' and 'Telecommunications' under the scope of said management.

### Human resources

Changes in the number of Parent employees are shown below. It is pointed out that as of 31 December 2010, the subsidiaries TELAT, SunTergrid and RTS and the companies held for sale (RTR and Valmontone Energia), had no employees.

| CHANGE IN THE WORKFORCE | Terna        |              |           |
|-------------------------|--------------|--------------|-----------|
|                         | 31 Dec. 2010 | 31 Dec. 2009 | Change    |
| Senior management       | 59           | 65           | -6        |
| Junior management       | 502          | 488          | 14        |
| Office staff            | 1,890        | 1,874        | 16        |
| Blue-collar workers     | 1,017        | 1,020        | -3        |
| <b>Total</b>            | <b>3,468</b> | <b>3,447</b> | <b>21</b> |

The above figures do not include terminations with effect from 31 December.

### Resource development

Resource development activities carried out in 2010 were organised into two important sectors: performance management and professional development.

The Global Performance System, introduced in 2009, in 2010 saw the first complete closure of an assessment cycle, broken-down into: a) assignment of 2009 objectives, b) assessment of performance and Terna organisational conduct, c) feedback by managers. In 2010, a new performance management cycle began with the assignment and communication of new objectives. In order to include new population targets, the number of participants involved in the process was gradually increased, now amounting to approximately 700.

With regards to professional development, in 2010, with the support of an external executive search company, an assessment process began in operations management, with the aim of training the resources in view of the generational takeover that will involve Terna in the years to come.

### Management incentive plans

Short-term management incentive schemes include an MBO plan for 2010 targeted at senior and middle management, related to the achievement of individual, department and company performance objectives.

As concerns long-term management incentives, the 2006 Stock Option Plan is still in place, the deferral of which to 31 March 2013 was resolved in 2009. We note that during the period, a total of 3,486,900 options were exercised and that as of 31 December 2010, a total of 5,596,300 options can be exercised.

Long-term cash-based managerial incentives are available to top managers and key people under the cash-based three-year Long Time Incentive (LTI) Plan, the purpose of which is to generate value and achieve the challenging performance targets set.

### Training

2010 saw the completion of the two-year training plan that had begun in 2009. This was the first training plan to be launched after the creation of the “Grid Campus Experience”, the umbrella under which all company training of 2008 was classed, at the same time as starting a complete review of the training model and supply in order to ensure that it better met actual demands on field deriving from the evolution of Terna and the new features introduced into the HR development and management systems.

In 2010, the main new features introduced were all activated and started-up. These include, perhaps the most relevant, the medium-long term training schemes targeting new employees, with the aim of *sharing knowledge* and transferring *typical, proprietary know-how* of Terna, in order to ensure that it is maintained and optimised. Medium-long term training schemes were also begun for active resources, with the aim of aligning and updating the skills of homogenous professional groups, often with strategic company relevance and duties.

Additionally, the training scheme for the education section was also reviewed and enriched with new initiatives, devoted to the development of managerial and personal skills, namely soft and organisational skills. More specifically, in the wake of the introduction of the Performance Management System (GPS), specifically-focussed initiatives have been developed for the various training targets (middle managers, team leaders, professional managers, etc.), laid out in a customised fashion on the Terna organisational conduct expected in performance. Alongside these new proposals, the training commitment continued with regards to the promotion and diffusion within the company at various levels of sensitivity and skills of matters of Economics, Project Management and the Electricity Market.

Finally, a new line of training products has been developed: homogenous management/department events/workshops with team building objectives and a focus on strategic matters and challenging objectives.

With reference to the initiatives taken in relation to the development of technical-professional knowledge, specialise safety-related knowledge and transversal skills (e.g. I&CT), the traditional major commitment has been confirmed to ensure the necessary update and adjustment to technological and process innovation. We should point out, as far as safety is concerned, the completion of the activities looking to apply the provisions of the Consolidated Law 81/08.

On corporate governance, the annual update training scheme was developed on the provisions of ex Model 231.

The Campus portal, which has been accessible from the intranet since the end of 2009, has been further enhanced. This has been done with a view both to supporting the diffusion of information on the training offer and to make the wealth of documentation available surrounding the courses, in particular those run by the Terna Faculty where there is a real baggage of company know-how.

In short, 96% of resources attended at least one course in 2010 (+0.5% on 2009), with more than 171,000 hours of training actually delivered (approx. +5% on 2009).

### Industrial relations

Industrial relations were marked by the negotiation for the renewal of the national collective employment contracts on 18 July 2006 for all workers of the electrical sector, as this expired on 30 June 2009.

The agreement reached was signed on 5 March 2010 by Assoelettrica, Federutility, Enel, GSE, SOGIN and Terna.

The expiry date for the renewed contract has been deferred by 6 months to 31 December 2012.

Together with the national contract, guidelines were signed for the definition of new rules governing the right to strike in the sector.

## Other information

### Related party transactions

Having been determined in 2007 that Cassa Depositi e Prestiti S.p.A. exercises de facto control, transactions undertaken by Terna and the Group with related parties during the year consisted of intercompany transactions, transactions with employee pension funds (Fondenel and Fopen), and transactions with companies of the:

- the GSE Group;
- the Enel Group;
- the Eni Group;
- the Ferrovie dello Stato Group;

and those with ANAS S.p.A.

The Parent's Corporate Governance rules, which are detailed in the specific report published with this Annual Report (available on the website [www.terna.it](http://www.terna.it)), establish the conditions for ensuring that related party transactions are carried out in accordance with criteria of procedural and substantive propriety under the same terms and conditions that would apply to transactions with third parties. More specifically, on 12 November 2010, the Board of Directors of the Parent, having obtained the favourable opinion of the Related Parties Committee, approved the "Related party transaction procedure" in implementation of CONSOB Regulation no. 17221 of 12 March 2010, subsequently amended by Resolution no. 17389 of 23 June 2010, which issued the "Regulation incorporating provisions on related party transactions" <sup>(9)</sup>. The Regulation provisions, looking to regulate information transparency with regards to the market and principles of transparency and substantive and procedural correctness in the implementation of related party transactions stand alongside the general principles concerning the duties of directors in conflict of interest established by art. 2391 of the Civil Code and art. 150 of the Consolidated Law on Finance, the principles of procedural correctness set out in the Self-Regulatory Code of listed companies published by Borsa Italiana S.p.A. and the accounting disclosure obligations established by the provisions on financial statements set out by the Civil Code (arts. 2423 *et seq.* of the Civil Code) and article 154-*ter* of the Consolidated Law on Finance.

The provisions relating to the public disclosure obligations (immediate and regular) in relation to related party transactions, considered individually, of significant importance, came into effect on 1 December 2010, whilst all other procedural provisions are compulsory as from 1 January 2011.

The nature of transactions, assets and liabilities with related parties as well as associated revenue and costs posted for the year, and receivables and payables at 31 December 2010, are presented in the respective notes on individual items in the separate and consolidated financial statements, and in a specific section of the notes ("Related party transactions"), which should be consulted for more details.

In addition, transactions with members of the Company's Board of Directors and Board of Statutory Auditors, and in particular their remuneration, bonuses and other incentives, are detailed in the notes to the financial statements in the sections "*Personnel expense*" and "*Services*", respectively.

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

As required by the provisions of art. 79 of CONSOB Resolution no. 11971/99, the following table lists the shares of Terna S.p.A. and its subsidiaries held by Directors, Statutory Auditors 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' register, communications received or other information obtained from the members of the boards of directors and statutory auditors, and from General Managers. These include all those persons who, in 2010, filled the position of Director, Statutory Auditor, and General Manager.

(9) The Regulation has been interpreted also considering CONSOB Communication no. DEM/10078683 of 24 September 2010 and subsequent amendments and supplements.

| Surname and name              | Associate    | Number of shares held at the end of the last year (2009) | Number of shares acquired (in 2010) | Number of shares sold (in 2010) | Number of shares held at the end of the last year (2010) | Possession of title <sup>(1)</sup> |
|-------------------------------|--------------|--|-------------------------------------|---------------------------------|--|------------------------------------|
| Luigi Roth                    | Terna S.p.A. | 0  | 40,000 <sup>(2)</sup>               | 0                               | 40,000 <sup>(3)</sup>                                    | ownership                          |
| Flavio Cattaneo               | Terna S.p.A. | 200,000  | 0                                   | 0                               | 200,000  | ownership                          |
| Cristiano Cannarsa            | Terna S.p.A. | 0  | 0                                   | 0                               | 0  | -                                  |
| Paolo Dal Pino                | Terna S.p.A. | 2,150  | 0                                   | 0                               | 2,150  | ownership                          |
| Matteo del Fante              | Terna S.p.A. | 0  | 0                                   | 0                               | 0  | -                                  |
| Claudio Machetti              | Terna S.p.A. | 0  | 0                                   | 0                               | 0  | -                                  |
| Salvatore Machì               | Terna S.p.A. | 40,000 <sup>(4)</sup>                                    | 20,000 <sup>(5)</sup>               | 0                               | 60,000 <sup>(6)</sup>                                    | ownership                          |
| Michele Polo                  | Terna S.p.A. | 1,700  | 0                                   | 0                               | 1,700  | ownership                          |
| Vittorio Rispoli              | Terna S.p.A. | 0  | 0                                   | 0                               | 0  | -                                  |
| Luca Aurelio Guarna           | Terna S.p.A. | 0  | 0                                   | 0                               | 0  | -                                  |
| Marcello Cosconati            | Terna S.p.A. | 0  | 0                                   | 0                               | 0  | -                                  |
| Lorenzo Pozza                 | Terna S.p.A. | 0  | 0                                   | 0                               | 0  | -                                  |
| Stefania Bettoni              | Terna S.p.A. | 0  | 0                                   | 0                               | 0  | -                                  |
| Mario Paolillo <sup>(7)</sup> | Terna S.p.A. | 0  | 0                                   | 0                               | 0  | -                                  |

(1) This column – which is in addition to the format provided for in Annex 3C of art. 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) of which: 40,000 held by spouse;

(3) of which: 40,000 held by spouse;

(4) of which: 40,000 held by spouse;

(5) of which: 10,000 held by spouse;

(6) of which: 50,000 held by spouse;

(7) deceased on 30 November 2010.

## Significant non-recurring events and operations, atypical or unusual transactions

No significant, non-recurring, atypical or unusual transactions – with the exception of the transactions described in the specific section entitled “Business Combinations” of the consolidated financial statements – were conducted during 2010, either with third parties or related parties.

## Other information

### Treasury shares

The Company does not hold any treasury shares or shares of Cassa Depositi e Prestiti S.p.A., nor has it acquired or sold any during the year, either directly or indirectly.

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

Within the legally prescribed deadline, Terna S.p.A. updated its 2010 Personal Data Protection Document pursuant to the personal data protection code (Legislative Decree no. 196 of 30 June 2003) and implemented the initiatives required to improve management as introduced by the new version.

Additionally, during the year it started-up some initiatives aimed at applying the Privacy Guarantor Provision of 8 April 2010 (in Official Journal no. 99 of 29 April 2010), concerning “measures on the processing of personal data and video-surveillance” in preparation for the expiry of the terms in April 2011, when all new security and protection measures for data recorded using video-surveillance systems must be duly adopted.

### Information on the ownership structure

Information required under art. 123-bis, “Report on Corporate Governance and ownership structures” of the “Consolidated Law on Financial Intermediation”, is presented in a separate report (Annex - Corporate Governance), which is attached to the Directors’ Report.

### Certifications in accordance with article 2.6.2 of the Borsa Italiana Regulation with regards to the conditions pursuant to articles 36 and 37 of the CONSOB Market Regulation (no. 16191/2007)

With regards to the provisions of article 36 of the CONSOB Markets Regulation (no. 16191/2007), Terna S.p.A. does not hold any majority shares in companies incorporated and regulated by the laws of countries not members of the European Union. Pursuant to art. 37 of the CONSOB Regulations, Terna is subject to the de facto control of Cassa Depositi e Prestiti S.p.A., which owns a 29.858% equity stake in the Company, according to a disclosure made by Cassa Depositi e Prestiti on 19 April 2007. At present, no management or coordination activities have been formalised or exercised; Terna conducts its own operations directly or through its subsidiaries, and is managerially and contractually independent.

# The Terna Group in the near future

## Events after the reporting date

### Continuing operations

#### Acquisition of the investment in CGES and agreement for the construction of the electrical connection between Italy - Montenegro

On 23 November 2010, Terna undersigned the definitive agreement for the strategic partnership with the transmission operator of Montenegro, CrnoGorski Elektroprenosni Sistem AD ("CGES"), and the government of Montenegro, acting in the capacity of majority shareholder of CGES; this agreement refers to the construction of the new electrical connection between Italy - Montenegro and the strategic Terna-CGES partnership. The transaction was completed in January following the occurrence of the conditions precedent. The stipulation was completed following the approval, on the part of the Shareholders' Meeting of CGES, of the share capital increase for Terna and the adoption of new Bylaws. Terna therefore became the shareholder of CGES with 22.09% of the share capital and, in its capacity as the new shareholder, undersigned the shareholders' agreement relative to the new governance system and the industrial contract for investments. The agreement represents the end point of a process of industrial and country cooperation and is part of the intergovernmental agreements between Italy and Montenegro which were initiated on 19 December 2007 with the start-up of activities of the Italy-Montenegro Work Group and consolidated on 6 February 2010 by means of the contract which ratified the commitment at an institutional level for the construction of a new submarine electrical connection and the implementation of partnerships with national transmission operators. It is expected that the overall investment of Terna for the first "electrical bridge" to the Balkans will amount to approximately €760 million. The investment of CGES for the connection of the existing network and the reinforcement of the local network will total circa €100 million.

#### 2011-2015 Business Plan

On **14 February 2011**, Terna presented to financial analysts the Company's 2011-2015 business plan, after approval of the plan by the Board of Directors on that same date. The 2011-2015 plan of the Terna Group follows five main guidelines:

- traditional regulated activities: Increase of investments from €4.3 to approx. 5 billion (+15%) in order to modernise the grid; development investments for which incentive-based remuneration is planned represents circa 82% of the total and increased from €3.3 billion to 4 billion;
- non-traditional activities. Investment activities were tripled for these activities, with planned allocations of up to €1 billion. In particular, the development of an additional set of photovoltaic projects of circa 50 MWp is planned for the course of 2011. In addition, other investment opportunities will also be assessed, including within the sector of energy efficiency, for the construction and management of grid infrastructures for connecting renewable energy source plants in the Balkans area to the local grid and for storage and battery systems in the Italian grid;
- improved margins (EBITDA margin): increasing revenue and containing costs will improve Group profitability from the current 74% to 78% at the end of the period covered by the plan;
- a sound capital structure: during the period of the plan, commitment to maintain the ration between debt and regulated invested capital (RAB) under 60%;
- confirmation of dividend policy: the 2011-2015 Strategic Plan confirms the dividend policy. As had previously occurred with the sale of Terna Participações, part of the capital gains attained with the sale of non-traditional assets may integrate the above-mentioned policy which provides for an annual growth of 4%, assuming the year 2008 as the year of reference.

#### Founding of new companies of the Group

On **8 March 2011**, the subsidiary SunTergrid S.p.A. formed "Nuova Rete Solare S.r.l." ("NRTS S.r.l.") with a share capital of €10,000. The corporate purpose of this new company is to design, install, manage, develop and maintain grids and other infrastructure connected to such grids, as well as plant and equipment for the transmission and dispatching of electricity, and for other segments of the energy sector and similar, related or connected sectors, together with plant for the generation of electricity from renewable or other sources, for self consumption or for sale.

#### 10-year bond issue for €1.25 billion

On **8 March 2011** Terna launched a bond issue on the market in euros, at a fixed rate, with expiry in 10 years, for a total of €1.25 billion under the scope of its Euro Medium Term Notes (EMTN) programme. This has been assigned an A+ rating for Standard and Poor's, A2 for Moody's and A+ for Fitch. The bond expires on 15 March 2021, has an annual coupon of 4.750% and issue price of 99.245. The security has thus been priced with a spread of 130 basis points as compared with the mid swap. Securities are listed on the Luxembourg Stock Exchange.

The transaction, destined for Institutional Investors, has been placed by a syndicate of banks comprising Banca Akros S.p.A., MPS Capital Services S.p.A., Natixis, UniCredit Bank AG and WestLB AG as joint-lead managers and joint-bookrunners. The transaction is intended to finance the grid development investments envisaged in the Parent's business plan.



### The new “SA.PE.I.” power line uniting Sardinia and mainland Italy is opened

On **17 March 2011** Terna was proud to open the new SA.PE.I. power line. SA.PE.I. is an acronym for SARdegna-PENisola-Italiana (Sardinia – Italian – Peninsula) and this is the first ever direct electrical connection to be created between Sardinia and mainland Italy, and the most important and technologically advanced high voltage power line ever to be developed in Italy. The infrastructure has achieved a great many records, in fact, which include: the world’s longest “electrical bridge”, with a power of 1,000 megawatts; the world’s deepest, as it extends for 435 km from Fiumesanto (Sardinia) to Latina (Lazio), reaching depths of 1,640 m; and the greatest investment: worth a grand total of € 750 million, it is the most important investment ever to be made in Italy in a single electrical infrastructure.

More than 50% of the work was funded by Terna’s own means with the remainder financed by grant of € 373 million awarded by the European Investment Bank (EIB) due to the high strategic value at hand. The result boasts a great many economic, electrical and environmental benefits. The work allows for annual savings of € 70 million for the electrical system, thanks to the elimination of “bottlenecks” between Sardinia and the rest of the electricity market, in addition to increased safety of the Sardinian electrical system and a more secure coverage of the demands of Lazio and central Italy, thanks to use of more efficient energy, partly originating from Sardinia.

### Assets held for sale

#### Financing Contract

On **28 January 2011** the company RTR, in view of the sale, signed a refinancing contract with a term of 18 years. The total maximum value of the refinancing transaction amounts to € 593.8 million (of which € 521.3 for cash and € 72.5 for signature) and aims to refinance the investments sustained to develop the photovoltaic plant portfolio held by Rete Rinnovabile on a project financing no recourse basis. The transaction was concluded with a pool of 7 banks consisting of Banca Popolare di Milano, Gruppo Credito Valtellinese, Meliorbanca e Banca Popolare dell’Emilia Romagna, MPS Capital Services (which will also act as Facility Agent), Natixis, Unicredit Corporate Banking and West LB.

#### Capital contribution payment in favour of Valmontone Energia S.r.l.

On **4 February 2011**, RTR completed a payment of € 10.0 million to Valmontone Energia S.r.l. as a capital contribution payment in order to complete the photovoltaic plant.

#### Sale of Rete Rinnovabile S.r.l. completed

In implementation of the agreement signed on 18 October 2010 by Terna S.p.A., SunTergrid S.p.A. and Terra Firma Investments (GP) 3 Limited (wholly owned by Terra Firma Capital Partners III, L.P.), on **31 March 2011**, the transfer to RTR Acquisition S.r.l. (an indirect subsidiary of Terra Firma Investment (GP) 3 Limited) of 100% of the share capital of Rete Rinnovabile S.r.l. (“RTR S.r.l.”) was completed. RTR S.r.l. owns 62 photovoltaic plants, located in 11 different regions of Italy, for a total capacity of 143.7 MWp, of which 101.6 MWp will benefit from the 2010 Energy Account tariffs for the 1<sup>st</sup> quarter 2011. The sale of the investment in RTR S.r.l. has resulted in total net income of around € 204 million and a reduction in the effective net financial debt of continuing operations of the Terna Group for more than € 200 million.

The completion of the sale confirmed the effect on the 2010 consolidated income statement, booked as the contract margin in terms as compared with total costs sustained during the year, on the basis of works progress, as described in full previously, amounts to € 147 million. The difference will instead be recognised on an accruals basis in 2011.

It is also specified that in addition to renting the land, Terna will also provide RTR S.r.l. with plant maintenance, surveillance and monitoring services, according to multiyear contracts defined in the context of the sale. At the end of the individual rental contracts, Terna will regain possession of the leased areas.

## Outlook

The focus of 2011 will be on implementing the 2011-2015 business plan adopted by the Company’s Board of Directors. Investments under the business plan will be targeted at increasing interconnections with abroad, reducing grid congestion and at removing bottlenecks caused by an increase in energy generated from renewable sources. The Company’s objectives are increasingly oriented towards achieving operating efficiencies, ensuring the highest possible standards of transmission service, and ensuring increasingly efficient and secure management of electricity system energy flows.

In 2011, there will also be the usual comparison of notes with AEEG, aiming to ensure continuity and stability of the principles underlying the determination of tariffs for the 4th regulatory period running from 2012 to 2015.

In terms of unregulated activities, in 2011 the company will also be involved in developing a second tranche of photovoltaic projects aimed at further optimising the Group’s assets.





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## Italy's regulatory framework

### Regulatory framework

Below is a brief description of the main regulatory measures that affected the Company in 2010.

**Presidential Decrees appointing special Commissioners for works on the national electricity transmission grid dated 12 November 2009**, published in Italian Official Journals 31 and 32, on 8 and 9 February 2010.

These Decrees, implementing Law Decree 78/2009 as subsequently modified, identify certain electricity grid infrastructure, urgently needed for the economic-social development of the country, to be constructed with special means and procedures. The Commissioners hold powers to make exceptions to current regulations and to override non-performing administrations in order to prepare the necessary deeds for authorisation.

**Law Decree 3 dated 25 January 2010, "Urgent measures to guarantee the certain supply of electricity to the largest islands"**, published in Italian Official Journal 20, on 26 January 2010, and converted with modifications into Law 41 dated 22 March 2010, and published in Italian Official Journal 72, on 27 March 2010.

The Decree envisages:

- for the three-year period 2010-2012, a new back-up service provided by Terna amounting to 500MW for Sicily and 500MW for Sardinia;
- an increase by up to 500 MW in the "interconnection capacity with abroad, pursuant to art. 32, paragraph 1 of Law 99 dated 23 July 2009" (interconnectors), linked to an increase in power available from the instantaneous reduction by end customers of their withdrawals from the grid;
- simplification measures for the performance of certain works on the national electricity transmission grid: a) extension of the simplified procedure for the Notification of the Beginning of the Activities for the reclassification interventions up to 380 kV on the existing cross-border interconnection lines of lower voltage; b) Notification of the Beginning of the Activities for the modifications in the electricity stations, even regarding volume, as long as with determined characteristics; c) the formalisation of the final authorisation for the works, which are part of the national transmission grid, existing at the date the ratification law becomes effective.

**Legislative Decree 27 dated 27 January 2010, "Implementation of Directive 2007/36/EC, regarding the exercise of certain rights by shareholders of listed companies"**, published in Italian Official Journal 53, on 5 March 2010.

This Decree contains numerous changes to the regulations governing the exercise of shareholder rights in terms of transparency and the calling of general Meetings.

The application of the provisions of Italian Legislative Decree no. 58/98 on the appointment of the Board of Directors and the Board of Statutory Auditors to companies with public ownership that are subject to the golden share rules (Legislative Decree 332/94) and, in particular, art. 147-ter and art. 148. At least one fifth of the directors not appointed pursuant to art. 2.1.d (without voting rights) must be appointed from the minority lists.

The Decree modifies the related provisions of the Consolidated Finance Act, establishing deadlines for the presentation of lists of candidates and for checking ownership of the minimum shareholdings required for the presentation of lists.

The law also establishes the applicability to all companies subject to golden share rules of the regulations governing the calling of general Meetings, covered by art. 125-bis which requires the notice to be published at least 30 days prior to the Meeting (40 if called for the election of directors and officers, 21 for capital reductions).

The new regulations concerning summoning and the rights in the Meetings apply to the Meetings whose notification is published after 31 October 2010.

**Legislative Decree 32 dated 27 January 2010, "Implementation of Directive 2007/2/EC of the European Parliament and of the Council dated 14 March 2007, which establishes an infrastructure for geographical information in the European Community (Inspire)"**, published in Italian Official Journal 56, on 9 March 2010.

**Legislative Decree 39 dated 27 January 2010, "Implementation of Directive 2006/43/EC, regarding the statutory audit of annual and consolidated financial statements, which modifies Directives 78/660/EEC and 83/349/EEC, and repeals Directive 84/253/EC"**, published in Italian Official Journal 68, on 23 March 2010.

**Legislative Decree 31 dated 15 February 2010, "Instructions for the location, construction and operation in Italy of nuclear power plants, plant for the production of nuclear fuel, systems for the storage of spent nuclear fuel and radioactive waste, as well as compensation measures and campaigns to inform the public, pursuant to art. 25 of Law 99 dated 23 July 2009"**, published in Italian Official Journal 55, on 8 March 2010.

This Decree governs the location and authorisation of plants for the production of nuclear power. The authorisation includes the “works to develop and prepare the national electricity transmission grid for the input of the power generated”.

**Legislative Decree 53 dated 20 March 2010, “Implementation of Directive 2007/66/EC which modifies Directives 89/665/EEC and 92/13/EEC with regard to improving the effectiveness of appeal procedures in the award of public contracts”**, published in Italian Official Journal 84, on 12 April 2010.

**Legislative Decree 56 dated 29 March 2010, “Modification and additions to Decree 115 dated 30 May 2008, implementing Directive 2006/32/EC, concerning the efficient end use of energy and energy services and repealing Directive 93/76/EEC”**, published in Italian Official Journal 92, on 21 April 2010.

This Decree modifies the definition of efficient system of usage, extending the category to plant for the production of electricity (from renewable sources or cogeneration), directly connected via a private link without obligation to connect third parties to the plant, for consumption by a single end user, with a nominal power of up to 20 MWe (instead of the current 10).

The Decree establishes that in the regulation adopted by the AEEG, in implementation of the Legislative Decree, with reference to the activities of transmission and dispatch, it shall be ensured that fees “are only applied to the electricity withdrawn from the connection point”.

**Decree by the Ministry for Economic Development dated 26 April 2010: extension of the national transmission grid**, published in Italian Official Journal 112, on 15 May 2010.

Decree for extending the National Transmission Grid, aiming to include the portions of high voltage distribution grid sold by A2A S.p.A. through the company RETRASM S.r.l.

**Law Decree 72 dated 20 May 2010, “Urgent measures for the deferral of deadlines on environmental and self-transportation matters, as well as for the allocation of CO<sub>2</sub> emission quotas”** published in Italian Official Journal 117, on 21 May 2010.

**Prime Minister's Decree dated 20 May 2010**, published in Italian Official Journal 117, on 21 May 2010.

In implementation of the European Court of Justice ruling on 26 March 2009, this Decree repeals the criteria for the exercise of special powers by the State in direct or indirect subsidiaries operating in strategic sectors, such as energy sources and public services, which include Terna. The rules covering the existence and definition of special powers pursuant to Law Decree 332/1994, attributed in the Bylaws to the public shareholder, remain in force.

**Law Decree 78 dated 31 May 2010, regarding financial stabilisation and economic competitiveness**, published in Italian Official Journal 125, on 31 May 2010, converted with modifications into enabling Law no. 122 dated 30 July 2010, published in Italian Official Journal 176, on 30 July 2010.

The Decree envisages:

- deferral of payment of the advance IRPEF due for 2011 and 2012 by the withholding agents;
- extension of the beneficial tax regime for production prizes, to which the rate of 10% applies;
- the right of Regions in the south of Italy to reduce the IRAP tax;
- from 1 July 2010, it transfers the insurance position of the Social Security fund for employees of the National Electricity Board and Private Electricity Companies to the Social Security fund for employees, so the same as other re-joining cases it will be on onerous terms, implementing the rules set out by general regulations;
- the possibility for the Environment Ministry, in the context of the Services Conference, for the purposes of the inquest and to ensure compliance with the terms of concluding the VIA procedure, to replace the VIA Commission with other bodies of the public administration or bodies and universities.

**Law 96 dated 4 June 2010, “Instructions for compliance with obligations deriving from Italy's membership of the European Communities - Community Law 2009”**, published in Italian Official Journal 146, on 25 June 2010.

The law enables the government to implement deeds of community interest, including:

- the renewables Directive (2009/28/EC), to be adopted by 5 December 2010;
- the internal energy market Directive (2009/72/EC), to be adopted by 3 March 2011;
- the critical European infrastructures Directive (2008/114/EC), to be adopted by 12 January 2011;
- the framework decisions on justice: by 10 July 2011, the crimes involving the administrative responsibility of companies will be extended to include violations of community or community-related environmental regulations committed with intent or gross negligence;
- the requirements of 2004/913/EC and 2009/385/EC: listed companies must publish a report on their policies for the remuneration during the coming financial year of their board of directors, general managers and managers with strategic responsibilities, as well as on the remuneration paid for any reason and in any form to such parties during the reference year.

**Constitutional Court Ruling 215 dated 9 June 2010**, published in Italian Official Journal 25, special series, on 23 June 2010.

The ruling declares the provisions of art. 4 of Law Decree 78/09, concerning the appointment of special commissioners for the performance of urgent works on the national electricity transmission grid, to be illegitimate.

**Legislative Decree 2 July 2010, no. 104, “Implementation of article 44 of Law dated 18 June 2009, no. 69, delegating the government to reorder the administrative process”**, published in Italian Official Journal 156, on 7 July 2010.

**Legislative Decree 29 June no. 128, “Changes and additions to Legislative Decree 3 April 2006, no. 152, regulating of environment issues, pursuant to article 12 of Law dated 18 June 2009, no. 69”**, published in Italian Official Journal 186, on 11 August 2010.

The Decree amends the Environmental Code (Legislative Decree no. 152/06) adding a new provision that specifies that the Strategic Environmental Evaluation is not necessary for changes to land plans “resulting from authorisations to single works that, by law, act as variants to the above-mentioned plans and programmes”. Therefore, the authorisations to intervene on the national electricity grid that cause changes in the regulatory plans of local bodies, do not constitute changes on which it is necessary to carry out a prior Evaluation.

**Italian Law no. 136 of 13 August 2010 “Extraordinary plan against the mafia and appointment of the government on anti-mafia regulations”**, published in Italian Official Journal 196, on 23 August 2010.

This introduces rules and regulations for anti-mafia certification and traceability of financial flows in tenders.

**Decree of the President of the Republic dated 2 August 2010, no. 150 on “Rules carrying regulations relative to releasing anti-mafia information following on from accessing and checking work sites of companies involved in carrying out public works”**, published in Italian Official Journal 212, on 10 September 2010.

### **National action plan for renewable energy**

On 30 June 2010, the Government sent to the European Commission the National action plan for renewable energy, required by Directive 2009/28/EC.

The Plan describes the industry’s objectives: to reach the threshold of 17% internal consumption of energy from renewable sources, it is expected that in 2020 43,823 MW of renewable source energy be installed, of which 8,600 MW solar power, 17,800 MW hydroelectric, 920 MW geothermal, 12,680 MW wind, 3,820 MW biomass, 3 MW tidal.

The Plan highlights the importance of a coordinated development of the electricity grid and renewable sources.

Law no. 129 of 13 August 2010, published in Italian Official Journal 192, on 18 August 2010 has then introduced both provisions designed to simplify the electricity grid authorisation procedures and provisions on renewable sources:

- a new regulation for the appointment of special commissioners for the performance of urgent works on the national electricity transmission grid and the possibility of extending the appointment of commissioners for the national electricity transmission grid to January 2010, where an agreement is reached between the government and the regions concerned by the works;
- that, for works on the grid subject to DIA, it is down to the Municipalities, which may detect irregularities, to notify the Ministry for Economic Development of the above-mentioned breaches; it is instead down to said Ministry to reach a final decision on whether to halt the works or not;
- that the consolidated authorisation in accordance with Legislative Decree no. 387/03 includes, along with renewable source plants, interventions on the electricity transmission and distribution grids envisaged in the connection solution prepared by the grid manager;
- the extension of the 2010 incentives to solar power plants realised before 31 December 2010 which enter service before 30 June 2011.

In implementation of the law, the Ministry for Economic Development shall define:

- appropriate financial guarantees to accompany the application for authorisation of renewable source plants, in accordance with art. 12 of Legislative Decree no. 387/03;
- strengthening of instruments aimed at guaranteeing the safety of the electrical system up to a power of 1,000 MW.

The Authority for Energy and Gas defines, on the basis of the directives of the Ministry for Economic Development, the rules aimed at preventing booking of grid capacity for plants powered by renewable sources for which the conditions of concrete realisation have not been verified within the established timings.

**Decree issued jointly by the Ministry for Economic Development jointly with the Ministry for the Environment of 6 August 2010 “Incentives for the production of electricity by means of photovoltaic conversion of the solar source”,** published in Italian Official Journal 197, on 24 August 2010.

The Decree sets incentives for solar power plants entering service after 31 December 2010.

The new tariffs for 2011 set out four-month brackets on the basis of the date of each plant coming into service:

- between 31 December 2010 and 30 April 2011
  - €0.314/kWh for plants of a power greater than 200 kW and up to 1,000 kW;
  - €0.313/kWh for plants of a power greater than 1,000 kW and up to 5,000 kW;
  - €0.297/kWh for plants of a power greater than 5,000 kW;
- between 30 April 2011 and 31 August 2011
  - €0.303/kWh for plants of a power greater than 200 kW and up to 1,000 kW;
  - €0.289/kWh for plants of a power greater than 1,000 kW and up to 5,000 kW;
  - €0.275/kWh for plants of a power greater than 5,000 kW;
- between 31 August 2011 and 31 December 2011
  - €0.266/kWh for plants of a power greater than 200 kW and up to 1,000 kW;
  - €0.264/kWh for plants of a power greater than 1,000 kW and up to 5,000 kW;
  - €0.251/kWh for plants of a power greater than 5,000 kW.

For the following years, 2012 and 2013, the Decree provides for an incentive to be calculated with a deduction of 6% to be applied respectively to the tariff of the last four months of 2011 and the tariff of 2012.

**Decree issued by the Ministry for Economic Development on 10 September 2010 “Guidelines for authorising plants powered by renewable sources”** published in Italian Official Journal 197, on 24 August 2010.

This Decree adopts the national guidelines for the authorisation of plants powered by renewable sources. The provision came into force on 3 October 2010 and applies to all national territory as from 1 January 2011, even if implementing regulations have not been issued by the regions, or if regional regulations should differ.

The guidelines set out that the proposer accompany the application with the documentation listed in the guidelines. It is specified that works connected to the plant, subject of a single authorisation pursuant to Legislative Decree 387/03, include all works necessary for the connection, indicated in the connection estimate prepared by Terna and accepted by the proposer, excluding new power lines or upgrades that Terna has included in the Development Plan, except for the connections attachment.

It is expressly set out that the documents that the proposer must attach to the plant authorisation application must include, at risk of being unable to proceed, the estimate for the connection, drawn up by the network operator and accepted by the proposer, inclusive of all printouts relative to the connection plant.

**Decree issued by the Ministry for Economic Development of 10 December 2010 “Implementation of article 30, paragraph 27 of Law no. 99 of 23 July 2009 on relations between the electricity grid managers, the concession distribution companies, the owners of private grids and the end customers connected to said grids”,** published in Italian Official Journal 310, on 31 December 2010.

The Decree intervenes in the relations between electricity grid managers, concession distribution companies, owners of private grids and end customers connected to said grids, in force as from 1 January 2011, establishing that the managers of private grids, including internal utility grids, must “connect all parties so requesting to their grids” and guarantee “the right of a party connected to a private grid to access, upon request, the public grid, as a guarantee of freedom of choice of electricity supplier”. The AEEG must define the method by which the right to free access to the electricity system shall be exercised.

The AEEG will need to define the criteria and conditions on which basis Terna “may use the infrastructures of a grid manager subjected to the obligation to grant free access to the electrical system, for the implementation of activities linked to the delivery of a distribution or transmission service, including the supply of the connection service”. The Authority shall also determine relations and economic conditions between the grid manager subjected to the obligation to ensure free access to the system and Terna or the distribution company.

Self-provisioning systems are excluded from the obligation to grant free access.



**Italian Law no. 220 of 13 December 2010 “2011 stability law”**, published in Italian Official Journal 297, on 21 December 2010. The 2011 stability law (Law 220/10) establishes that for 2011, upon application by a company and up to the limit of the allocation of € 650 million, benefits shall be granted on contributions on increased productivity, quality, profitability, innovation, organisational efficiency linked to the results in relation to the economic trend or business income or any other element that is relevant in terms of ensuring the improvement of business competitiveness. The total annual amount inclusive of supplies admitted to the benefit has been established as up to a maximum of 5 percent of the contractual income received. The benefit on social security contributions due from employers is established as 25 percentage points. The benefit on social security contributions due from employees amounts the entire value of social security contributions at his expense.

**Decree by the Ministry for Economic Development of 15 December 2010: update of the Convention annexed to the Concession to Terna for transmission and dispatching activities**, published in Italian Official Journal 4, on 7 January 2011. The Decree amends the Convention annexed to the Concession granted to Terna.

The corporate purpose is extended to include the development and management of "plants for the storage and conversion into electricity, aimed at guaranteeing the safety of the system, its correct function and maximum use of the power available from renewable sources and the provisioning of resources for dispatching services".

It is envisaged that, in compliance with the connected principles of independence, third party nature and non-discrimination, Terna shall "design, develop and manage, only on a temporary basis, infrastructures and plants for the production of electricity, also held for sale, through independent corporate structures" as long as production does not become prevalent over the activities concerned by the Concession and does not affect the independence of Terna with respect to the interests of the production, importing and sale of electricity.

The development plan must also include a specific section devoted to grid infrastructures for the development of renewable sources.

The development plan approval procedure is amended to establish that: by 31 January, the plan shall be sent for preliminary review by the Ministry for Economic Development, which, within forty-five days of receipt shall verify that it complies with the guidelines given, make any requests and prescriptions and, if necessary, amendments and supplements. Once these terms have expired, the plan shall be intended as deemed to have been accepted. Following adoption of the SEA opinion by the Ministry for the Environment jointly with the Ministry for Cultural Heritage in accordance with Legislative Decree no. 152/06, the Ministry for Economic Development shall approve the grid development plan "within thirty days of receipt of the SEA opinion".

In compliance with criteria of organisational efficiency, Terna may entrust the development and management of the activities concerned by the Convention to subsidiaries. In this case, Terna must notify the Ministry to this effect.

**Decree issued by the Ministry for the Environment and Protection of the Territory and the Sea of 22 December 2010 “Amendments and supplements to the Decree of 17 December 2009, setting out the institution of the system for controlling the traceability of waste”**, published in Italian Official Journal 302, on 28 December 2010.

**Decree by the Ministry for Economic Development of 22 December 2010: extension of the national transmission grid**, published in Italian Official Journal 11, on 15 January 2011.

Decree for extending the National Transmission Grid, aiming to include the portions of high voltage distribution grid sold by SET Distribuzione S.p.A and Dolomiti Energia S.p.A.

**Law Decree no. 225 of 29 December 2010 “Extension of the terms established by legislative provisions and urgent interventions in tax matters and in support of enterprises and families”**, published in Italian Official Journal 303, on 29 December 2010.

The Decree has amended the procedure by which urgent works to be commissioned are identified: the terms within which the Council of Ministers, upon proposal by the Ministry for Economic Development jointly with the Ministry for Infrastructures and the Ministry for the Environment with the Ministry for regulatory simplification must reach an agreement with the independent provinces and regions concerned, in order to identify the electricity production and transmission infrastructures of national strategic interest, has now been established as until 31 March 2011 (no longer “within thirty days of the calling of the first Meeting of the government and independent province or region concerned by the reaching of the agreement”). Once these terms have expired, by resolution grounded by the Council of Ministers which the Chairman of the independent province or region concerned has been invited to attend, the government may identify urgent interventions “even regardless of the understanding”.

## Resolutions of the Authority for Electricity and Gas

### ARG/elt Resolutions 5/10, 100/10 and 207/10

With this decision, the Authority has modified the conditions for the dispatching of non-programmable renewable sources, revoking at the same time Resolution no. 330/07. The interventions mainly refer to four aspects:

1. remuneration modalities of the lack of wind energy production deriving from the implementation of dispatching orders given by Terna;
2. the definition of grid services to which wind power production plants are subjected. In order to take account of the specific nature of wind power units, Terna modifies Grid Code Attachments A6 and A13, after consultation with the operators and subsequent approval by the Authority. With regard to Attachment A17 and without prejudice to the requirements established for new plant, a procedure is introduced for the voluntary alignment of existing plant. With Resolution ARG/elt 207/10, a budget has been established for Terna for the remuneration of existing manufacturers intending to adapt to the provision of grid services, in accordance with the terms and conditions defined by Terna, establishing that 5% of expenses sustained for the adaptation shall be deducted from the Terna incentive for the provisioning of dispatching resources pursuant to Resolution 351/07;
3. incentives for accurate forecasting by the units powered by renewable sources that cannot be planned (change to Resolution 111/06 in order to introduce incentives whereby Terna recognises a fee for accurate forecasting to the Dispatching Users who own such units);
4. further instructions to Terna for improvement of the dispatching service.

With Resolution ARG/elt 100/10, the Authority has positively checked the modification proposals of Attachments A6 and A13 of the Network Code, and the proposal to define the methods of use of the remote switch-off applied to wind farms prepared by Terna S.p.A. The documents in question had been subjected to the ordinary update procedure of the Network Code as per paragraph 14.2; said paragraph sets out that, before the Authority's approval, the subjects interested are consulted and the opinion of the Users' Consultative Committee is obtained, pursuant to art. 1, paragraph 4 of DPCM dated 11 May 2004.

### ARG/elt Resolution 15/10

By this resolution, issued pursuant to art. 1 of Law Decree 3 dated 25 January 2010, concerning urgent measures to guarantee the certain supply of electricity to the largest islands, the Authority has established the conditions applying to the service of instantly reducing the withdrawal of electricity on the largest islands (Sicily and Sardinia).

The resolution defines the characteristics of the service that differs from the interruptibility service covered by Resolution 289/06 (given the special nature of the resources procured on the islands). In particular, the resolution envisages that Terna:

- defines the minimum technical and functional requirements of the plant at the withdrawal points;
- defines the minimum performance required for the resources which can be reduced instantaneously, with reference to the power which can be reduced instantaneously and the modality for the verification by Terna of such performance;
- assigns the service by means of descending price bidding procedures, starting from the annual amount of 300,000 €/MW/year (value which corresponds to double the annual rate for the service of instantaneous interruptibility);
- recognises a variable remuneration of 3,000 €/MW for the reductions exceeding 20 per year;
- arranges for and forwards to AEEG for approval, the notification and related contract and updates urgently, outside the ordinary update procedures, the Grid Code.

With Resolution ARG/elt 19/10, the Authority has approved with certain additions the Regulations governing the competitive procedures for the procurement of resources that can be reduced instantly, together with the standard contract prepared by Terna pursuant to Resolution ARG/elt 15/10.

### ARG/elt Resolution 19/10

With this decision, the Authority has approved, with a few integrations, the Regulation concerning the tendering procedures for the supply of the resources which can be reduced instantaneously and the related contractual scheme arranged by Terna pursuant to the Resolution ARG/elt 15/10. In particular, the resolution foresees that Terna's proposal is integrated for:

- including adequate regulations free of charge for the operators in the event of inefficiencies, of any kind, of the service of load instantaneous reduction;
- allowing the widest possible adhesion of the subjects capable of providing the service and that, in particular:
  - admission to the competitive procedures of those end-customer sites with medium voltage connections that are able to offer a service with at least the minimum effectiveness characteristics identified by Terna;
  - express inclusion in the competitive procedures of end-customer sites that are not connected to the grid with an obligation to connect third parties.



#### **ARG/elt Resolution 28/10**

With this decision, the Authority has verified the full compliance of Terna to the conditions for accessing the reward for the activities related to the reduction of volumes moved on the ancillary services market, quantifying the reward to be recognised to Terna on the basis of the incentives scheme for the supply of resources for the service of energy dispatching for 2009 regulated by AEEG Resolution no. 351/07 of 29 December 2007.

In particular, Terna will receive incentives of €40 million via update of the DIS component for 2011.

#### **ARG/elt Resolution 32/10**

With this decision, the Authority has postponed to 1 July 2010 the effectiveness of the mitigation services provided by the distribution companies for the continuity in the event of outages which affect plant directly connected to the National Transmission Grid, in accordance with article 10 of Annex A to the AEEG Resolution no. 341/07 of 27 December 2007. Contextually, the Authority has started a procedure for the definition of the management modalities of the items related to the mitigation services.

#### **ARG/elt Resolution 38/10**

With this decision, the Authority has modified Resolution ARG/elt 90/09, by foreseeing that, for the purposes of implementing Resolutions no. 27/99, no. 42/02 and no. 188/06, CIP 6 generation units and/or units producing both electricity and heat that are not authorised for dispatching, for which Terna has established generation restrictions for the purpose of ensuring the operational safety of the national electrical system, may exclude the period to which the generation restrictions imposed and the generation limitation refer, as such restrictions are outside the control of the generators.

With regard to Terna, by 31 January of each year, the Company must send the producer, the dispatching user, the GSE and the Authority, a register of production obligations for each production unit concerned.

#### **ARG/elt Resolution 50/10**

By this resolution, the Authority has introduced modifications and additions to the combined text for the monitoring of the wholesale electricity market and the dispatching services market (TIMM), referred to in Resolution ARG/elt 115/08.

In particular, with this resolution, the Authority:

- reserves the right to introduce an incentives mechanism for rewarding Terna for the realisation of activities which are deemed strategic by the Authority, by set deadlines;
- states the modality for covering costs related to performing monitoring activities and potential rewards related to the previous year which will be included in the DIS of the following year;
- modifies Annex B of TIMM for keeping into account the market reform for the dispatching service;
- requires Terna to create a simulator of the dispatching services market in order to carry out what-if analyses at the planning stage.

#### **ARG/elt Resolution 51/10**

With this decision, the Authority has modified Resolution ARG/elt 179/09, for keeping into account the regulations of art. 2 of Law Decree no. 3 of 25 January 2010, as converted into Law 41 dated 22 March 2010.

This resolution modifies the provisions of Resolution 179/09 in order to make them applicable to the parties selected for the financing of interconnectors under the competitive procedures organised by Terna pursuant to art. 2 of Law 41/10, and defines the fees for virtual interconnection across the border with Austria, making it the same as that for the borders with Slovenia and France (35,000 €/MW/year) given the technical similarities of the link.

The parties selected under the new competitive procedures may make use of the virtual importation service from 1 April 2010, and, to this end, must sign a contract with Terna for such virtual importation service.

#### **ARG/elt Resolutions 52/10 and 66/10**

By these resolutions, having considered the opinion of the Ministry for Economic Development, the Authority has identified the internal usage grids pursuant to art. 33 of Law 99 dated 23 July 2009. In particular, two lists have been defined:

1. a list of electricity grids classifiable as internal usage grids pursuant to Law 99/09, which include those grids with an obligation to connect third parties, since it was deemed appropriate to safeguard and not discriminate against long-established entrepreneurial situations, principally in the chemicals sector. In this regard, the Authority has clarified that the inclusion of these grids in the list of internal usage grids does not exonerate their operators from the obligation to connect third parties;
2. a list of electricity grids that do not meet the requirements for being internal usage grids established by Law 99/09, which include the internal grids of self-producers, being those grids that connect units of production and consumption that are owned by the same legal entity or the same group of companies.



### ARG/com Resolution 57/10

By this resolution, the Authority has introduced certain modifications to Resolution 11/07 and the related attachment (the Unbundling text), in order to comply with the rulings of the Council of State following the appeals filed against Resolution 11/07. In accordance with these rulings, the resolution essentially envisages that:

- a vertically-integrated company may manage at the same time, without any obligation for functional unbundling, the activities of transmission, dispatching, distribution and metering of electricity, since the Council of State considered unjustified the inclusion of metering activities in the list of activities for which functional unbundling is required;
- the components of the independent operator, for all activities covered by art. 7.1 (activities requiring functional unbundling) comprise: the directors, or the members of the operating board, and the senior managers (i.e., general managers and key managers).

The resolution also:

- repeals Resolution ARG/com 132/08, which established guidelines for preparation of the compliance programme by the independent operator;
- envisages the exemption of vertically-integrated companies from specific requirements for functional unbundling when they provide the service solely via the use of infrastructure exempted from the requirement to allow third parties access to 100% of the capacity;
- envisages certain exceptions to the functional unbundling requirements. In particular, the resolution allows joint management, without a requirement for functional unbundling, of the activities referred to in art. 7.1 of the Unbundling text, as well as:
  - a) foreign activities, when they relate solely to the same activities referred to in art. 7.1 of the Unbundling text carried out in Italy;
  - b) other activities, on condition that they are carried out under concession and/or relate to public service monopolies that use grid infrastructure;
- corrects certain errors of substance and makes additions and changes to parts V and VI of the Unbundling text regarding the requirements for accounting unbundling.

### ARG/elt Resolution 59/10

By this resolution, following an appeal to the Lombardy Administrative Court against certain provisions contained in Resolution 348/07 and while awaiting a ruling from the Council of State, the Authority establishes as a transitional exception to the provisions of Resolution 348/07, for the years of the regulatory period 2008, 2009 and 2010 and solely for users with a nominal power in excess of 220 kV, that the p3(disAT) component is not applied to cover the cost of the high voltage distribution service referred to in art. 6 of the TIT and that a specific tariff component, TRASprov, is applied to cover the cost of the transmission service. The TRASprov component for the years 2008, 2009 and 2010 takes the values of, respectively, 0.282, 0.298 and 0.336 eurocents per kWh.

The lower revenue deriving from the introduction of this transitional arrangement will be offset by the electricity sector's equalisation fund, using the general compensation mechanisms envisaged in Resolution 348/07.

### GOP Resolution 19/10

By this resolution, the Authority has established the contribution for the functioning of the Authority in 2010. In particular, by this resolution the Authority:

- confirms the 2010 contribution to the Authority's functioning costs, pursuant to Law 481 dated 14 November 1995, and subsequent amendments and additions, as 0.03 percent of the revenue reported in the approved 2009 financial statements of the parties operating in the relevant sectors;
- establishes that the contribution from parties operating in the electricity and gas sectors be paid by 31 July 2010;
- establishes that, by 15 September 2010, the parties required to pay the contribution shall send information about such contribution to the Authority, using the electronic communication system introduced in Resolution GOP 35/08.

### ARG/elt Resolutions 65/10, 121/10 and 187/10

By these resolutions, with regard to the competitive procedures for assignment of the interconnector capacity referred to in art. 2, paragraph 1 of Law Decree 3 dated 25 January 2010, as converted into Law 41 dated 22 March 2010, Terna is given specific instructions designed to ensure the actual availability to the system of additional interruptible resources. In particular, the Authority has considered it appropriate for:

- Terna to re-determine the guarantees required from participants in the competitive procedure for the financing of the interconnector on the basis indicated in the resolution;
- Terna to check that the projects presented with reference to loads different to those who already provide the instantaneous interruption service, are able to guarantee provision of the instantaneous interruption service for the specified loads in accordance with the regulatory requirements;
- Terna to send the Authority a detailed report on the above-mentioned checks;
- Terna to assign the quotas for the financing of the interconnection with Austria with priority assignment in two successive steps:

- temporary assignment solely to those parties who already provide an instantaneous interruption service and which are additional to those assigned at 31 December 2007;
- re-assignment by 30 November 2010, to the parties included in the point above and to those parties who commit to making an instantaneous interruption service available by 31 March 2011, and which pass the checks mentioned above; The terms and conditions for this assignment were subsequently amended by Resolution ARG/elt 187/10.

Lastly, the resolution envisages that any differences incurred by Terna shall be settled via the uplift fee.

By Resolution ARG/elt 121/10, the Authority also established that by 15 November 2010 for subjects who have applied to take part in the above procedure (500 MW) should confirm the unconditional commitment to make available the “future” interruptible resources on the basis of which the request was made.

### **ARG/elt Resolutions 55/10 and 77/10**

By these resolutions, in the context of activities to monitor the wholesale electricity market and the dispatching services market (TIMM), the Authority has:

1. quantified as €454,200 the costs incurred by Terna in 2009 on performing the activities associated with the monitoring function; such costs are covered by the fee recognised for the coverage of Terna's 2011 operating costs determined by the Authority pursuant to art. 3 of Resolution ARG/elt 351/07 (DIS 2011).
2. approved the plans for the data warehouse project, the plan for the dispatching service market simulator and the plan for the fuel consumption platform project, directing Terna to prepare user manuals for each project.

### **ARG/elt Resolution 87/10**

This resolution from the Authority strengthens the incentives for the activation of new transmission infrastructure considered strategic for the development of competition. In particular, the Authority has introduced an optional incentive mechanism that uplifts the remuneration of construction in progress on strategic works (those included in category I3 of Resolution 348/07), on condition that a subset of such works enters into service by the established date.

### **ARG/elt Resolution 99/10**

By this resolution, the Authority has given instructions for the incentive regulation of the quality of the electricity transmission service and governing the mitigation services provided by distributors to ensure continuity, pursuant to Attachment A of Resolution 341/07 dated 27 December 2007, with reference to:

- the scope of application of the rules for transmission service quality;
- the definition and remuneration of the mitigation services.

In relation to the first aspect, the TELAT grid has been excluded from the application of the incentive regulation of the quality of the transmission service until the end of the current regulatory period.

With regard to the governance of mitigation services, the resolution envisages:

- the remuneration of mitigation services on a decreasing basis with reference to the duration of the interruption and differentiating between transformation plants connected directly or indirectly to the NTG at 31 December 2008;
- a specific “ceiling” on Terna's total payments for mitigation service fees and a “ceiling” for each interruption;
- exclusion from the application of mitigation services of interruptions due to force majeure, external factors or insufficient resources;
- neutralisation of the mitigation services for problems originated by certain configurations of the TELAT grid (radial grid configurations), up to the alternative supply of 90% of end customers;
- a mechanism of deductions from the remuneration of mitigation services if the distributor does not open/close the power lines using remote systems for the control of the procedures;
- specific disclosure requirements for distributors in order to be remunerated for the service.

### **ARG/elt Resolution 103/10**

By this resolution, the Authority has introduced modifications and additions to Attachments A (TIT) and B (TIC) of Resolution 348/07 and to Resolution ARG/elt 67/10, as well as transitional arrangements for temporary connections to the distribution grids, with particular reference - as far as Terna is concerned - to the following aspects:

- payment of grid transmission fees on station ancillary services. Given that pursuant to art. 16.4 of the TIT, the withdrawal of electricity to fuel ancillary generation services are excluded from the application of transmission and distribution fees, while each distributor, pursuant to arts. 13 and 14 of the TIT, makes payments deriving from the charging of grid transmission fees in relation to quantities of electricity that do not take account of the above exemption, the resolution envisages that this lower revenue for the distributor shall be offset as part of the equalisation mechanism for the distribution costs applying to the medium and low-voltage grids, referred to in art. 38 of the TIT, and that such offset be recognised from the first year of application of the exemption, which was 2008;
- possibility for the owner of a withdrawal point to waive part of the power available, although such waiver will not give a right to the return of the connection fee already paid for the previous level of power available, while any subsequent requirements to increase the power will be subject to the application of a connection fee that includes the level of power previously waived. To this end, the definition of available power referred to in art. 1.1 of the TIT has been modified.

### ARG/elt Resolution 112/10

With this resolution the Authority defined, on the basis of a proposal elaborated by Terna, the Index of Reliability “IA” for the purposes of calculating the failure to generate wind power. The definition of said index was set out by Resolution ARG/elt 5/10, with which the Authority dictated new methods of remuneration for failure by wind farms to produce energy due to the implementation of dispatching orders imposed by Terna to ensure the safety of the electrical system. The IA index is an indicator of the level of reliability of the dispatching user, in relation to a determined wind power production unit, in complying with the dispatching orders issued by Terna; this is valid only for the purposes of calculating the failure to produce wind power, notwithstanding the provisions of the Network Code in relation to the consequences arising from failure to comply with Terna’s dispatching orders.

### ARG/elt Resolution 124/10

With this resolution the Authority has set up a system for the Management of Production Plants and Units’ Unique Data (GAUDI) and for the rationalisation of information flows between the various subjects operating in the sector of electricity production. The resolution contains instructions for:

- a) the rationalisation of information flows between the various subjects operating in the electricity sector, aimed at simplifying process and reducing the tasks arising from electricity operators’ information obligations;
- b) the completion of the process, started with Resolution ARG/elt 205/08, to set up a unique data system at national level for electricity production plants and relative production units, which would allow production plants to be identified unequivocally;
- c) the integration, within GAUDI, of a control panel that can highlight the sequence of phases that characterise the processes of network connection and admission to the electricity market.

### ARG/elt Resolutions 125/10 and 173/10

With this resolution the Authority has introduced changes and additions to the Authority for Electricity and Gas’s Resolution ARG/elt 99/08 in matters of technical and economic conditions for grid connection, with the obligation of connecting third parties to production plants (TICA), also in order to manage more profitably the applications for connection and accepted estimates, reducing possible instances of occupying the grid’s transport capacity in the absence of the concrete realisation of the electricity production plant.

The main new features introduced by the resolution can be summarised as follows:

- the preparation by Terna and distributing companies with at least 100,000 customers, by 30 June 2011, of a computer portal aimed at managing the complementary connection procedure to the system implemented by Terna for the purpose of the so-called “GAUDI” system;
- the definition and publication, by 30 June 2011, by Terna and the distribution companies with at least one primary booth, of the atlases relating respectively to the grids in high, very high voltage and primary HV/MV booths in order to provide quality indications on the availability of production capacity;
- the possibility for Terna of activating open season procedures in critical areas covering six-month periods, in order to allow for a joint analysis of more than one request for connection and consequently plan the necessary grid development more appropriately;
- the forecast for further hypotheses of forfeiture of estimates presented;
- the definition by Terna of specific technical and economic conditions in the event of connections of production plants to the NTG with voltage levels of below 220 kV;
- the introduction of a “guarantee for the booking of additional capacity” over and above that already forecast upon payment of connection fees, in the form of a caution deposit or bank security guarantee, for requests for connections in critical areas or on critical lines.

With Resolution ARG/elt 173/10, the Authority approved Terna’s proposal incorporating the methodology by which to define critical areas and critical lines in high and extremely high voltage, prepared in accordance with article 4.2 of Attachment A to Resolution ARG/elt 125/10.

By order of the Regional Administrative Court of Lombardy, filed on 13 January 2011, whilst awaiting sentencing, the effects of Resolutions ARG/elt 125/10 and 173/10 have been suspended as regards to parts concerning financial guarantees.

### ARG/elt Resolution 126/10

By this provision, the Authority has made changes and supplements to AEEG Resolution no. 88/07 of 11 April 2007, establishing that, with effect as from 1 January 2011.

Terna, as subject responsible for the collection, validation and registration of electricity inserted relatively to the points of input located on its own grid, becomes responsible for the same activities in the measure of the electricity produced in case of several production plants with nominal power exceeding 20 kW that share a single concession point, or in the case in which this is functional to the correct implementation of current regulations.



### ARG/elt Resolution 129/10

With this resolution the Authority introduced changes and additions to the instructions as per Attachment A to the Authority for Electricity and Gas's Resolution 30 July 2009 ARG/elt 107/09 (Combined settlement text, TIS) setting out, amongst other things, specific registration and archival obligations, for a minimum of 5 years, of the data communicated by the distributors to Terna, pursuant to articles 37 and 38 of the TIS; it also sets out that Terna establish and notify the distributors of the characteristics of unique identification and traceability of the data communicated by the distributors of reference, also requiring Terna to add such provisions to the Network Code.

The same resolution, from 1 January 2011:

- eliminates the fee for aggregating the input measures paid by each dispatching user to Terna to take account of the fact that said service is already remunerated through the DIS component;
- it confirms distributors' pooling for the purposes of aggregation of measures, eliminating the pooling of work of subjects identified with public evidence procedures starting from 2011;
- re-determines the measurement aggregation fees;
- it introduces premiums and penalties to be applied to distributors on the basis of compliance with the performance parameters of effectiveness and efficiency of collection aggregation;
- it introduces a system of automatic indemnities to be recognised to dispatching users connected to the fulfilment of distributors' information obligations in the context of measure aggregation.

### ARG/elt Resolution 130/10

With this resolution the Authority approved, with some changes, Terna's proposal for NTG development pursuant to paragraph 11.2 of the Authority for electricity and gas's Resolution 11 June 2008, ARG/elt 87/10 (milestone), relative to the extra remuneration mechanism for works in progress relative to development work of category I3 for the period 2010-2011 (Resolution ARG/elt 87/10).

### ARG/elt Resolutions 143/10 and 243/10

By these provisions, the Authority has expressed an opinion on the Market Coupling project for the interconnection of Italy-Slovenia as from 1 January 2011. More specifically, by Resolution ARG/elt 143/10, it approved the approved the Master Agreement scheme prepared between network operators and Italian and Slovenian electricity markets, including objectives and criteria to manage congestion on the Italy-Slovenia interconnection through a mechanism of Market Coupling, setting out that:

- for 2011, financial income and expense deriving from Terna exercising the role of "shipping agent" shall be ascribed separately and respectively to increase and reduce the fee as per article 44 of Resolution 111/06;
- income from the implementation of Market Coupling on the Slovenia-Italy interconnection to assign the capacity of daily interconnection for 2011 and due to Terna shall be used to reduce the fees to access the grid for all the national electrical system's final users through reducing the fee for providing the resources to the market for dispatching services as per article 44 of Resolution 111/06, maintaining separate evidence of the various financial items that concur to its determination.

By **Resolution ARG/elt 243/10** the Authority approved the "Pentalateral Agreement" scheme setting out the operative procedures aiming to implement Market Coupling between Italy and Slovenia. The resolution also establishes that all financial income/expense accrued by Terna by virtue of its role as Shipping Agent shall be calculated by Terna on the basis of the same interest rate used to define the uplift, and that Terna shall be released of all charges and costs relating to the implementation of market coupling and connected to the role of shipping agent.

### ARG/elt Resolution 160/10

With this resolution the Authority approved Terna's proposal, including the Regulation for virtual importation auctions as per the Authority for Electricity and Gas's Resolution 20 November 2009 ARG/elt 179/09 for 2011.

### ARG/elt Resolutions 161/10, 222/10 and 247/10

With these measures, the Authority amended Resolution no. 111/06 with regard to plants essential to electricity system security. Specifically, the Authority has:

- amended the criteria by which to determine the fees to be recognised to said plants, considering it appropriate to standardise, as far as possible, the criteria and procedures for determining fees (Resolution ARG/elt 161/10);
- approved Terna's proposals with regards to the definition of some variable cost items recognised for 2011, also amending the criteria for preparing bids on the market of the energy for essential plants (Resolutions ARG/elt 222/10 and 247/10);
- made their decisions with regards to the application to be admitted to the regime for the re-integration of costs presented by dispatching users in accordance with article 63, paragraph 63.11 of Attachment A to Resolution no. 111/06 for 2011 and thereon, approving the requests for admission to the re-integration of costs of the essential plants included on the list published by Terna (Resolution ARG/elt 247/10).

### **ARG/elt Resolutions 162/10 and 210/10**

With this resolution the Authority defined, on the basis of the elements provided by Terna, its decision in fulfilment of provisions as per art. 65-bis, paragraph 65-bis.3, of the Authority's Resolution 9 June 2006 111/06 in the matter of the contracting of plants essential for safety (alternative methods to absolve the obligations of offer deriving from owning essential plants). These elements are transmitted from the Authority to the interested operators and Terna.

### **ARG/elt Resolution 166/10**

By this resolution, the Authority has amended and supplemented Attachment A to AEEG Resolution no. 48/04 of 27 March 2004 on further payments for the remuneration of available production capacity pursuant to article 36 of the attachment. The main change in the calculation method consists of considering the difference between the market prices of the various areas and territorial distribution of operator production capacity in order to provide support to producers with plants situated mainly in market areas featuring an excess supply or export constraints, and encourage a suitable supply of electricity in the national grid system.

### **Resolution ARG/elt 172/10 and decision by the Markets director of 16 December 2010**

By Resolution ARG/elt 172/10, the Authority instructed Terna on the supplements to the Grid Code concerning applicative rules for the governance of settlement and the determination of the uplift fee with amendments and supplements to Attachment A to AEEG Resolution no. 111/06 of 9 June 2006 and Attachment A to Resolution ARG/elt 107/09 of 30 July 2009 (Combined Settlement Text, TIS). More specifically, this resolution:

- amended the interest rate to be applied in order to determine the uplift fee – establishing it as Euribor 12 months increased by 1%;
- considers the conclusive proposal of the forum conducted by Terna with the operators on the completion of the update and maintenance rules of the code identifying points of distribution (POD) as having been positively checked and establishes that Terna shall update and supplement the Grid Code with this proposal;
- establishes that as from 1 April 2011, Terna shall publish and keep up-to-date on its website, a list of distributor companies and the related identification codes, in addition to the historical record of corporate changes;
- requires Terna to present a proposed supplement to the Grid Code, no later than 30 June 2011, incorporating applicative rules of the settlement regulation in cases where the ownership structure of the distribution grids should change, in accordance with the methods subsequently defined by the Decision of the Market Management Director on 16 December 2010.

### **ARG/elt Resolution 180/10**

By this resolution, the Authority approved the proposal presented by Terna on the definition of the items for calculating the variable cost recognised to essential plants, at the same time amending the definition of some variable cost items recognised.

### **ARG/elt Resolution 181/10**

By this resolution, the Authority has defined the conditions for the supply of incentive tariffs in effect as from 1 January 2011 for photovoltaic production (the "Third Energy Account").

With reference to the measurement of electricity produced, this resolution, confirming that already envisaged by Resolution no. 90/07 for the previous incentive regime, establishes that Terna shall provide the GSE with records of measurements:

- of the electricity produced, should Terna be responsible for the collection, validation and registration in accordance with Resolution 88/07;
- of the electricity emitted, as the party responsible for the collection, validation and registration in accordance with the TIT.

### **ARG/elt Resolution 186/10**

By this resolution, the Authority has specified the volumes of electricity taken as reference for the purpose of determining the transmission tariffs for 2009 and relevant for the revenue level guarantee mechanism recognised for the transmission service in accordance with article 4 of AEEG Resolution ARG/elt 188/08 of 19 December 2008.

On the basis of the difference between total energy volumes for 2009 and the reference volumes specified, the economic items have thus been determined as guarantee of the revenue recognised to the transmission service, for a total amount of €56,326,693.



#### **ARG/elt Resolutions 187/10 and 212/10**

By this resolution, the Authority issued provisions regarding Terna's procedures for the forward provisioning of interruptible resources for 2011-2013.

In general terms, the provision confirms the regulation of the interruptibility service in force in the previous three-year period, but alters the assignment mechanism to adjust it to the provisions of Law 99/09 and 41/10. More specifically, the resolution establishes that the service shall be allocated through lowest-bid procedures starting from a reserve rebate of 150,000 €/MW/year in the event of instant interruptibility and 100,000 €/MW/year in the event of emergency interruptibility with the assignment of the marginal rebate in the event of a quantity required that is above that available or, vice versa, the marginal rebate.

The resolution also establishes:

- the provisioning of instantly and emergency interruptible resources for preference, for the entire period 2011-2013. Any quantities not provisioned through three-year contracts must be provisioned through progressively shorter contracts;
- an assignment "reserved" to principals of instantly interruptible resources who have presented a request to participate in the financing of the interconnector on the Austrian border (500 MW). On the basis of that established by the resolution, Terna has defined and transmitted a proposed regulation to the Authority, for the procedures of assignment and contractual layout for the supply of the interruptibility service. The proposed regulation was subsequently approved by Resolution ARG/elt 212/10.

#### **ARG/elt Resolution 211/10**

By this resolution, the Authority has:

- issued a favourable assessment of the proposed Attachments A.54 and A.66 to the Grid Code, prepared by Terna in accordance with Resolution ARG/elt 99/10 and respectively incorporating "Classification and registration of energy not supplied to users directly and indirectly connected to the NTG" and "Procedure for determining mitigation services to distributor companies";
- asked Terna to supplement the proposed amendment of the Grid Code - prepared by Terna S.p.A. in order to implement, as from 1 January 2011, the supplement, in functional terms, of the infra-day energy market with the Ancillary Services Market - and to send the Authority this new proposed amendment of the Grid Code, for verification of compliance, with it being forecast that the new proposed amendment of the Grid Code will be issued with a favourable assessment once terms of 10 days have expired as from its receipt, with no notice to the contrary having been provided. The new proposal sent by Terna has been approved by tacit assent.

#### **ARG/elt Resolution 221/10**

By this resolution, the Authority has approved Terna's proposal to implement the competitive procedure for the assignment of instruments to hedge the risk of volatility of fees for the assignment of transport capacity (CCC) for 2011.

#### **ARG/elt Resolution 228/10**

With Resolution ARG/elt 228/10, the Authority has established the update of transmission tariffs for 2011. In particular:

- the grid transmission fee item for transmission services for distribution companies has gone from 0.388 to 0.416 €/kWh;
- the grid transmission fee elements\* pursuant to paragraph 13.3 of the TIT have gone from 0.0510 to 0.0512 c€/kWh, including the application of the revenue guarantee mechanism introduced by Resolution 188/08.

#### **ARG/elt Resolution 230/10**

By this resolution, the Authority has recognised the covering of costs estimated for 2010 and 2011 for the performing of activities associated with the monitoring function pursuant to article 3, paragraph 3.2 of AEEG Resolution 115/08 of 5 August 2008.

#### **ARG/elt Resolution 231/10**

By this resolution, the Authority has updated the amount of fees pursuant to articles 45, 46, 48 and 73 of Resolution no. 111/06 for 2011, to be paid by users of withdrawal dispatching, also establishing the update of the DIS fee to cover Terna's operating costs pursuant to article 46 of Resolution 111/06, established as 0.0308 c€/kWh.

#### **ARG/elt Resolution 241/10**

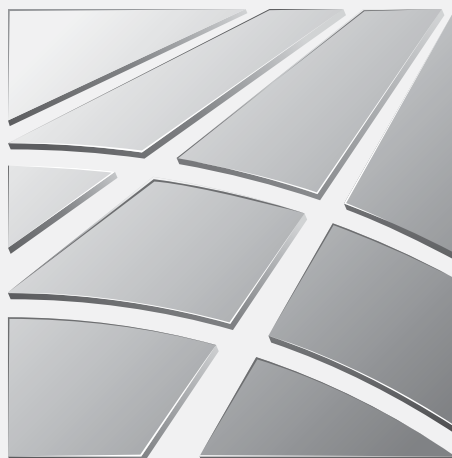
By this resolution, the Authority has issued provisions for 2011 on the management of congestion in imports and exports on the interconnection grid with abroad and, specifically:

- has approved the Access Rules prepared jointly by Terna and the other grid managers participating in the forum set up under the scope of the regional initiative for Central-South Europe headed by ERGEG;
- for 2011, has defined provisions on the management of congestion in imports and exports on the interconnection grid with abroad;
- has approved the regulation scheme prepared by Terna, containing the applicative methods by which to manage congestion on the interconnection grid for 2011;
- has asked Terna to send detailed information on the operative costs of the company CASC S.A. to which, in 2011, the role of Auction Operator has been entrusted.









Consolidated financial statements  
as at and for the year ended 31 December 2010

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## Consolidated financial statements

## Consolidated income statement

| In millions of euros   | Note      | 2010                           | 2009                           |
|--|-----------|--------------------------------|--------------------------------|
| <b>A. Revenue</b>  |           |                                |                                |
| 1. Revenue from sales and services<br><i>of which: related parties</i>   | 1         | 1,533.1<br>1,359.0             | 1,346.8<br>1,270.4             |
| 2. Other revenue and income<br><i>of which: related parties</i>  | 2         | 56.1<br>2.7                    | 43.4<br>2.1                    |
| <b>Total revenue</b>   |           | <b>1,589.2</b>                 | <b>1,390.2</b>                 |
| <b>B. Operating expenses</b>   |           |                                |                                |
| 1. Raw materials and consumables<br><i>of which: related parties</i>   | 3         | 28.2<br>0.1                    | 12.4<br>0.1                    |
| 2. Services<br><i>of which: related parties</i>  | 4         | 152.2<br>7.5                   | 149.7<br>8.2                   |
| 3. Personnel expense<br>- <i>personnel expense, gross</i><br>- <i>personnel expense, capitalised</i><br><i>of which: related parties</i> | 5         | 212.2<br>276.5<br>-64.3<br>3.6 | 185.5<br>244.1<br>-58.6<br>3.4 |
| 4. Amortisation, depreciation and impairment losses  | 6         | 360.7                          | 326.6                          |
| 5. Other operating expenses<br><i>of which: related parties</i>  | 7         | 21.5<br>0.2                    | 21.6<br>0.6                    |
| <b>Total operating expenses</b>  |           | <b>774.8</b>                   | <b>695.8</b>                   |
| <b>A-B Operating profit</b>  |           | <b>814.4</b>                   | <b>694.4</b>                   |
| <b>C. Net financial expense</b>  |           |                                |                                |
| 1. Financial income<br><i>of which: related parties</i>  | 8         | 11.2<br>0.0                    | 29.2<br>3.1                    |
| 2. Financial expense<br><i>of which: related parties</i>   | 8         | -116.3<br>1.3                  | -180.4<br>1.2                  |
| 3. Share of profit/(losses) of equity-accounted investees  | 9         | 2.6                            | 2.9                            |
| <b>D. Pre-tax profit</b>   |           | <b>711.9</b>                   | <b>546.1</b>                   |
| E. Income taxes  | 10        | 245.2                          | 192.1                          |
| <b>F. Profit from continuing operations</b>  |           | <b>466.7</b>                   | <b>354.0</b>                   |
| <b>G. Profit from discontinued operations and assets held for sale</b>   | <b>11</b> | <b>146.9</b>                   | <b>417.0</b>                   |
| <b>H. Profit for the year</b>  |           | <b>613.6</b>                   | <b>771.0</b>                   |
| <b>Profit for the year attributable to the owners of the Parent</b>  |           | <b>613.6</b>                   | <b>771.0</b>                   |
| <b>Profit for the year attributable to non-controlling interests</b>   |           | <b>0.0</b>                     | <b>0.0</b>                     |
| <b>Earnings per share</b>  |           |                                |                                |
| Basic earnings per share   | 12        | 0.306                          | 0.385                          |
| Diluted earnings per share   |           | 0.305                          | 0.384                          |
| <b>Earnings per share of continuing operations</b>   |           |                                |                                |
| Basic earnings per share   | 12        | 0.233                          | 0.177                          |
| Diluted earnings per share   |           | 0.232                          | 0.176                          |

## Consolidated statement of comprehensive income

| In millions of euros   | Note | 2010         | 2009         |
|--|------|--------------|--------------|
| <b>Profit for the year</b>   |      | <b>613.6</b> | <b>771.0</b> |
| Other comprehensive income of the year   |      |              |              |
| - Cash flow hedges net of tax effect of continuing operations                            | 23   | 25.9         | -11.9        |
| - Cash flow hedges net of tax effect of discontinued operations and assets held for sale | 23   | 16.0         | 0.0          |
| - Translation of financial statements of foreign operations                              | 23   | 0.0          | 3.4          |
| <b>Comprehensive income of the year</b>  |      | <b>655.5</b> | <b>762.5</b> |
| <b>Comprehensive income attributable to:</b>   |      | <b>655.5</b> | <b>762.5</b> |
| <i>Owners of the Parent</i>  |      | 655.5        | 762.5        |
| <i>Non-controlling interests</i>   |      | 0.0          | 0.0          |

# Consolidated statement of financial position

## Assets

| In millions of euros                                       | Note | at 31 Dec. 2010 | at 31 Dec. 2009 | at 1 Jan. 2009 |
|--|------|-----------------|-----------------|----------------|
| <b>A. Non-current assets</b>                               |      |                 |                 |                |
| 1. Property, plant and equipment                           | 13   | 7,802.6         | 6,989.9         | 5,952.6        |
| <i>of which: related parties</i>                           |      | 39.0            | 30.3            | 21.1           |
| 2. Goodwill  | 14   | 190.2           | 190.2           | 203.9          |
| 3. Intangible assets                                       | 15   | 280.4           | 267.4           | 362.5          |
| 4. Deferred tax assets                                     | 27   | 0.0             | 0.0             | 127.0          |
| 5. Equity-accounted investees                              | 16   | 23.6            | 15.5            | 38.2           |
| 6. Non-current financial assets                            | 17   | 200.8           | 123.2           | 115.5          |
| 7. Other non-current assets                                | 18   | 6.3             | 5.5             | 5.5            |
| <b>Total non-current assets</b>                            |      | <b>8,503.9</b>  | <b>7,591.7</b>  | <b>6,805.2</b> |
| <b>B. Current assets</b>                                   |      |                 |                 |                |
| 1. Inventories   | 19   | 11.4            | 11.7            | 17.7           |
| 2. Trade receivables                                       | 20   | 1,495.8         | 1,169.1         | 1,730.4        |
| <i>of which: related parties</i>                           |      | 153.7           | 120.8           | 102.3          |
| 3. Current financial assets                                | 17   | 0.5             | 501.0           | 6.9            |
| <i>of which: related parties</i>                           |      | 0.4             | 0.5             | 0.2            |
| 4. Cash and cash equivalents                               | 21   | 150.1           | 0.1             | 779.7          |
| 5. Tax assets  | 22   | 16.8            | 18.4            | 25.9           |
| 6. Other current assets                                    | 18   | 20.3            | 27.6            | 28.9           |
| <i>of which: related parties</i>                           |      | 0.8             | 1.5             | 0.1            |
| <b>Total current assets</b>                                |      | <b>1,694.9</b>  | <b>1,727.9</b>  | <b>2,589.5</b> |
| <b>C. Discontinued operations and assets held for sale</b> |      |                 |                 |                |
|  | 30   | <b>575.8</b>    | <b>0.1</b>      | <b>0.0</b>     |
| <b>Total assets</b>  |      | <b>10,774.6</b> | <b>9,319.7</b>  | <b>9,394.7</b> |



# Consolidated statement of financial position

## Liabilities and equity

| In millions of euros  | Note | at 31 Dec. 2010 | at 31 Dec. 2009 | at 1 Jan. 2009 |
|---|------|-----------------|-----------------|----------------|
| <b>D. Equity attributable to the owners of the Parent</b>                   |      |                 |                 |                |
| 1. Share capital  |      | 441.0           | 440.2           | 440.2          |
| 2. Other reserves   |      | 791.0           | 758.7           | 771.3          |
| 3. Reserves for assets held for sale  |      | 16.0            | 0.0             | 0.0            |
| 4. Retained earnings  |      | 1,059.4         | 671.7           | 656.3          |
| 5. Interim dividend   |      | -160.4          | -140.1          | -118.5         |
| 6. Profit for the year  |      | 613.6           | 771.0           | 327.5          |
| <b>Total equity attributable to owners of the Parent</b>                    | 23   | <b>2,760.6</b>  | <b>2,501.5</b>  | <b>2,076.8</b> |
| E. Equity attributable to non-controlling interests                         |      | 0.2             | 0.0             | 86.9           |
| <b>Total equity</b>   |      | <b>2,760.8</b>  | <b>2,501.5</b>  | <b>2,163.7</b> |
| <b>F. Non-current liabilities</b>   |      |                 |                 |                |
| 1. Long-term loans  | 24   | 5,147.5         | 4,199.2         | 3,955.3        |
| 2. Employee benefits  | 25   | 122.3           | 125.1           | 153.9          |
| 3. Provisions for risks and charges   | 26   | 171.6           | 149.4           | 81.6           |
| 4. Deferred tax liabilities   | 27   | 330.3           | 363.8           | 316.5          |
| 5. Non-current financial liabilities  | 24   | 47.1            | 82.6            | 66.7           |
| 6. Other non-current liabilities  | 28   | 141.8           | 151.6           | 407.6          |
| <i>of which: related parties</i>  |      | 0.0             | 0.0             | 0.8            |
| <b>Total non-current liabilities</b>  |      | <b>5,960.6</b>  | <b>5,071.7</b>  | <b>4,981.6</b> |
| <b>G. Current liabilities</b>   |      |                 |                 |                |
| 1. Short-term loans   | 24   | 73.1            | 40.0            | 160.2          |
| 2. Current portion of long-term loans                                       | 24   | 59.7            | 59.7            | 79.0           |
| 3. Trade payables   | 29   | 1,542.2         | 1,482.0         | 1,880.6        |
| <i>of which: related parties</i>  |      | 55.7            | 39.3            | 52.2           |
| 4. Tax liabilities  | 29   | 69.6            | 44.0            | 1.8            |
| 5. Current financial liabilities  | 24   | 24.2            | 25.5            | 34.0           |
| <i>of which: related parties</i>  |      | 2.4             | 1.2             | 0.0            |
| 6. Other current liabilities  | 29   | 135.7           | 95.3            | 93.8           |
| <i>of which: related parties</i>  |      | 7.8             | 4.6             | 7.0            |
| <b>Total current liabilities</b>  |      | <b>1,904.5</b>  | <b>1,746.5</b>  | <b>2,249.4</b> |
| <b>H. Liabilities from discontinued operations and assets held for sale</b> | 30   | <b>148.7</b>    | <b>0.0</b>      | <b>0.0</b>     |
| <b>Total liabilities and equity</b>   |      | <b>10,774.6</b> | <b>9,319.7</b>  | <b>9,394.7</b> |

# Statement of changes in consolidated equity

31 DECEMBER 2009 – 31 DECEMBER 2010

CONSOLIDATED SHARE CAPITAL AND RESERVES

|   | Share/quota<br>capital | Legal<br>reserve | Share<br>premium<br>reserve | Hedging<br>reserve |
|---|------------------------|------------------|-----------------------------|--------------------|
| In millions of euros  |                        |                  |                             |                    |
| <b>Equity at 31 December 2009 (*)</b>   | <b>440.2</b>           | <b>88.0</b>      | <b>1.8</b>                  | <b>-61.2</b>       |
| <b>Profit for the year</b>  |                        |                  |                             |                    |
| <b>Other comprehensive income:</b>  |                        |                  |                             |                    |
| Change in fair value of derivatives<br>and cash flow hedges net of tax effect |                        |                  |                             | 25.9               |
| <b>Total other comprehensive income</b>                                       | <b>0.0</b>             | <b>0.0</b>       | <b>0.0</b>                  | <b>25.9</b>        |
| <b>Comprehensive income</b>   | <b>0.0</b>             | <b>0.0</b>       | <b>0.0</b>                  | <b>25.9</b>        |
| <b>Transactions with equity owners:</b>                                       |                        |                  |                             |                    |
| Allocation of 2009 profit   |                        |                  |                             |                    |
| - 2009 dividend   |                        |                  |                             |                    |
| - Retained earnings 2009  |                        |                  |                             |                    |
| Exercise of stock options   | 0.8                    |                  | 6.8                         |                    |
| 2010 interim dividend   |                        |                  |                             |                    |
| <b>Total transactions with equity owners</b>                                  | <b>0.8</b>             | <b>0.0</b>       | <b>6.8</b>                  | <b>0.0</b>         |
| Other changes   |                        |                  |                             |                    |
| <b>Equity at 31 December 2010</b>   | <b>441.0</b>           | <b>88.0</b>      | <b>8.6</b>                  | <b>-35.3</b>       |

(\*) The retrospective application of IFRIC 12 - Service concession arrangements had no effect on opening equity at 31 December 2009.

31 DECEMBER 2008 – 31 DECEMBER 2009

CONSOLIDATED SHARE CAPITAL AND RESERVES

|   | Share/quota<br>capital | Legal<br>reserve | Share<br>premium<br>reserve | Hedging<br>reserve |
|---|------------------------|------------------|-----------------------------|--------------------|
| In millions of euros  |                        |                  |                             |                    |
| <b>Equity at 31 December 2008</b>   | <b>440.2</b>           | <b>88.0</b>      | <b>2.7</b>                  | <b>-49.3</b>       |
| <b>Profit for the year</b>  |                        |                  |                             |                    |
| <b>Other comprehensive income:</b>  |                        |                  |                             |                    |
| Translation of financial statements<br>of foreign operations                  |                        |                  | -0.9                        |                    |
| Change in fair value of derivatives<br>and cash flow hedges net of tax effect |                        |                  |                             | -11.9              |
| <b>Total other comprehensive income</b>                                       | <b>0.0</b>             | <b>0.0</b>       | <b>-0.9</b>                 | <b>-11.9</b>       |
| <b>Comprehensive income</b>   | <b>0.0</b>             | <b>0.0</b>       | <b>-0.9</b>                 | <b>-11.9</b>       |
| <b>Transactions with equity owners:</b>                                       |                        |                  |                             |                    |
| Allocation of 2008 profit   |                        |                  |                             |                    |
| - 2008 dividend   |                        |                  |                             |                    |
| - Retained earnings 2008  |                        |                  |                             |                    |
| Exercise of stock options   |                        |                  |                             |                    |
| 2009 interim dividend   |                        |                  |                             |                    |
| <b>Total transactions with equity owners</b>                                  | <b>0.0</b>             | <b>0.0</b>       | <b>0.0</b>                  | <b>0.0</b>         |
| <b>Equity at 31 December 2009 (*)</b>   | <b>440.2</b>           | <b>88.0</b>      | <b>1.8</b>                  | <b>-61.2</b>       |

(\*) Net equity attributable to non-controlling was equal to € 86.9 million at 31 December 2008 and to 0 at 31 December 2009.

| Equity investments in assets held for sale | Other reserves                    | Effect of foreign currency trans. | Retained earnings | Interim dividend    | Profit for the year                             | Equity attributable to the owners of the Parent | Equity attributable to non-controlling interests | Total equity   |
|--|-----------------------------------|-----------------------------------|-------------------|---------------------|---|---|--|----------------|
| <b>0.0</b>                                 | <b>730.1</b>                      | <b>0.0</b>                        | <b>671.7</b>      | <b>-140.1</b>       | <b>771.0</b>                                    | <b>2,501.5</b>                                  | <b>0</b>   | <b>2,501.5</b> |
|  |                                   |                                   |                   |                     | <b>613.6</b>                                    | <b>613.6</b>                                    | <b>-</b>   | <b>613.6</b>   |
| 16.0                                       |                                   |                                   |                   |                     |   | 41.9  | -  | 41.9           |
| <b>16.0</b>                                | <b>0.0</b>                        | <b>0.0</b>                        | <b>0.0</b>        | <b>0.0</b>          | <b>0.0</b>                                      | <b>41.9</b>                                     | <b>-</b>   | <b>41.9</b>    |
| <b>16.0</b>                                | <b>0.0</b>                        | <b>0.0</b>                        | <b>0.0</b>        | <b>0.0</b>          | <b>613.6</b>                                    | <b>655.5</b>                                    | <b>0.0</b>                                       | <b>655.5</b>   |
|  |                                   |                                   |                   | 140.1               | -380.5  | -240.4  | -  | -240.4         |
|  |                                   |                                   | 390.5             |                     | -390.5  | 0.0   | -  | 0.0            |
|  | -0.4                              |                                   |                   |                     |   | 7.2   | -  | 7.2            |
|  |                                   |                                   |                   | -160.4              |   | -160.4  | -  | -160.4         |
| <b>0.0</b>                                 | <b>-0.4</b>                       | <b>0.0</b>                        | <b>390.5</b>      | <b>-20.3</b>        | <b>-771.0</b>                                   | <b>-393.6</b>                                   | <b>-</b>   | <b>-393.6</b>  |
|  |                                   |                                   | -2.8              |                     |   | -2.8  | 0.2  | -2.6           |
| <b>16.0</b>                                | <b>729.7</b>                      | <b>0.0</b>                        | <b>1,059.4</b>    | <b>-160.4</b>       | <b>613.6</b>                                    | <b>2,760.6</b>                                  | <b>0.2</b>                                       | <b>2,760.8</b> |
| Other reserves                             | Effect of foreign currency trans. | Retained earnings                 | Interim dividend  | Profit for the year | Equity attributable to the owners of the Parent |   |  |                |
| <b>729.9</b>                               | <b>-3.2</b>                       | <b>659.5</b>                      | <b>-118.5</b>     | <b>327.5</b>        | <b>2,076.8</b>                                  |   |  |                |
|  |                                   |                                   |                   | <b>771.0</b>        | <b>771.0</b>                                    |   |  |                |
| 0.2  | 3.2                               | 0.9                               |                   |                     |   |   |  | 3.4            |
|  |                                   |                                   |                   |                     |   |   |  | -11.9          |
| <b>0.2</b>                                 | <b>3.2</b>                        | <b>0.9</b>                        | <b>0.0</b>        | <b>0.0</b>          | <b>-8.5</b>                                     |   |  |                |
| <b>0.2</b>                                 | <b>3.2</b>                        | <b>0.9</b>                        | <b>0.0</b>        | <b>771.0</b>        | <b>762.5</b>                                    |   |  |                |
|  |                                   |                                   |                   | 118.5               | -316.2  |   |  | -197.7         |
|  |                                   | 11.3                              |                   |                     | -11.3   |   |  | 0.0            |
|  |                                   |                                   |                   |                     |   |   |  | 0.0            |
|  |                                   |                                   |                   | -140.1              |   |   |  | -140.1         |
| <b>0.0</b>                                 | <b>0.0</b>                        | <b>11.3</b>                       | <b>-21.6</b>      | <b>-327.5</b>       | <b>-337.8</b>                                   |   |  |                |
| <b>730.1</b>                               | <b>0.0</b>                        | <b>671.7</b>                      | <b>-140.1</b>     | <b>771.0</b>        | <b>2,501.5</b>                                  |   |  |                |

# Consolidated statement of cash flows (\*)

| In millions of euros   | 31 Dec. 2010    | 31 Dec. 2009    |
|--|-----------------|-----------------|
| <b>Profit for the year</b>   | <b>613.6</b>    | <b>771.0</b>    |
| <b>Adjustments for:</b>  |                 |                 |
| Amortisation, depreciation, impairment losses/(reversals of impairment losses) on property, plant and equipment and intangible assets (**) | 351.4           | 303.2           |
| Provisions (including employee-related provisions) and impairment losses   | 63.5            | 114.0           |
| (Gains)/Losses on disposals of property, plant and equipment   | -3.1            | -1.3            |
| Net financial income   | 99.5            | 126.0           |
| Income taxes   | 249.2           | 197.3           |
| <b>Cash flows generated by operating activities, before changes in net working capital</b>   | <b>1,374.1</b>  | <b>1,510.2</b>  |
| Decrease in provisions (including employee-related and tax provisions)   | -42.6           | 14.4            |
| (Increase)/decrease in inventories   | 0.3             | 6.0             |
| (Increase)/decrease in trade receivables and other current assets  | -346.1          | 576.6           |
| Increase/(decrease) in other non-current liabilities   | -0.3            | -247.6          |
| Increase/(decrease) in other non-current assets  | -187.0          | 89.4            |
| Increase/(decrease) in trade payables and other liabilities  | 333.7           | -328.5          |
| Interest income and other financial income received  | 109.1           | 59.9            |
| Interest expense and other financial expense paid  | -212.1          | -227.1          |
| Income taxes paid  | -255.7          | -174.0          |
| <b>Cash flows generated by operating activities [a]</b>  | <b>773.4</b>    | <b>1,279.3</b>  |
| Investments in property, plant and equipment, net of grants received   | -1,092.2        | -834.5          |
| Recognition of acquired companies' property, plant and equipment   | -43.4           | -1,101.4        |
| Revenue from sale of property, plant and equipment and intangible assets   | 4.7             | 7.5             |
| Property, plant and equipment of discontinued operations   | 0.0             | 620.2           |
| Contract work in progress in intangible assets, net of grants received   | -58.1           | -51.0           |
| Recognition of intangible assets - new acquisitions  | 0.0             | -6.3            |
| Goodwill from acquisitions   | 0.0             | -101.6          |
| Contract works in progress relative to assets held for sale  | -503.5          | 0.0             |
| Profit Intangible assets and goodwill from discontinued operations held for sale   | -1.4            | 227.4           |
| Increase/decrease in investments in associates and joint ventures  | -8.1            | -2.7            |
| Acquisition of investments   | -0.5            | 0.0             |
| Investment in discontinued operations and assets held for sale   | 0.1             | -0.1            |
| <b>Cash flows used in investing activities [b]</b>   | <b>-1,702.4</b> | <b>-1,242.5</b> |
| Increase/(decrease) in share capital   | 0.8             | 0.0             |
| Increase/(decrease) in reserves  | 6.4             | 3.7             |
| Increase/(decrease) in net income and accumulated losses   | -2.8            | 0.0             |
| Dividends paid   | -400.8          | -337.8          |
| Non-controlling interests in discontinued operations held for sale   | 0.2             | -86.9           |
| Change in short- and medium/long-term financial payables (including short-term portions) (***)   | 981.4           | 607.3           |
| Change in short-term financial investments   | 500.0           | -500.0          |
| Financial debt of discontinued operations  | 0.0             | -502.7          |
| <b>Cash flows generated by (used in) financing activities [c]</b>  | <b>1,085.2</b>  | <b>-816.4</b>   |
| <b>Increase/(decrease) in cash and cash equivalents [a+b+c]</b>  | <b>156.2</b>    | <b>-779.6</b>   |
| Opening cash and cash equivalents  | 0.1             | 779.7           |
| Closing cash and cash equivalents  | 156.3           | 0.1             |
| of which: Cash and cash equivalents of discontinued operations and assets held for sale  | 6.2             | 0.0             |

(\*) For comments on the consolidated statement of cash flows, please see the section "Notes to the consolidated statement of cash flows" in the notes to the financial statements;

(\*\*) net of grants related to assets recognised in the consolidated income statement;

(\*\*\*) net of FVH derivatives.







## Notes to the consolidated financial statements



# A. Accounting policies

## Foreword

Terna S.p.A. has registered offices in Viale Egidio Galbani 70, Rome, Italy. Its consolidated financial statements as at and for the year ended 31 December 2010 include its separate financial statements and those of its subsidiaries (the “Group”), as well as the Group’s share of associates and joint ventures. The subsidiaries included within the scope of consolidation are listed below.

These consolidated financial statements have been authorized for publication by the Directors on 31 March 2011.

The consolidated financial statements as at and for the year ended 31 December 2010 are available upon request within the registered offices of the company Terna S.p.A., Viale Egidio Galbani, 70 Rome or at the website [www.terna.it](http://www.terna.it).

## Compliance with IFRS

The consolidated financial statements as at and for the year ended 31 December 2010 have been prepared in accordance with International Financial Reporting Standards (IFRS), International Accounting Standards (IAS) and the interpretations of the International Financial Reporting Interpretations Committee (IFRIC) and the Standing Interpretations Committee (SIC), endorsed by the European Commission (IFRS-EU) at that date.

These consolidated financial statements have also been prepared by taking into account the provisions of Legislative Decree no. 38 of 28 February 2005, the Italian Civil Code and CONSOB Resolutions nos. 15519 (“*Provisions governing financial statements in implementation of art. 9, paragraph 3, of Legislative Decree no. 38/2005*”) and 15520 (“*Amendments to the implementing rules for Legislative Decree no. 58/1998*”), both of 27 July 2006, as well as CONSOB Communication no. DEM/6064293 of 28 July 2006 (“*Disclosure requirements for listed issuers and issuers of financial instruments that are widely held among the public and pursuant to art. 116 of the Consolidated Financial Act*”).

The consolidated financial statements have been prepared on a historic cost basis, modified where necessary for certain financial instruments, as well as on a going concern basis. The Group has determined that, despite the challenging economic and financial environment, it does not face material uncertainties (as defined in paragraph 25 of IAS 1) that might cast doubt on its ability to continue as a going concern.

## Basis of presentation

The consolidated financial statements are composed of the balance sheet, the income statement, the statement of comprehensive income, the statement of cash flows, the statement of changes in equity and the notes thereto.

In the balance sheet, assets and liabilities are classified on a “current/non-current” basis, with separate reporting of assets and liabilities held for sale. Current assets, which include cash and cash equivalents, are those held for realisation, sale or consumption in the Group’s normal operating cycle; current liabilities are those expected to be settled in the Group’s normal operating cycle or within one year from the close of the financial year.

The income statement is classified on the basis of the nature of costs. The income statement is presented as two statements, the first of which (income statement) presents the components of profit or loss for the year; while the second (statement of comprehensive income) starts with the result for the year and then presents the revenue and expense items (including reclassification adjustments) that are recognised in equity rather than profit or loss for the year.

The statement of cash flows has been prepared using the indirect method.

The consolidated financial statements are accompanied by the Directors’ Report for Terna S.p.A. and the Terna Group, which as from the 2008 financial year has been prepared as a single document, exercising the option granted under Legislative Decree no. 32 of 2 February 2007, which amended art. 40 (Directors’ Report) of Legislative Decree no. 127 of 9 April 1991.

These consolidated financial statements are presented in millions of euros, and all figures are shown in millions of euros, unless otherwise indicated.

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

### Rights on the infrastructure

As at 1 January 2010, IFRIC 12 - Service concession arrangements (also the "Interpretation") became effective. IFRIC 12 specifies the accounting treatment of service concession arrangements, not expressly governed by any specific accounting standard, in order to ensure the consistency and comparability of the financial statements of companies that hold concessions for the delivery of public services. More specifically, the interpretation sets out rules for accounting for the infrastructure used to provide the services under concession, for the costs associated with developing and maintaining such infrastructure, and for the revenue generated by the overall provision of the services. IFRIC 12 does not apply to all arrangements. Its scope is limited to service concession arrangements between public bodies and private operators in which the grantor: (1) controls the use of the infrastructure and governs which services are to be provided, the manner in which they are to be provided and the prices of such services and (2) controls any residual interest in the infrastructure at the end of the concession period. The interpretation also applies to infrastructure constructed by or obtained from third parties for the provision of services under the concession, and to existing infrastructure that the grantor makes available to the operator in order to provide such services. It does not apply to infrastructure owned and accounted for as property, plant and equipment by the operator prior to entering into the service concession arrangement.

Assisted by external consultants, Terna has performed a detailed study of the applicability of IFRIC 12 and the effects of its adoption on the financial statements, identifying that this interpretation does not apply to the transmission activities aspect of Terna's concession. In particular, neither the concession nor related legislation envisage the NTG's return to public ownership, either via the payment of an indemnity or otherwise.

Accordingly, the public sector does not control, whether as owner or as holder of beneficial interests or other rights, any significant residual interest in the NTG's infrastructure at the end of the concession period.

By contrast, the Ministry is entitled to reclaim the operating assets employed directly in dispatching activities at the end of the concession. As such, the Group considers that IFRIC 12 does apply to its dispatching infrastructure since the relevant criteria apply: the services provided are regulated and control exists over the residual interest. In particular, having regard for the tariff regime that remunerates dispatching activities, the Intangible Asset model envisaged by IFRIC 12 has been applied. Consequently, the property, plant and equipment and intangible assets employed in the dispatching activities carried out under concession are classified as "Intangible assets", in the "Infrastructure rights" caption, with application of the original amortisation schedule.

The revenue and costs relating to the investment in dispatching activities are recognised with reference to the contracts concerned on a stage-of-completion basis; revenue recognised during the construction phase is limited to the amount of the internal and external construction costs incurred, considering that the fair value of the construction services is equivalent to the construction cost recognised to third party contractors plus the internal cost of the technical personnel employed on such construction activities.

By contrast, tariff revenue continues to be recognised in accordance with IAS 18 and borrowing costs continue to be capitalised pursuant to IAS 23R.

As envisaged in the same interpretation, the Group has adopted the interpretation on a retrospective basis at 1 November 2005, when the TSO line of business was acquired from GRTN, the manager of the NTG, and the provision of dispatching services commenced under concession. The retrospective application of IFRIC 12 has had no effect on consolidated equity at 1 January 2009 and 31 December 2009, or on the comprehensive income for 2009 presented for comparative purposes in these consolidated financial statements at 31 December 2010.

Pursuant to the above, the investments of the year 2009 have been reclassified in the income statement, showing construction costs and revenue separately.

In conclusion, the application of IFRIC 12 to the corresponding information provided has involved the reclassification as intangible assets of property, plant and equipment totalling € 83.2 million at 1 January 2009 and € 85.4 million at 31 December 2009 (including the reclassification of work in progress amounting to € 13.2 million), and the recognition of construction costs and revenue in 2009, equal to € 29.5 million.

### Discontinued operations and non-current assets held for sale

Non-current assets (or disposal groups) whose carrying amount will be recovered principally through a sale rather than through continuing use are classified as held for sale and reported separated from other assets and liabilities in the statement of financial position. Non-current assets (or disposal groups) classified as held for sale are first measured in conformity with the IFRS/IAS applicable to each asset and liability and subsequently are measured at the lower of their carrying amount and fair value less costs to sell. The carrying amounts of each asset and liability that are not governed by the measurement rules set out in IFRS 5, but are held for sale, are re-measured on the basis of the applicable IFRS before the fair value less costs to sell is redetermined. The individual assets of the companies classified as held for sale are not depreciated/amortised, whereas financial expense and other expenses attributable to liabilities held for sale continue to be recognised. Any subsequent impairment losses are recognised directly as an adjustment to the carrying amount of the non-current assets (or disposal groups) classified as held for sale through profit or loss. The corresponding statement of financial position values for the previous year are not reclassified. A discontinued operation is a component of an entity

that either has been disposed of, or is classified as held for sale, and:

- represents a separate major line of business or geographical area of operations;
- is part of a single co-ordinated plan to dispose of a separate major line of business or geographical area of operations; or
- is an operation acquired exclusively with a view to resale.

On 18 October 2010 Terna, SunTergrid and Terra Firma Investments (GP) 3 Limited (wholly-owned by Terra Firma Capital Partners III, L.P.) signed an agreement to transfer 100% of the share capital of Rete Rinnovabile S.r.l. (as well as the latter's subsidiaries).

As a result of this agreement, and in accordance with IFRS 5 - Non-current assets held for sale and discontinued operations, the company RTR and its subsidiary Valmontone have been reported within the consolidated financial statements of 31 December 2010 under the item "Assets held for sale" for all asset items of their financial statements and under "liabilities held for sale" for all liability items of their financial statements. With reference to the comparative statements of 31 December 2009, on the other hand, the balance sheet items were not re-classified and therefore continue to be reported in the various items of the financial statements of interest.

## Use of estimates

The preparation of the consolidated financial statements 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 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 periodically and the effects of any changes are recognised in the income statement for the period, if they relate solely to that period. In the case that the revision affects both current and future years, the change is recorded in the year in which the revision is implemented as well as in the relative future years.

The critical areas for key valuations and assumptions used by management in applying the 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 recognised net of any plan assets and is measured on the basis of actuarial assumptions, estimating the amount of future benefits that employees have vested at the reporting date.

### Provisions for risks and charges

Accruals to the provisions for contingencies and charges are recognised when, at the reporting date, there is a legal or constructive obligation as a result of a past event, and 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 financial effect of the passage of time is material, accruals are measured by discounting the estimated outflow at a pre-tax discount rate that reflects current market assessments of the time value of money (free risk) and, if applicable, the risks specific to the liability. Any increase in provisions associated with the passage of time is taken to the income statement under "Financial expense".

### Allowance for impairment

Trade receivables are initially recognised at fair value net of any impairment losses relating to sums considered non recoverable, which are taken to the specific allowance for impairment. 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 analysed 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 scope of consolidation

The scope of consolidation includes the parent Terna S.p.A. and the companies over which the Parent has the power to directly or indirectly govern financial and operating policies so as to obtain benefits from their activities, regardless of the type of ownership. 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.

The companies included within the scope of consolidation are listed below:

| Company  | Registered office | Assets  | Currency | Share/quota capital | % held | Consolidation method |
|--|-------------------|---|----------|---------------------|--------|----------------------|
| <b>COMPANIES CONTROLLED DIRECTLY BY TERNA S.P.A.</b> |                   |   |          |                     |        |                      |
| <b>TELAT S.r.l.</b>                                  | Rome              | Design, construction, management, development, operation and maintenance of high-voltage power lines  | euro     | 243,577,554         | 100%   | Line-by-line         |
| <b>SunTergrid S.p.A.</b>                             | Rome              | Construction and maintenance of electricity transmission grids and plants for the generation of electricity, including renewables' generation, for own use and sale in Italy and abroad                             | euro     | 120,000             | 100%   | Line-by-line         |
| <b>CONTROL THROUGH SUNTERGRID S.P.A.</b>             |                   |   |          |                     |        |                      |
| <b>RTR S.r.l. (*)</b>                                | Rome              | Construction and maintenance of electricity transmission grids and plants for the generation of electricity, including renewables generation, for own use and sale in Italy and abroad                              | euro     | 50,000              | 100%   | Line-by-line         |
| <b>Rete Solare S.r.l.</b>                            | Rome              | Construction and maintenance of electricity transmission grids and plants for the generation of electricity, including renewables generation, for own use and sale in Italy and abroad                              | euro     | 10,000              | 100%   | Line-by-line         |
| <b>CONTROL THROUGH RTR S.R.L.</b>                    |                   |   |          |                     |        |                      |
| <b>Valmontone Energia S.r.l. (*)</b>                 | Rome              | Design, construction, management, and maintenance of photovoltaic plants for the production and sale of electrical energy, in accordance with the licensing agreement stipulated with the Comune of Valmontone (FR) | euro     | 1,135,134           | 98.50% | Line-by-line         |

(\*) Reclassified under assets held for sale.

The **change in the scope of consolidation** since 31 December 2009 relates to:

- the founding - on 18 May 2010 and on the part of the subsidiary SunTergrid S.p.A. - of the company named "Rete Solare S.r.l." (henceforth, for brevity, referred to as "RTS S.r.l.") with a share capital of € 10,000;
- the acquisition - on 25 October 2010 - of shares representing circa 98.5% of the share capital (equal to € 1,118,106.99) Valmontone Energia S.r.l. by Troiani & Ciarrocchi S.r.l. and C.I.EL. S.p.A.

## Associates

Investments in associates are those over which the Terna Group has significant influence but which are neither subsidiaries nor joint ventures. In assessing whether or not Terna has a significant influence, potential voting rights that are presently exercisable or convertible are also considered.

These investments are initially recognised at acquisition cost and subsequently measured using the equity method. The profits or the losses attributable to the Group are recognised within the consolidated financial statements from the date when it begins to exercise significant influence and until that influence ceases.

In the event that the loss pertaining to the Group exceeds that investment's carrying amount, the latter is written off and any excess is recognised in a specific provision in the case that the Parent is required to meet the legal or constructive obligations of the subsidiary or, in any case, to cover its losses.

## Joint ventures

Investments in jointly-controlled entities, in which the Group exercises joint control of other entities, are recognised initially at cost and subsequently measured using the equity method. The profits or the losses pertaining to the Group are recognised within the consolidated financial statements when it begins to exercise significant influence and until that influence ceases. For more information on the Group's accounting treatment of jointly-controlled entities held for sale, see the section "Discontinued operations and non-current assets held for sale" above.

In assessing whether or not the Parent has a joint interest, potential voting rights that are presently exercisable or convertible are also considered.

| Company office           | Registered          | Assets  | Currency capital | Share/quota | % held | Consolidation method |
|--------------------------|---------------------|---|------------------|-------------|--------|----------------------|
| <b>ASSOCIATES</b>        |                     |   |                  |             |        |                      |
| <b>CESI S.p.A.</b>       | Milan               | Experimental electro-technical research   | euro             | 8,550,000   | 39.9%  | Equity Method        |
| <b>CORESO S.A.</b>       | Bruxelles (Belgium) | Technical centre owned by various electrical energy transmission companies which implements joint TSO technical coordination activities in order to improve and strengthen security and coordination of the electrical system in central/western Europe. It prepares daily forecasts and analyses in real time on energy flows in the region, identifying potentially critical areas and promptly informing any affected TSO's. | euro             | 1,000,000   | 22.49% | Equity Method        |
| <b>JOINT VENTURES</b>    |                     |   |                  |             |        |                      |
| <b>ELMED Études Sarl</b> | Tunis               | Analysis and preliminary consulting for the preparation of tender documentation of the Tunisian government for construction tenders and the management of the electricity generation site in Tunisia involved in the project for the interconnection of Italy and Tunisia   | Tunisian Dinar   | 2,700,000   | 50%    | Equity Method        |

## Consolidation policies

All financial statements of subsidiaries used to prepare the consolidated financial statements were drafted as at and for the year ended 31 December 2010 and have been approved by their respective Board of Directors; they have been adjusted, where necessary, to align them with the Parent's accounting policies. During the preparation of the consolidated financial statements, intercompany balances, transactions, revenue and costs are fully eliminated, net of the related tax effect, where material ("consolidation on a line-by-line basis").

Unrealised gains and losses with associates and joint ventures are eliminated in proportion to the Group's holding therein. In both cases, unrealised losses are eliminated, unless they represent impairment.

## Translation of foreign currency items

The financial statements of each consolidated company are prepared using the functional currency for the economic environment in which each company operates.

In these financial statements, all transactions in currencies other than the functional currency are recognised at the exchange rate prevailing on the date of the transaction. Monetary assets and liabilities in currencies other than the functional currency are subsequently adjusted at the exchange rate prevailing at year end. Any exchange rate differences are taken to profit or loss.

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

## Translation of financial statements of foreign operations

For the purposes of the consolidated financial statements, profits and losses, assets and liabilities are expressed in euros, which is the parent Terna S.p.A.'s functional currency.

For the purposes of drafting the consolidated financial statements, the financial statements of subsidiaries with a functional currency other than the euros, including goodwill and consolidation adjustments, are converted into euros at the exchange rate prevailing at the reporting 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 profit or loss when the shareholding is sold.

## Business combinations

The Group books company acquisitions in compliance with the updated version of IFRS 3 - Business combinations which was endorsed on 3 June 2009 by the European Commission by means of Regulations no. 495/2009 and became effective as at 1 January 2010. The change in the accounting principle was applied prospectively and did not have significant effects on earnings per share.

Business combinations are booked by applying the purchase method on the date of acquisition, or on the date in which control is effectively attained; control is defined as the power to formulate the financial and managerial policies of an entity in order to obtain benefits from its activities. When evaluating the existence of this control, the Group must take into account the potential voting rights which are effectively exercisable.

The new provisions of IFRS 3 also require the booking – within the income statement – of accessory costs, including transaction costs, which are associated with the business combination as well as the booking – again within the income statement – of changes in contingent consideration in addition to providing the right to book the entire value of goodwill that derives from the operation by taking into account, as a result, of the quota of non-controlling interest (the full goodwill method). The principle states that the contingent consideration must be booked at fair value on the date of acquisition. If this consideration is classified under shareholders' equity, it must not be re-calculated and its subsequent redemption must be booked under equity. If this is not the case, subsequent changes in the fair value of the contingent consideration are booked under profit or loss for the year.



The new provisions also modify the current criterion for booking acquisitions in subsequent phases and require the booking – within the income statement – of the difference between the fair value on the date of acquisition of control over previously held net assets and the relative carrying amount.

In the case of acquisitions implemented from 1 January 2010, the Group will evaluate the fair value of the goodwill on the date of acquisition, increased by any potential value of non-controlling interest in the acquired company and including – in the case that the business combination is realized across several phases – the fair value of the interest which was previously held; from this amount, the net amount booked for identifiable acquired assets and assumed liabilities must be deducted. If this surplus, as calculated above, is negative, a profit deriving from an acquisition at a bargain price is immediately booked within the profit or loss of the year.

On 3 June 2009 and by means of Regulation no. 494/2009 issued by the European Commission, the updated version of IAS 27 - Consolidated and separate financial statements was also ratified. In compliance with the new principle, acquisitions of third party shareholdings are booked as operations implemented with shareholders – acting in the capacity of shareholders – and therefore these operations will not result in bookings of goodwill. Adjustments to third party shareholdings are based on a proportional amount of the net assets of the subsidiary.

The updated version of IAS 27 also states that the effects deriving from the acquisition (sale) of investments following the acquisition of control (without losses of control) must be booked under equity. In addition, the new provisions state that – in the case of a sale of part of the owned investment with a corresponding loss of control or of joint or affiliation – the remaining investment must be adjusted to the relative fair value and the revaluation must contribute towards generating the capital gain (loss) that arises from the sale.

The new principle is not applicable to past operations but only to potential business combinations which are created after the date of effectiveness.

## Property, plant and equipment

Property, plant and equipment are recognised at historic cost, including costs directly 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 booked under future provisions for risks and charges. Borrowing costs directly attributable to the acquisition, construction or production of an asset that qualify for capitalisation pursuant to IAS 23R are capitalised as part of the cost of the asset. For more information, please see the section “Financial income and expense” below. Costs incurred after purchase are recognised as an increase in the carrying amount of the asset to which they relate if it is probable that the future benefits of that cost will flow to the Company and if the cost can be reliably measured. All other costs are recognised in profit or loss 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 recognised and depreciated separately.

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

Property, plant and equipment is 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 economic life of the asset, which is reviewed annually, with revisions applied on a prospective basis. The depreciation of assets 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 booked to the income statement through the depreciation of the tangible fixed asset.



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

#### DEPRECIATION RATES

|  |        |
|--|--------|
| Civil and industrial buildings                       | 2.50%  |
| Transmission lines                                   | 2.50%  |
| Transformer stations:                                |        |
| - Electrical machinery                               | 2.38%  |
| - Electrical devices and equipment                   | 3.13%  |
| - Automation and control systems                     | 6.70%  |
| Central systems for remote management and control:   |        |
| - Devices, electrical equipment and ancillary plants | 5.00%  |
| - Electronic calculation equipment                   | 10.00% |
| Solar power plants:                                  |        |
| - Buildings  | 5.00%  |
| - Electrical machinery                               | 5.00%  |
| - Devices, electrical equipment and ancillary plants | 5.00%  |
| - Panels and support structures                      | 5.00%  |
| - Inverters  | 10.00% |
| - Automation and control systems                     | 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 leases – and through which the Group has substantially acquired all the risks and rewards of ownership – are recognised 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 exercise the purchasing option. The corresponding liability to the lessor is recognised 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.

## Intangible fixed assets

Intangible assets, which all have finite useful lives, are recognised at cost, having obtained the approval of the Board of Statutory Auditors, and shown net of accumulated amortisation and any impairment losses, measured as described below. Amortisation begins when the asset becomes available for use and is calculated on a straight-line basis over the estimated useful life of the related asset, which is reviewed annually. Any revisions to estimated figures are applied on a prospective basis.

Intangible assets essentially regard the exclusive license to carry out electricity transmission and dispatching activities and other intangible fixed assets. In particular, Terna S.p.A. obtained the license for electricity transmission and dispatching activities in Italy on 1 November 2005 when it acquired the TSO business unit. As established in the Decree issued by the Ministry of Productive Activities on 20 April 2005, this license runs for twenty-five years, renewable for another 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 S.p.A. This intangible asset was initially recognised at cost, which reflected fair value.

Other intangible assets mainly relate to the following:

- the development and innovation of application software to manage the electricity invoicing process;
- the development and innovation of application software to protect the electrical 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.

Development costs are capitalised by the Group only if all following conditions are met: costs can be reliably estimated and there is technical feasibility and intent to complete the intangible asset so as for it to be available after use; the intangible asset can be used and it is possible to demonstrate that it will generate probable future economic benefits.

Borrowing costs directly attributable to the acquisition, construction or production of a qualifying asset pursuant to IAS 23R are capitalised as part of the cost of the asset. For more information, please see the section "Financial income and expense" below.

All other development costs and research expenses are recognised in profit or loss when incurred. These intangible assets are amortised over their estimated residual useful life, which is 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 electricity transmission and dispatching activities. Goodwill is not amortised after initial recognition. It is adjusted to reflect impairment losses, measured as described below. Goodwill relating to investments in associates and joint ventures is included in the carrying amount of those companies. Where negative goodwill arises, it is booked within the income statement at the time of the acquisition. In the adoption of the 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 recognised 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 evidence 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 at least annually.

Recoverable amount is equal to the greater of fair value less costs to sell and value in use. Value in use is 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 pre-tax rate that reflects current market assessment of the time value of money for the investment period and risks specific to the asset. If the intangible asset does not generate cash inflows that are largely independent, the asset's recoverable amount is calculated as part of the CGU to which it belongs.

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

Impairment losses 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 up to the recoverable amount 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 recognised and measured at the lower of purchase cost and net estimated realisable value. Cost is calculated as the weighted average cost, including related charges. Net estimated realisable value stands for the estimated price of sale under normal conditions net of completion costs and the estimated costs to sell.

## Contract work in progress

When the profit or loss on a contract can be reliably estimated, the related contract costs and revenue are recognised separately in the income statement on a percentage of completion basis. Progress is measured on the basis of the work carried out and measured proportionally to the ratio of costs for the works carried out up to reporting date and total cost of the contract (cost-to-cost). Differences between the value of completed contracts and payments on account received are recognised 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 recognise the work performed. Expected contract losses are immediately taken to profit or loss.

Contract costs include all those costs that relate directly to the specific contract, as well as fixed and variable costs incurred by the Group companies as part of normal operations.

## Financial instruments

### Financial assets

Any financial assets other than financial derivatives that the Company has the positive intention and ability to hold to maturity are recognised 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 amortised 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 derecognised when, following their transfer or settlement, the Group companies are no longer involved in their management and no longer hold the risks and rewards of the transferred or settled instruments.

### Trade receivables

Trade receivables are initially recognised at fair value and subsequently measured at amortised 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 measured on the basis of the present value of estimated future cash flows, discounted at the original 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 monetary items, i.e. amounts that are available on demand or with a very short maturity, subject to an insignificant risk and without collection costs.

### Trade payables

Trade payables are initially recognised at fair value and subsequently stated at amortised cost. If their due date falls under normal commercial terms, they are not discounted.

### Financial liabilities

Financial liabilities other than financial derivatives are initially recognised at the settlement date and measured at fair value, net of directly related transaction costs.

Subsequently, financial liabilities are measured at amortised cost, using the original effective interest method. If the liabilities are covered by fair value hedges, they are adjusted to reflect changes in fair value with respect to the hedged risk.

### Derivative financial instruments

Derivatives are recognised 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 within a range of 80% to 125%, as initially verified and periodically checked. When derivatives cover the risk of changes in the cash flows of the hedged instruments (cash flow hedges), the part of changes in the fair value qualifying as effective is initially taken to equity and subsequently to profit or loss, in line with the effects of the hedged transaction. The portion of the fair value of the hedging instrument that does not qualify as effective is taken to profit or loss.

When hedging derivatives cover the risk of changes in the fair value of hedged instruments (fair value hedges), they are recognised at fair value in the income statement. Accordingly, the hedged items are adjusted to reflect changes in the fair value associated with the hedged risk.

Changes in the fair value of derivatives that do not meet hedge accounting requirements pursuant to the IFRS-EU are recognised in profit or loss.

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

Financial and non-financial contracts (which are not already measured at fair value) are also analysed to identify any embedded derivatives, which must be separated and measured at fair value. This analysis is conducted at the time the entity becomes party to the contract or when the contract is renegotiated in a manner that produces a material change in the original associated cash flows.

The measurement techniques used for derivatives existing at year end did not change with respect to the previous year. Accordingly, the effects of these measurement on the income statement and equity are essentially attributable to normal market developments, as well as new derivative contracts signed during the year.

## Employee benefits

The liability in respect of employee benefits payable upon or after termination of employment relates to defined benefit plans (termination benefits, additional month's pay, indemnity for lack of notice, energy discount, Asem health benefits and other benefits) or other long-term employee benefits (loyalty bonus) and is recognised 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 that employees have accrued at the reporting date. The liability is recognised on an accruals basis over the vesting period. It is measured by independent actuaries.

Actuarial gains and losses as of 1 January 2004 (date of transition to IFRS-EU) were recognised under equity. After that date, unrecognised actuarial gains and losses in excess of 10% of the greater of the present value of the defined benefit plan obligation and the fair value of plan assets are booked to the income statement for the average expected term of service of employees participating in the plan. Otherwise, actuarial gains and losses are not recognized.

## 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 recognised under personnel expense 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. Such estimate is reviewed where subsequent information indicates that the expected number of instruments representative of capital that will mature differs from the estimate previously carried out, regardless of achievement of the market conditions.

The measurement method used to calculate fair value considers all the characteristics of the options (term, price and conditions etc.), as well as the price of Terna S.p.A. shares at the grant date, the volatility of the stock and the yield curve at the grant date, in line with the term of the plan.

At the vesting date, the estimate is revised through the income statement to recognise the actual amount corresponding to the number of equity instruments that have actually vested, regardless of achievement of the market conditions.

## Provisions for risks and charges

Accruals to the provisions for risks and charges are recognised when, at the reporting date, the company has a legal or implicit obligation towards others as a result of a past event and it is probable that an outflow of resources will be required to settle the obligation and a reliable estimate can be made of the amount of the 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 assessment of the time value of money (free risk) and those risks specific to the liability, if present. Where discounting is used, the increase in the provision due to the passage of time is booked within the income statement as an interest expense. If the liability relates to property, plant and equipment (site disposal and restoration, for example), the provision is recognised as a balancing entry to the asset to which it relates. The expense is recognised in the income statement through depreciation of the tangible fixed asset itself.

Changes in the estimate are recognised within the income statement for the year in which the change happens, except for those costs expected for dismantling, removal and reclamation, which come as a result of changes in the timing and use of economic resources necessary to extinguish the obligation or attributable to a material change in the discount rate, which are recognised as an increase or reduction of the related assets and recognised in profit or loss through depreciation.

## Grants

Revenue is recognised when it is probable that the economic benefits deriving from the operation will be used by the enterprise. However, when there is uncertainty concerning the recovery of an amount already recognised in revenue, the non-recoverable value or the amount whose recovery is no longer probable is recorded as a cost.

Grants received in relation to specific assets whose value is recognised under non-current assets are, for plants operating before 31 December 2002, recognised under other liabilities and taken to profit or loss over the depreciation period of the related assets. Since 2003, grants related to assets for new plants that have entered service are recognised as a direct reduction in the value of the related asset.

Grants related to income are expensed in full when the recognition requirements are satisfied.

## Revenue

Revenue is recognised when it is probable that the economic benefits deriving from the operation will be used by the enterprise. Depending on the type of transaction, revenue is recognised on the basis of the following specific criteria:

- revenue from the sale of goods is recognised when the material risks and rewards of ownership of the goods have been transferred to the buyer and their total amount can be reliably determined and collected;
- revenue from services rendered is recognised with reference to the stage of completion of the transaction. If revenue cannot be reliably measured, it is recognised to the extent of recoverable costs;
- revenue accrued during the year in respect of contract work in progress is recognised on the basis of the payments agreed for the progress of works using the cost-to-cost method. In addition to contractual payments, project revenue includes any payments in respect of variations, price revisions and incentives, with the latter recognised where it is probable that they will actually be earned and can be reliably determined. Revenue is also adjusted for any penalties for delays attributable to Group companies;
- when the recovery of an amount already recognised in revenue is uncertain, the non-recoverable value or the amount whose recovery is no longer probable is recorded as a cost, with a balancing entry in provisions for risks and charges;
- amounts collected on behalf of third parties, such as the fees paid to non-Terna grid owners, as well as revenue recognised for managing activities related to the balancing of the national electrical system, which do not increase equity, are reported net of the related costs. This reporting method, which reflects the substance of transactions by offsetting revenue with the related costs arising from the “same transaction”, is discussed in full in a specific section of the explanatory notes.

## Financial income and expense

Borrowing costs directly attributable to the acquisition, construction or production of an asset that qualify for capitalisation are capitalised as part of the cost of the asset. The qualifying assets (property, plant and equipment and intangible assets) involved are those that require at least one year before being ready for use. The directly attributable borrowing cost is that which would not have been incurred if the expenditure for the asset had not been incurred.

Where funds are borrowed specifically, costs eligible for capitalisation are the actual costs incurred less any income earned on the temporary investment of such borrowings. Where funds are raised through general borrowing, the eligible amount is determined by applying a capitalisation rate to the expenditure on that asset. The capitalisation rate will be the weighted average of the borrowing costs applicable to the general pool, excluding any specifically borrowed funds. The amount of borrowing costs capitalised during a year shall in any case not exceed the amount of borrowing costs incurred during that year.

Capitalisation commences as from the date all the following conditions have been met: (a) expenditures have been incurred for the asset; (b) borrowing costs are being incurred; and (c) activities to prepare the asset for its intended use or sale are in progress.

Capitalisation ceases when the activities necessary to prepare the asset for its intended use or sale are substantially complete.

The capitalisation rate used for 2009 is 3.12%, while that for 2010 is 2.63%.

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

## Dividends

Dividends from subsidiaries are booked when shareholders are granted the right to receive the payment which generally coincides with the date of the assembly resolution.

Dividends and advances on 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.

## Earnings per share

Basic earnings per share are calculated by dividing the profit or loss 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 profit 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 that could have a diluting effect.

## Income taxes

Current income taxes are recognised 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, taking account of applicable exemptions.

Deferred tax assets and liabilities are calculated on the temporary differences between the carrying amounts of assets and liabilities recognised in the financial statements and the corresponding amounts recognised for tax purposes, using current tax rates or the rates expected to be in effect when the temporary differences reverse, based on current rates or those that are substantially approved at the reporting date.

Deferred tax assets are recognised when their recovery is considered probable, i.e. when future taxable income will be available against which the asset can be used. The recoverability of deferred tax assets is reviewed at each year end.

Deferred tax liabilities are recognised in any case if they exist. Taxes in respect of components recognised directly in equity are also recognised in equity.







## New standards

### International Financial Reporting Standards entering into force as from 1 January 2010

As from 1 January 2010, the following International Financial Reporting Standards and their interpretation took effect:

#### IFRS 3 - Business Combinations (revised in 2007)

As from 1 January 2010, the Group recognises company acquisitions in compliance with the updated version of IFRS 3 - Business combinations which was endorsed on 3 June 2009 by the European Commission with Regulation no. 495/2009. The change in this standard was applied prospectively and did not have significant effects on earnings per share. This standard was therefore applied for the recognition of business combinations carried out by the Group in 2010; for more details on the methods of application and the relative effects on the data which are reported for comparative purposes, refer to section "F. Business combinations" of these consolidated financial statements.

On 3 June 2009 and by means of Regulation no. 494/2009 issued by the European Commission, the updated version of IAS 27 - Consolidated and separate financial statements was also endorsed.

The new principle is not applicable to past operations but only to potential business combinations which are created after the date of effectiveness. The change in the accounting principle was applied to all third party shareholdings in a prospective manner without having significant effects on earnings per share.

#### IFRIC 12 - Service Concession Arrangements

As previously specified, on 1 January 2010, IFRIC 12 - Service concession arrangements became effective. This interpretation was applied for the first time to the Terna Group's interim consolidated report at 31 March 2010 in relation to the only assets related to the licensing of the dispatching activities on the part of the Parent.

For more details regarding the application modality and the related effects on the corresponding figures, please refer to paragraph "Compliance with IFRS and basis of presentation" of these consolidated financial statements.

#### IFRIC 18 - Transfers of Assets from Customers

Endorsed by Regulation 1164/2009, this interpretation applied on a prospective basis to accounting periods commencing after 31 October 2009, provides clarification and guidance about the accounting for items of property, plant and equipment received from customers, or cash received from customers for the acquisition or construction of items of property, plant and equipment in order to connect them. In particular, this interpretation envisages the following accounting treatment in the financial statements of entities that receive property, plant and equipment, or cash for their construction, from customers in order to connect them to a network and/or to guarantee their ongoing access to a supply of goods or services (e.g. electricity, gas, water etc.):

- the asset received is recognised at fair value pursuant to the provisions of IAS 16 - Regarding the exchange of dissimilar assets, with the consequent recognition of revenue if an ongoing service is provided;
- specific accounting rules apply if the customer gives the entity an amount of cash sufficient to purchase the item of property, plant and equipment.

This standard has modified the recognition of NTG connections within the financial statements of the Parent without significant effects on the consolidated financial position or results of operations.

#### Amendment of IAS 39 - Financial Instruments - Recognition and Measurement: eligible hedged items

This amendment provides guidance on two aspects of hedge accounting: the identification of inflation as the hedged risk, or a part of it, and hedging by the use of options.

This standard has not had a significant impact on the financial statements at 31 December 2010.

#### Improvements to IFRS (published in 2009)

2009 version of the document that contains minor amendments to the standards already published. These amendments were endorsed during the first quarter of 2010 and apply immediately; they have not had a significant impact on the financial statements at 31 December 2010.

#### Practice Statement for the Directors' Report

Following its entry into force on 8 December 2010 at the time of its publication on the part of the IFRS, the Practice Statement on the Directors' Report provides a non-binding framework for presenting a Directors' Report relative to financial statements that are drafted in compliance with the IFRS.

### Other amendments and interpretations of standards

The following amendments and interpretations became effective in 2010, which govern issues that currently do not affect Terna Group's financial statements:

- IFRIC 9 - Embedded derivatives;
- amendment to IAS 39 - Reclassification of financial assets: application date;
- IFRIC 15 - Agreements for the construction of real estate;
- IFRIC 16 - Hedges of a net investment in a foreign operation;
- IFRIC 17 - Distributions of non-cash assets to owners;
- IFRS 1 - Revised first-time adoption of IFRS;
- amendment of IAS 32 - Financial instruments - Presentation: classification of option rights (or warrants);
- revisions to IFRS 1 - Additional exemptions for entities adopting IFRS for the first time;
- revision of IFRS 1 - Limited exemptions from comparative IFRS 7 - Disclosures for first-time adopters;
- amendment of IFRS 2 - Group cash-settled share-based payment transactions. The amendment clarifies the booking of operations with share-based payments that are settled in cash within a group (repeals IFRIC 8 and IFRIC 11).

The above amendments and interpretations have not had a significant impact on the financial statements of 31 December 2010.

### International financial reporting standards endorsed but not yet in force

As at the date of drafting of these financial statements, the European Commission has endorsed the following amendments to the international financial reporting standards:

#### Amendment of IAS 24 - Related Party Disclosures

Issued on 4 November 2009, this amendment simplifies the related party disclosures to be made by entities subject to control, joint control or significant influence by a governmental body, and eliminates certain difficulties in applying the current definition of related parties. The standard comes into force on 1 January 2011.

#### Improvements to IFRS (published in 2010)

2010 version of the document that contains minor amendments to the standards already published. This group of amendments was ratified on 18 February 2011 and will become effective as at 1 January 2011.

The following standards and interpretations have also been endorsed, governing circumstances currently not relevant to the financial statements of the company:

- amendment of IAS 32 - Financial instruments - Presentation: classification of option rights (or warrants), which comes into force on 1 January 2011;
- amendment to IFRIC 14 - The limit on a defined benefit asset, minimum funding requirements and their interaction;
- IFRIC 19 - Extinguishing financial liabilities with equity instruments.

### International Financial Reporting Standards not yet endorsed

For amendments, new standards and interpretations that have not yet been endorsed by the EU, but which address issues that affect or could affect the Terna Group, the Parent is assessing the possible impact of their application on its financial statements, taking account of the date on which they take effect. This assessment, in particular, covers the standards and interpretations listed below.

#### IFRS 9 - Financial Instruments

On 12 November 2009 the IASB published IFRS 9 - Financial instruments on the classification and measurement of financial assets, which will take effect as at 1 January 2013. This publication is the first part of a project to replace IAS 39. Unlike that provided for by the exposure draft published last July, the scope of the standard does not include financial liabilities, as the IASB, partly in reaction to comments on the exposure draft, decided to devote further study to issues concerning the including of own credit risk in the measurement of the fair value of financial liabilities. The European Commission has currently suspended the process of endorsing IFRS 9 and, accordingly, the standard will not apply to European companies until the Commission has been able to complete an evaluation of the entire project to replace IAS 39.

### Amendment to IFRS 7 - Financial Instruments

Issued on 7 October 2010, the amendment has the objective of integrating financial statements in order to provide more information relative to the transfer of financial assets for which part of the risk is not completely transferred and the effect of such transactions on the financial position. This amendment should also increase comparability of recognition of transfers of financial assets between the IFRS and US GAAP financial statements.

### Amendment to IAS 12 - Recovery of underlying assets

This amendment is applicable to all entities which apply IAS 40 - Investment properties by utilizing the fair value method as well as to those which have assets booked under property, plant and equipment that are not depreciated but are booked by means of the revaluation method pursuant to IAS 16. This amendment does not currently regulate cases which are applicable to our financial statements.

### Amendments to IFRS 1

#### Serious hyperinflation and removal of previously defined dates for parties which apply the IFRS principle for the first time

Two amendments to IFRS 1 have been published: the first replaces the references to a fixed transition date, 1 January 2004, as the "transition date to the IFRS", thereby eliminating the need for companies which adopt the IFRS for the first time to repeat cancellation operations which occurred before the date of transition to the IFRS. The second amendment provides specifications on how an entity must return to drafting the financial statements in compliance with the IFRS following a period in which the party was not capable of complying with the IFRS since its functional currency was subject to serious hyperinflation.

## B. Operating segments

In view of the characteristics of the Terna Group's business in Italy, the following operating segments have been identified:

- **Regulated activities**
- **Unregulated activities**
- **Assets held for sale**

The **regulated activities** segment comprises electricity transmission and dispatching, as well as the measurement, validation and registration activities associated with metering.

These activities form part of a single operating segment since they meet the relevant aggregation criteria based on similar economic characteristics, such as the common economic/regulatory context in which the services are provided, the type of tariffs and the way they are determined, and the public-interest nature of the activities concerned.

The **unregulated activities** mainly regard the management (operation and maintenance) of high-voltage plant owned by other entities, plant engineering services, maintenance of the third-party fibre optic network and housing of TLC equipment. In essence, this segment comprises the specialist services provided by the Terna Group to third-party customers.

These activities are pursued as commercial initiatives that are not regulated by the AEEG. They are pursued in a free market in which the Group leverages its skills and resources to offer other companies specialised services in, principally, the high- and very-high voltage sector and in telecommunications.

Within the realm of non-regulated activities of the Terna Group, note should be made of construction, implementation, management and maintenance activities relative to plants producing electrical energy from photovoltaic sources.

In particular, and following the agreement of 18 October 2010 for the transfer of the entire share capital of Rete Rinnovabile S.r.l. from the subsidiary SunTergrid to Terra Firma Capital Partners III, L.P., the company RTR S.r.l. and its direct subsidiary Valmontone Energia S.r.l. represent **assets held for sale** and are reported as a separate operating segment.

The identification of the Terna Group's operating segments has been carried out consistently with the internal management control system adopted by the Parent; in particular in the internal reports periodically presented and reviewed by senior management (management control reports) we used the adjusted EBITDA <sup>(3)</sup> indicator for unregulated activities.

Below we report the results of the Terna Group's operating segments in 2010 and 2009, as well as the reconciliation with the Group's profit before tax and discontinued operations and assets held for sale.

(3) EBITDA (gross operating profit) represents an indicator of operating performance; it is calculated by adding depreciation and amortization back to the operating results (EBIT).

| In millions of euros  | Italy          |                |
|---|----------------|----------------|
|   | 2010           | 2009           |
| Revenues from regulated activities  | 1,514.2        | 1,328.0        |
| Revenues from unregulated activities  | 75.0           | 62.2           |
| <b>Total continuing operations revenue</b>  | <b>1,589.2</b> | <b>1,390.2</b> |
| Assets held for sale  | 503.3          | -              |
| <b>Total revenue - Terna Group</b>  | <b>2,092.5</b> | <b>1,390.2</b> |
| Regulated activities: adjusted EBITDA <sup>(*)</sup>  | 1,245.7        | 1,058.9        |
| Unregulated activities: adjusted EBITDA <sup>(**)</sup>   | 40.7           | 31.6           |
| <b>Continuing operations: adjusted EBITDA</b>   | <b>1,286.4</b> | <b>1,090.5</b> |
| Adjusted EBITDA: assets held for sale <sup>(***)</sup>  | 148.2          | -              |
| <b>Terna Group: adjusted EBITDA</b>   | <b>1,434.6</b> | <b>1,090.5</b> |
| <b>Continuing operations total reconciliation</b>   | <b>2010</b>    | <b>2009</b>    |
| Continuing operations: adjusted EBITDA  | 1,286.4        | 1,090.5        |
| Unallocated costs   | 111.5          | 87.3           |
| <b>Continuing operations: EBITDA</b>  | <b>1,174.9</b> | <b>1,003.2</b> |
| Depreciation  | 360.5          | 308.8          |
| <b>EBIT continuing operations</b>   | <b>814.4</b>   | <b>694.4</b>   |
| Net financial expense   | -105.1         | -151.2         |
| Share of profit/(loss) of equity-accounted investees  | 2.6            | 2.9            |
| <b>Pre-tax profit from continuing operations</b>  | <b>711.9</b>   | <b>546.1</b>   |
| <sup>(*)</sup> Regulated activities: adjusted EBITDA margin (%) 82.3%;<br><sup>(**)</sup> unregulated activities: adjusted EBITDA margin (%) 54.3%;<br><sup>(***)</sup> assets held for sale: adjusted EBITDA margin (%) 29.4%. |                |                |

For the purposes of valuating the adjusted EBITDA of the operating segment “Regulated activities”, non-monetary costs (allocations to provisions for future risks and charges) totalling € 6.0 million are booked.

The information regularly reported to senior management does not made direct reference to sector activities but rather to the measurement and presentation of gross invested capital. The following table reports that indicator relative to continuing operations and assets held for sale for the years 2010 and 2009:

| In millions of euros                         | Italy                 |                      |                       |                      |
|--|-----------------------|----------------------|-----------------------|----------------------|
|  | 2010                  |                      | 2009                  |                      |
|  | Continuing operations | Assets held for sale | Continuing operations | Assets held for sale |
| Net fixed assets <sup>(1)</sup>              | 8,303.6               | 1.4                  | 7,468.5               | -                    |
| Contract work in progress                    | -                     | 509.0                | -                     | -                    |
| NWC <sup>(2)</sup>                           | -368.7                | -102.9               | -570.6                | -                    |
| Gross invested capital                       | 7,934.9               | 407.5                | 6,897.9               | -                    |
| Investments in associates and joint ventures | 23.6                  | -                    | 15.5                  | -                    |

(1) Net fixed assets include the value of the items “Property, plants and equipment”, “Goodwill”, “Intangible assets”, “Equity-accounted investees”, “Other non-current assets” and “Non-current financial assets” for the value of the other equity investments (€ 0.5 million);

(2) NWC (Net Working Capital) is equal to the difference between current assets, net of liquid funds, and current liabilities net of short-term financing, the short-term portion of long-term financing and other non-current liabilities.

As regards the dependence of Terna Group customers on external customers, in 2010 transactions that generated revenue from individual customers or companies under common control equal to more than 10% of consolidated revenue were represented by transactions with related parties in respect of regulated activities; for more information, please see the section on “Related party transactions”.







## C. Notes to the consolidated income statement

### Revenue

#### 1. Revenue from sales and services – € 1,533.1 million

“Revenue from sales and services” for the years 2010 and 2009 is analysed in the following table:

| In millions of euros                              | 2010           | 2009           | Change       |
|---|----------------|----------------|--------------|
| Grid transmission fees                            | 1,309.2        | 1,185.4        | 123.8        |
| Adjustments for prior year grid transmission fees | -2.9           | 0.2            | -3.1         |
| Other energy revenue                              | 169.8          | 121.0          | 48.8         |
| Other revenue from sales and services             | 57.0           | 40.2           | 16.8         |
| <b>Total</b>                                      | <b>1,533.1</b> | <b>1,346.8</b> | <b>186.3</b> |

#### Grid transmission fees and related adjustments

Grid transmission fees largely refer the remuneration paid to the Parent for use of the National Transmission Grid (€ 1,173.0 million). It also comprises the net revenue from the portion of the NTG pertaining to the subsidiary TELAT (€ 133.3 million). The increase of € 120.7 million in this caption mainly derives from the following factors:

- an increase in the revenue of the Parent by € 85.1 million, essentially due to:
  - the application of AEEG Resolution 203/09, which revised the tariffs for 2010 (+€ 55.0 million);
  - an incentive on remuneration of investments in strategic transmission infrastructures (ARG/elt 87/10 resolution – +€ 16.8 million);
  - increased grid transmission fees related to the Defence plan (+€ 15.5 million);
  - Negative impact for past net grid transmission fee balances (-€ 2.2 million).
- remuneration of the quota of NTG owned by TELAT which was not included within the scope of consolidated in the first three months of 2009 (+€ 35.6 million) including revenues which refer to plants of the incorporated company Rete di Trasmissione Brescia as of the date of its acquisition (+€ 2.8 million).

#### Other energy revenue

This caption comprises the fees paid to the Parent by electricity companies for dispatching services (DIS component, € 131.4 million), together with the revenue from the construction and development of dispatching infrastructure recognised pursuant to IFRIC 12 (€ 38.3 million); please note that, as specified in section “A. Accounting policies”, such revenue corresponds to the costs incurred during the same period to purchase raw materials and consumables, services and staff which are included in operating expenses.

The increase with respect to 2009 – equal to € 48.8 million – reflects the revenue from increased investments during the year in dispatching infrastructures (€ 8.8 million) and, in particular, the economic effects linked to the DIS component and due to:

- the effects of Resolution 213/09 which redefined – for the period 2010-2012 – the remuneration mechanism that gives Terna incentives to procure resources from the dispatching service market (€ 77.0 million; +€ 37.0 million compared with incentives of € 40.0 million recognized in 2009 on the basis of AEEG 206/08 resolution); more specifically, the result achieved in 2010 has been stated at fair value in view of the three-year nature of the incentives mechanism; the application of AEEG Resolution no. 204/09 concerning rates adjustment for the DIS component in 2010 (+€ 3.5 million);
- Regulating providing incentives for the quality of the transmission service (AEEG resolution 169/08 – +€ 4.4 million);
- Redefinition of the compensation for grouping of measures (ARG/elt resolution 129/10 – -€ 5.1 million).

#### Other energy items – pass-through revenue/costs

This caption includes revenue and costs of a “pass-through” nature for the Group (whose balance is therefore nil) relating entirely to the Parent. They arise in respect of daily purchases and sales with operators on the electricity market to carry out transmission and dispatching activities. To that end, the measurements at each point of input and withdrawal are taken and the differences from the energy market schedules are calculated. These differences (imbalances) are measured using algorithms established by the regulatory framework. The net charge resulting from the measurement of these imbalances and of the buying and selling transactions executed by Terna on the Ancillary Services Markets are billed on a pro rata basis to each consumer with the uplift fee.



It also includes the grid utilisation fee which Terna pays to other owners of the grid.  
The various components of these transactions are analysed below.

| In millions of euros  | 2010           | 2009           | Change        |
|---|----------------|----------------|---------------|
| <b>Revenue - Power Exchange:</b>  |                |                |               |
| - foreign market - exports  | 1.1            | 4.4            | -3.3          |
| - sale of energy on the Day Ahead Market, Adjustment Market, Ancillary Services Market and others | 653.4          | 813.5          | -160.1        |
| - unbalancing and other minor items   | 928.3          | 1,597.4        | -669.1        |
| - ancillary service resources procurement   | 1,152.5        | 980.9          | 171.6         |
| - congestion rent – rights for use of transportation capacity (RTC), Res. no. 288/06              | 821.4          | 733.4          | 88.0          |
| - other items - Power Exchange  | 140.4          | 311.5          | -171.1        |
| - Interconnector/Shipper  | 125.6          | 0.0            | 125.6         |
| <b>Total revenue - Power Exchange</b>   | <b>3,822.7</b> | <b>4,441.1</b> | <b>-618.4</b> |
| Revenue under Res. nos. 168/04 - 237/04 and others  | 817.3          | 613.5          | 203.8         |
| Other items (CBT and other)   | 171.4          | 47.3           | 124.1         |
| Revenue from grid transmission fees of other owners and GRTN share CIP/6                          | 19.2           | 18.7           | 0.5           |
| <b>Total revenue from outside the Power Exchange</b>  | <b>1,007.9</b> | <b>679.5</b>   | <b>328.4</b>  |
| <b>Total pass-through energy revenue</b>  | <b>4,830.6</b> | <b>5,120.6</b> | <b>-290.0</b> |
| <b>Energy purchases:</b>  |                |                |               |
| - on Day Ahead Market and Adjustment Market   | 160.3          | 9.5            | 150.8         |
| - to provide the dispatching service  | 1,664.8        | 2,431.6        | -766.8        |
| - for unbalancing   | 902.7          | 1,373.4        | -470.7        |
| - on the foreign market - imports   | 0.5            | 0.1            | 0.4           |
| - Electricity Market Operator fees  | 2.7            | 2.7            | 0.0           |
| - congestion rent – RTC, res. no. 288/06  | 513.9          | 559.3          | -45.4         |
| - other items - Power Exchange  | 72.7           | 64.5           | 8.2           |
| - Interconnector/Shipper  | 505.1          | 0.0            | 505.1         |
| <b>Total costs - Power Exchange</b>   | <b>3,822.7</b> | <b>4,441.1</b> | <b>-618.4</b> |
| Purchase of electricity market related services   | 817.3          | 613.5          | 203.8         |
| Other items (CBT and other)   | 171.4          | 47.3           | 124.1         |
| Fees to be paid to NTG owners, GRTN and other   | 19.2           | 18.7           | 0.5           |
| <b>Total services and fees</b>  | <b>1,007.9</b> | <b>679.5</b>   | <b>328.4</b>  |
| <b>Total pass-through energy costs</b>  | <b>4,830.6</b> | <b>5,120.6</b> | <b>-290.0</b> |

#### Other revenue from sales and services

Other revenue from sales and services amounted to € 57.0 million and mainly relates to revenue from a variety of specialised high- and very-high-voltage services that the Parent provides to third-party customers (€ 46.2 million). The amount reflects revenue from:

- the operation, maintenance and development of the optical fibre owned by the Wind Group hosted on plants (safety cables) of the Parent (€ 2.2 million);
- NTG connection services, primarily including plants for the production of energy from renewable sources (€ 4.9 million);
- the contribution due to the Parent for coverage of costs incurred for electricity discounts to its employees (€ 1.6 million);
- Management fee services provided to the subsidiary RTR which is being sold (€ 1.8 million).

The increase of € 16.8 million is essentially due to work orders for the realization/expansion of electrical stations and the relative connections to the NTG's requested by third parties.

## 2. Other revenue and income – € 56.1 million

“Other revenue and income” for the years 2010 and 2009 are analysed in the following table:

| In millions of euros                      | 2010        | 2009        | Change      |
|---|-------------|-------------|-------------|
| Rental income                             | 19.9        | 19.4        | 0.5         |
| Sundry grants                             | 9.5         | 9.3         | 0.2         |
| Insurance settlements for losses          | 7.2         | 3.3         | 3.9         |
| Gains on the disposal of plant components | 3.5         | 4.8         | -1.3        |
| Prior period income                       | 6.7         | 4.1         | 2.6         |
| Sales to third parties                    | 2.4         | 1.0         | 1.4         |
| Other revenue                             | 0.9         | 1.5         | -0.6        |
| Gain from purchase at bargain prices      | 6.0         | 0.0         | 6.0         |
| <b>Total</b>                              | <b>56.1</b> | <b>43.4</b> | <b>12.7</b> |

Other revenue and income, totalling € 56.1 million, include € 45.3 million for the Parent and € 10.8 million for the subsidiary TELAT.

Rental income mainly refers to rent from the Wind Group for the housing of optical fibre on the grid (€ 15.3 million) and Enel Distribuzione's use of the Parent's infrastructure for power line communication (€ 2.0 million); it also includes receivable rents from the Parent for the leasing of land to the subsidiary RTR (which is being sold). This land will be used for the construction of photovoltaic plants (€ 0.6 million).

The increase in other revenue and income (€ 12.7 million) is essentially attributable to:

- the gain from bargain purchase (+€ 6.0 million) deriving from the process of allocation of the price paid for the acquisition of the shareholding in Trasmissione Brescia based on the fair value at the date of acquisition of the identifiable net assets acquired;
- increased insurance indemnities (+€ 3.9 million) for damages to plants which primarily occurred in the previous year;
- increased contingent assets (+€ 2.6 million) which were essentially due to the net issue of past accruals to the allowance for impairment of the Parent following the collection of the relative items (€ 1.9 million).

## Operating expenses

## 3. Raw materials and consumables – € 28.2 million

The item totalled € 28.2 million. It comprises costs incurred for the purchase of sundry materials and equipment used in the operation and maintenance of plants. The increase of € 15.8 million with respect to the previous year (€ 12.4 million on 31 December 2009) was primarily attributable to the Parent (+€ 15.2 million) and is essentially due to costs sustained as a result of application of IFRIC 12 for increased investment and development activities pertaining to Dispatching Infrastructures (€ 7.1 million) as well as the consumption of materials for increased maintenance activities of the NTG.

## 4. Services – € 152,2 milioni

The cost of services totalled € 152.2 million, of which € 149.0 million related to the Parent and € 2.8 million was relative to the subsidiary TELAT.

The cost of “Services” for the years 2010 and 2009 is analysed in the following table:

| In millions of euros              | 2010         | 2009         | Change     |
|-----------------------------------|--------------|--------------|------------|
| Tenders on plants                 | 34.9         | 41.1         | -6.2       |
| Maintenance and sundry services   | 62.9         | 61.3         | 1.6        |
| Insurance                         | 6.7          | 6.4          | 0.3        |
| Remote transmission and telephone | 14.2         | 12.6         | 1.6        |
| IT services                       | 21.3         | 14.4         | 6.9        |
| Leases and rentals                | 12.2         | 13.9         | -1.7       |
| <b>Total</b>                      | <b>152.2</b> | <b>149.7</b> | <b>2.5</b> |

The item “Services” refers to costs for tenders and services for routine maintenance operations and plant maintenance and expenditures for general services (a total of € 97.8 million). It also includes costs for IT services (€ 21.3 million) remote transmission and telephone services (€ 14.2 million), leases and rentals (€ 12.2 million), and insurance (€ 6.7 million). The increase (€ 2.5 million) is primarily due to the effects of applying IFRIC 12 for activities associated with the dispatching infrastructures; this resulted in the booking of increased costs totalling € 2.2 million (€ 6.2 million for IT services, +0.6 million for maintenance and miscellaneous services and - € 4.6 million for tenders on primary plants).

Fees paid to the Parent’s Statutory Auditors are detailed in the following table. The table has been prepared on the basis of the term of office of the position on an accruals basis.

| Surname and Name                      | Position                                    | Term of office      | Expiry of term                        | Remuneration      | Total             |
|---------------------------------------|---|---------------------|---------------------------------------|-------------------|-------------------|
| Guarna Luca Aurelio                   | Chairman of the Board of Statutory Auditors | Jan. ‘10 - Dec. ‘10 | Approval of 2010 financial statements | 55,000.00         | 55,000.00         |
| Cosconati Marcello <sup>(*)</sup>     | Statutory Auditor                           | Jan. ‘10 - Dec. ‘10 | Approval of 2010 financial statements | 45,000.00         | 45,000.00         |
| Pozza Lorenzo                         | Statutory Auditor                           | Jan. ‘10 - Dec. ‘10 | Approval of 2010 financial statements | 45,000.00         | 45,000.00         |
| <b>Total Statutory Auditors’ fees</b> |   |                     |                                       | <b>145,000.00</b> | <b>145,000.00</b> |

(\*) Fees for the position were paid to Cassa Depositi e Prestiti.

## 5. Personnel expense – € 212.2 million

“Personnel expense” for the years 2010 and 2009 is analysed in the following table:

| In millions of euros   | 2010         | 2009         | Change      |
|--|--------------|--------------|-------------|
| Wages, salaries and other short-term employee benefits                           | 256.1        | 248.9        | 7.2         |
| Termination indemnities, electricity discount and other post-employment benefits | 15.8         | 15.5         | 0.3         |
| Reversal of provision for electricity discount                                   | 0.0          | -26.8        | 26.8        |
| Early retirement incentives  | 4.6          | 6.5          | -1.9        |
| <b>Personnel expense, gross</b>  | <b>276.5</b> | <b>244.1</b> | <b>32.4</b> |
| Personnel expense, capitalised   | -64.3        | -58.6        | -5.7        |
| <b>Total</b>   | <b>212.2</b> | <b>185.5</b> | <b>26.7</b> |

This caption includes the cost of wages and salaries, social security contributions and other costs incurred by the Parent for early retirement incentives, as well as benefits paid to employees who stay with the company and termination indemnities provided for by the currently effective collective national employment contract for the electricity sector. The increase of € 26.7 million was essentially due to the release, in 2009, of the provision for electricity discount. This followed the undersigning of an agreement with Enel Servizio Elettrico that redetermined the number of retired recipients of this benefit for which the Parent is liable (€ 26.8 million). There is also an increase of employee and social security compensations and other short-term employee benefits (€ 7.2 million) due mainly to the greater per-unit cost. The above-mentioned changes were partly offset by an increase in the personnel expense capitalised (+€ 5.7 million) as a result of greater investment by the Parent during the year.

The fees paid to the Directors of the Parent are summarised in the following table. The table has been prepared on the basis of the term of office of the position on an accruals basis.

| Surname Name                 | Position          | Term of office     | Expiry of term                        | Remuneration     | Bonus and other incentives (***) | Other compensation (****) | Other compensation (*****) | Total            |
|------------------------------|-------------------|--------------------|---------------------------------------|------------------|----------------------------------|---------------------------|----------------------------|------------------|
| Roth Luigi                   | Chairman/Director | Jan. 10<br>Dec. 10 | Approval of 2010 financial statements | 600,000          | 150,000                          |                           | 100,000                    | 850,000          |
| Cattaneo Flavio              | CEO               | Jan. 10<br>Dec. 10 | Approval of 2010 financial statements | 200,000          | 1,200,000                        | 1,000,000                 |                            | 2,400,000        |
| Cannarsa Cristiano (*)       | Director          | Jan. 10<br>Dec. 10 | Approval of 2010 financial statements | 25,000           |                                  |                           |                            | 25,000           |
| Dal Pino Paolo               | Director          | Jan. 10<br>Dec. 10 | Approval of 2010 financial statements | 125,000          |                                  |                           |                            | 125,000          |
| Del Fante Matteo (*)         | Director          | Jan. 10<br>Dec. 10 | Approval of 2010 financial statements | 75,000           |                                  |                           |                            | 75,000           |
| Machetti Claudio (**)        | Director          | Jan. 10<br>Dec. 10 | Approval of 2010 financial statements | 25,000           |                                  |                           |                            | 25,000           |
| Machì Salvatore              | Director          | Jan. 10<br>Dec. 10 | Approval of 2010 financial statements | 135,000          |                                  |                           |                            | 135,000          |
| Polo Michele                 | Director          | Jan. 10<br>Dec. 10 | Approval of 2010 financial statements | 75,000           |                                  |                           |                            | 75,000           |
| Rispoli Vittorio             | Director          | Jan. 10<br>Dec. 10 | Approval of 2010 financial statements | 85,000           |                                  |                           |                            | 85,000           |
| <b>Total Directors' fees</b> |                   |                    |                                       | <b>1,345,000</b> | <b>1,350,000</b>                 | <b>1,000,000</b>          | <b>100,000</b>             | <b>3,795,000</b> |

(\*) Fees for the position were paid to Cassa Depositi e Prestiti;

(\*\*) fees for the position were paid to Enel S.p.A.;

(\*\*\*) this amount refers to the variable portion of fees and compensation relative to the year 2010. It also states that the CEO Flavio Cattaneo there is a way-out of about € 7 million;

(\*\*\*\*) this amount refers to executive compensation;

(\*\*\*\*\* the amount regards compensation for position as Chairman of the Board of Directors of TELAT from 1 January 2010 to 31 December 2010.

The following table shows the number of employees by category at year end and the average number for the year:

|                     | Average number |              | Final number |              |
|---------------------|----------------|--------------|--------------|--------------|
|                     | 2010           | 2009         | 31 Dec. 2010 | 31 Dec. 2009 |
| Senior management   | 64             | 67           | 59           | 65           |
| Junior management   | 495            | 485          | 502          | 488          |
| Office staff        | 1,897          | 1,908        | 1,890        | 1,874        |
| Blue-collar workers | 1,030          | 1,058        | 1,017        | 1,020        |
| <b>Total</b>        | <b>3,486</b>   | <b>3,518</b> | <b>3,468</b> | <b>3,447</b> |

The net change in the average number of employees on the end of 2009 was -32.

Reference should be made to section "25. Employee benefits" 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. Amortisation, depreciation and impairment losses – € 360.7 million

These relate to accruals during the year calculated on the basis of amortisation and depreciation rates that reflect the useful lives of the Group companies' plant, property and equipment and intangible assets (€ 360.5 million), and related write-downs (€ 0.2 million).

The following table details the amortisation, depreciation and impairment losses for the years 2010 and 2009:

| In millions of euros   | 2010         | 2009         | Change      |
|--|--------------|--------------|-------------|
| Amortisation on intangible fixed assets                                  | 45.1         | 39.9         | 5.2         |
| - of which: Infrastructure rights  | 23.7         | 22.7         | 1.0         |
| Depreciation of property, plant and equipment                            | 315.4        | 268.9        | 46.5        |
| Impairment losses on property, plant and equipment and intangible assets | 0.2          | 3.7          | -3.5        |
| Impairment losses on trade receivables                                   | 0.0          | 14.1         | -14.1       |
| <b>Total</b>   | <b>360.7</b> | <b>326.6</b> | <b>34.1</b> |

The increase in the item, totalling € 34.1 million, primarily reflects the growth in depreciation/amortization (€ 51.7 million) with respect to 2009 and attributable to:

- the Parent for € 39.4 million, essentially due to increased property, plants and equipment (+€ 34.4 million) and intangible assets (+€ 5.0 million, of which +1 million ascribable to infrastructure rights) which entered into operation during the year;
- the subsidiary TELAT in the amount of € 12.3 million (compared to the 29.4 million of the last nine months of 2009), including charges for the portion of excess cost definitively allocated to transmission plants and intangible assets (overall +€ 2.4 million) as well as amortization/depreciation of the incorporated company Rete Trasmissione Brescia (+€ 0.5 million).

The change was also affected by the recognition of increased impairment losses, in 2009 on property, plant and equipment and intangible assets (-€ 3.5 million) as well as increased accruals to the allowance for impairment losses in relation to items for which default is probable (-€ 14.1 million).

## 7. Other operating expenses – € 21.5 million

Other operating expenses" for the years 2010 and 2009 are analysed in the following table:

| In millions of euros                     | 2010        | 2009        | Change      |
|--|-------------|-------------|-------------|
| Provisions for risks and charges         | 2.0         | 0.8         | 1.2         |
| Power failure charges                    | 4.0         | 2.8         | 1.2         |
| Indirect and local taxes and duties      | 6.6         | 5.6         | 1.0         |
| Prior year expense                       | 2.7         | 2.3         | 0.4         |
| Losses on the disposal/closure of plants | 0.5         | 3.5         | -3.0        |
| Other operating expenses                 | 5.7         | 6.6         | -0.9        |
| <b>Total</b>                             | <b>21.5</b> | <b>21.6</b> | <b>-0.1</b> |

Other operating expenses are primarily attributable to the Parent (€ 17.8 million) and the subsidiary TELAT (€ 3.6 million).

This item, equal to 21.5 million, was unchanged compared to the balance of the previous year. It decreased by -€ 0.1 million mainly from the combined effect of the following events:

- the booking, in 2009, of increased capital losses for disposals/sales of primary plants (€ 3.0 million);
- allocations, in 2010, to the provisions for charges which are payable to distributing companies for power failures of the transformation plants linked to the NTG (in accordance with Resolution 341/07 – € 0.9 million) as well as for the sharing of indemnities due to final users (€ 0.2 million);
- booking of the contribution for power failure events (in accordance with Resolution 333/07 – € 1.2 million);
- increased taxes, duties and local charges which accrued during the year (€ 1.0 million) and which primarily refer to TARSU (solid waste disposal tax, +€ 0.8 million).

## Financial income and expense

### 8. Net financial expense – -€ 105.1 million

This caption is analysed below:

| In millions of euros   | 2010          | 2009          | Change       |
|--|---------------|---------------|--------------|
| <b>Financial income</b>  |               |               |              |
| Financial income from parents  | -             | 3.1           | -3.1         |
| Interest income from Terna Participações   | -             | 14.3          | -14.3        |
| Interest income and other financial income   | 9.0           | 10.6          | -1.6         |
| Debt adjustment (bonds) and related hedges   | 2.2           | 1.2           | 1.0          |
| <b>Total income</b>  | <b>11.2</b>   | <b>29.2</b>   | <b>-18.0</b> |
| <b>Financial expense</b>   |               |               |              |
| Interest expense on medium/long-term loans and related hedges                        | -121.2        | -147.6        | 26.4         |
| Exchange rate differences and related non-hedge-accounting exchange-rate derivatives | -5.6          | -25.2         | 19.6         |
| Discounting of post-employment benefits and other personnel-related provisions       | -4.9          | -5.7          | 0.8          |
| Financial expense - Parent   | -1.3          | -1.2          | -0.1         |
| Interest expense on short-term loans and other financial expense                     | -0.7          | -11.9         | 11.2         |
| Capitalised borrowing costs  | 17.4          | 11.2          | 6.2          |
| <b>Total expense</b>   | <b>-116.3</b> | <b>-180.4</b> | <b>64.1</b>  |
| <b>Total</b>   | <b>-105.1</b> | <b>-151.2</b> | <b>46.1</b>  |

Net financial expense amounted to € 105.1 million, entirely attributable to the Parent, comprising € 116.3 million in financial expense and € 11.2 million in financial income. The decrease of € 46.1 million with respect to the previous year is primarily due to the following main factors:

- financial income which accrued in 2009 with respect to CDP bonds subscribed by Terna and reimbursed in the same year (-€ 3.1 million);
- interest income accrued during 2009 on the financing between Terna and Terna Participações (-€ 14.3 million);
- decreased financial income (-€ 1.6 million) which was primarily attributable to the joint effect of:
  - decreased invested liquid funds and decreased interest rates (-€ 5.8 million);
  - increased interest on arrears debited in 2009 as a result of the delayed payment of receivables deriving from dispatching activities (€ 1.8 million);
  - booking of net uplift proceeds in 2010 (+€ 2.3 million) compared to the negative balance (€ 11.8 million, booked under financial expense) of the previous year;
  - increased interest income accrued on short-term securities issued by UBS and MPS (+€ 4.0 million);
- positive economic effects deriving from the fair value adjustment of bonds and the relative hedges (€ 1.0 million);
- decreased financial charges relating to medium to long-term debt (€ 26.4 million) caused by a decrease in interest rates which was partially compensated by the increase in debt;
- the positive impact (€ 19.6 million) mainly of the 2009 reporting of charges on hedges not qualifying for hedge accounting to mitigate the risk associated with the volatility of exchange rates with respect to dividends and intercompany loan payments from Terna Participações;
- reductions in interest expense on short-term loans and in other financial expense (€ 11.2 million) due almost entirely to the uplift charges recognised in 2009;
- lower financial expense deriving from the discounting of employee benefits (€ 0.8 million);
- increased capitalized financial expense (€ 6.2 million) due to greater capital expenditure during the year.

## 9. Share of profit/(loss) from equity-accounted investees – € 2.6 million

This item refers to the economic effects of adjusting the investment in the associate company CESI S.p.A. to equity held at 31 December 2010 (€ 3.2 million, an increase of € 0.3 million with respect to 2009) as well as the impairment losses on the investment in ELMED Études (-€ 0.6 million), a Tunisian joint venture, following the changed political situation in Tunisia which currently renders the recovery of the investment difficult.

## 10. Income taxes – € 245.2 million

Income taxes for the year amount to € 245.2 million.

The following table reports changes in taxes with respect to 2009:

| In millions of euros                                       | 2010         | 2009         | Change       |
|--|--------------|--------------|--------------|
| <b>Income taxes of the year</b>                            |              |              |              |
| Current taxes:   |              |              |              |
| - IRES   | 237.4        | 177.1        | 60.3         |
| - IRAP   | 58.9         | 53.9         | 5.0          |
| <b>Total current taxes</b>                                 | <b>296.3</b> | <b>231.0</b> | <b>65.3</b>  |
| New temporary differences:                                 |              |              |              |
| - deferred tax assets                                      | -13.9        | -14.2        | 0.3          |
| - deferred tax liabilities                                 | -            | -            | -            |
| Reversal of temporary differences:                         |              |              |              |
| - deferred tax assets                                      | 11.5         | 16.7         | -5.2         |
| - deferred tax liabilities                                 | -43.7        | -36.2        | -7.5         |
| <b>Total change in deferred tax assets and liabilities</b> | <b>-46.1</b> | <b>-33.7</b> | <b>-12.4</b> |
| Adjustment of prior-year taxes                             | -5.0         | -5.2         | 0.2          |
| <b>Total</b>   | <b>245.2</b> | <b>192.1</b> | <b>53.1</b>  |

### Current taxes

Current taxes have increased by € 65.3 million compared to the balance of 2009; this was essentially due to the higher pre-tax profit.

### Deferred tax assets and liabilities

Deferred tax assets and liabilities, totalling -€ 46.1 million, showed a net increase of € 12.4 million with respect to 2009. The change is mainly attributable to:

- decreased set-offs for advance taxes (-€ 4.9 million) which were primarily due to bookings, in 2009, on the part of the Parent for both the provisions for energy discounts following the previously mentioned agreement with Enel Servizio Elettrico (-€ 7.4 million) as well as the allowance for impairment (+€ 2.2 million); the decreased accruals to the provisions for employee benefits (+€ 0.9 million) as well as deferred tax assets on the subsidiary TELAT's accruals with respect to the results of the general equalization (Leg. Decree 348/07 and its subsequent amendments – -€ 1.6 million) were also booked;
- higher utilization of deferred tax liabilities (-€ 7.5 million), largely due to the accelerated depreciation in the year with respect to that recorded by the Parent (-€ 3.6 million) and TELAT (-€ 4.2 million having regard also for the effect of transferring certain transmission plants to the Parent and for the greater value allocated to the NTG and its intangible assets).



### Adjustment of prior-year taxes

Adjustments of taxes referring to previous years, and equal to -€ 5.0 million, primarily refer to increased current taxes paid in past years.

The effective rate of income tax (which totalled € 245.2 million) on taxable income came to 34.4% (equal to 35.1%, without taking into account adjustments from previous years), down from 35.2% in 2009 (equal to 36.1%, without taking into account adjustments from previous years).

For a clearer presentation of the differences between the theoretical and actual tax rates, the table below reconciles the profit before taxes with taxable income for IRES (corporate income tax) purposes:

| In millions of euros                            | 2010         | 2009         |
|---|--------------|--------------|
| Profit before taxes                             | 711.9        | 546.1        |
| <b>Theoretical tax charge</b>                   | <b>195.8</b> | <b>150.2</b> |
| IRAP  | 58.9         | 53.9         |
| Permanent differences                           | -4.5         | -6.8         |
| <b>Actual tax charge</b>                        | <b>250.2</b> | <b>197.3</b> |
| <b>Actual tax rate</b>                          | <b>35.1%</b> | <b>36.1%</b> |
| Adjustment of prior-year taxes                  | -5.0         | -5.2         |
| <b>Actual tax net of prior year adjustments</b> | <b>245.2</b> | <b>192.1</b> |

## 11. Profit from discontinued operations and assets held for sale – € 146.9 million

This item essentially includes the valuation of the margin which accrued with respect to the construction of photovoltaic plants which are subject to transfer along with the sale of the companies RTR and Valmontone. In particular, and as a result of the sales agreement, the group of photovoltaic plants of RTR and Valmontone Energy, as described in the Directors' Report, are structured as a contracted construction agreement where the customer is the buyer Terra Firma Investments (GP) 3 Limited. The revenues and costs for construction are booked on the basis of the progress of works on 31 December 2010 by means of the cost to cost method.

The capital gain realized from the sale of the residual shareholding in Terna Participações (10,000 units) in response to the Public Offer on 6 May 2010 by Alterosa, the company deriving from the partial spin-off from TAESA S.A., which acquired control over it during the course of 2009 (€ 0.1 million).

The previous year, in fact, reported the result attained through the sale of the Brazilian subsidiaries, overall totalling € 417.0 million.

The economic items which resulted in the net income of the year for discontinued operations and assets held for sale, totalling € 146.9 million (detailed below, are commented in the following paragraphs:

| In millions of euros   | 2010         | 2009         | Change        |
|--|--------------|--------------|---------------|
| Total revenue  | 503.3        | 198.8        | 304.5         |
| Total operating expenses   | -355.3       | -72.1        | -283.2        |
| <b>Operating profit (EBIT)</b>   | <b>148.0</b> | <b>126.7</b> | <b>21.3</b>   |
| Net financial expense  | 0.0          | -28.7        | 28.7          |
| <b>Pre-tax profit</b>  | <b>148.0</b> | <b>98.0</b>  | <b>21.3</b>   |
| Income taxes   | -1.2         | -31.9        | 30.7          |
| <b>Profit for the year</b>   | <b>146.8</b> | <b>66.1</b>  | <b>52.0</b>   |
| <b>Attributable to the owners of the Parent</b>  | <b>146.8</b> | <b>43.6</b>  | <b>103.2</b>  |
| Net capital gain   | 0.1          | 305.0        | -304.9        |
| Translation reserve  | 0.0          | 68.4         | -68.4         |
| <b>Profit from discontinued operations and assets held for sale attributable to the owners of the Parent</b> | <b>146.9</b> | <b>417.0</b> | <b>-270.1</b> |

### Total revenue

This item essentially includes the valuation of the contractual compensation for the work order relative to the construction of photovoltaic plants as of 31 December 2010; this valuation was determined on the basis of the work progress status and the overall costs which were sustained during the year compared to those which were overall attributed to the work order itself (€ 501.7 million).

### Total operating expenses

The operating expenses essentially refer to work order costs which were incurred for investments made to construction photovoltaic plants which were in operation and in construction on 31 December 2010 (equal to 352.7 million).

The profit from discontinued operation and assets held for sale for the year therefore totalled € 146.8 million.

The amounts of earnings per share and diluted earnings per share of discontinued operations and assets held for sale were equal to € 0.073 (numerator equal to € 146.9 million, reflecting the profit from discontinued operations and assets held for sale, while the denominators were 2,004,395.7 thousand and 2,009,992.0 thousand, respectively).

## 12. Earnings per share

The basic and diluted earnings per share from continuing and discontinued operations and assets held for sale are, respectively, € 0.306 (numerator of € 613.6 million being the sum of the profit from continuing operations, € 466.7 million, and that from discontinued operations and assets held for sale, € 146.9 million, and denominator of 2,004,395.7 thousand) and € 0.305 (numerator of € 613.6 million and denominator of 2,009,992.0 thousand).

The basic and diluted earnings per share from continuing operations are, respectively, € 0.233 (numerator of € 466.7 million and denominator of 2,004,395.7 thousand) and € 0.232 (numerator of € 466.7 million and denominator of 2,009,992.0 thousand).



## D. Notes to the consolidated statement of financial position

### Assets

#### 13. Property, plant and equipment – € 7,802.6 million

Property, plant and equipment amount to € 7,802.6 million (€ 6,989.9 million at 31 December 2009). The amount and changes for each category are reported in the following table:

|   | Land        | Buildings     | Plant and machinery | Industrial and commercial equipment | Other assets | Assets under construction and payments on account | Total           |
|---|-------------|---------------|---------------------|-------------------------------------|--------------|---|-----------------|
| In millions of euros  |             |               |                     |                                     |              |   |                 |
| <b>Cost at 1 January 2010</b>   | <b>53.1</b> | <b>822.5</b>  | <b>10,235.0</b>     | <b>53.3</b>                         | <b>84.2</b>  | <b>883.1</b>                                      | <b>12,131.2</b> |
| Re-classified cost of assets held for sale  | -           | -             | -3.3                | -                                   | -            | -2.4  | -5.7            |
| Investment  | 3.6         | 1.8           | 11.1                | 3.9                                 | 4.0          | 1,080.0   | 1,104.4         |
| Entry into use  | 24.2        | 134.2         | 866.8               | 5.6                                 | 5.4          | -1,036.2  | 0.0             |
| Contribution of newly acquired companies  | -           | 0.3           | 53.7                | -                                   | -            | -   | 54.0            |
| Disposals and impairment losses   | -           | -0.4          | -54.2               | -0.1                                | -0.6         | -0.2  | -55.5           |
| Other changes (grants)  | -           | -             | -18.0               | -                                   | -            | 5.8   | -12.2           |
| Reclassifications   | 0.8         | -0.4          | -0.4                | -                                   | 0.1          | -   | 0.1             |
| <b>Cost at 31 December 2010</b>   | <b>81.7</b> | <b>958.0</b>  | <b>11,090.7</b>     | <b>62.7</b>                         | <b>93.1</b>  | <b>930.1</b>                                      | <b>13,216.3</b> |
| <b>Accumulated depreciation and impairment losses at 1 January 2010</b>             | <b>0.0</b>  | <b>-266.1</b> | <b>-4,793.4</b>     | <b>-38.3</b>                        | <b>-43.5</b> | <b>0.0</b>  | <b>-5,141.3</b> |
| Reclassified accumulated depreciation and impairment losses of assets held for sale | -           | -             | -                   | -                                   | -            | -   | 0.0             |
| Depreciation for the year   | -           | -20.4         | -279.6              | -3.2                                | -12.2        | -   | -315.4          |
| Contribution of newly acquired companies  | -           | -             | -10.6               | -                                   | -            | -   | -10.6           |
| Disposals   | -           | 0.4           | 52.7                | 0.1                                 | 0.4          | -   | 53.6            |
| Reclassifications   | -           | -             | 0.1                 | -                                   | -0.1         | -   | 0.0             |
| <b>Accumulated depreciation and impairment losses at 31 December 2010</b>           | <b>0.0</b>  | <b>-286.1</b> | <b>-5,030.8</b>     | <b>-41.4</b>                        | <b>-55.4</b> | <b>0.0</b>  | <b>-5,413.7</b> |
| <b>Carrying amount</b>  |             |               |                     |                                     |              |   |                 |
| At 31 December 2010   | 81.7        | 671.9         | 6,059.9             | 21.3                                | 37.7         | 930.1   | 7,802.6         |
| At 31 December 2009   | 53.1        | 556.4         | 5,441.6             | 15.0                                | 40.7         | 883.1   | 6,989.9         |

The category “Plants and machinery”, as of 31 December 2010, includes the energy transportation network as well as the transformation stations in Italy.

In addition to ordinary movements during the year which refer to investments (€ 1,104.4 million, of which € 17.4 million are relative to capitalized financial expense), disinvestments, write-downs and other movements (€ 14.0 million) and amortization/depreciation (€ 315.4 million), this item includes the fair value of property, plant and equipment deriving from the acquisition – completed on 5 August 2010 - of the company Rete Trasmissione Brescia S.r.l. (€ 43.4 million, of which € 9.6 million relative to leased goods which were redeemed during the course of October 2010) which owns a portion of the National Transmission Grid (NTG) and the relative bays in addition to an electrical station. As described in more detail in the paragraph “Business combinations” (refer to this section for more details), the determination of the fair value of plants falling under the portion of the NTG which was acquired with the company Rete Trasmissione Brescia is derived from the process of allocation of the purchase price which was implemented on the basis of a specific valuation on the part of independent professionals.

A summary of the movements of property, plant and equipment during the year – net of the re-classification of the value of the company RTR under the item “Discontinued operations and assets held for sale”, totalling € 5.7 million - is reported below:

In millions of euros

|  |                |
|--|----------------|
| Investment                                     |                |
| - Transmission lines                           | 511.0          |
| - Transformation stations                      | 468.0          |
| - Other additions                              | 124.4          |
| <b>Total core business investments</b>         | <b>1,103.4</b> |
| Photovoltaic                                   | 1.0            |
| <b>Total investments</b>                       | <b>1,104.4</b> |
| Contribution of newly acquired companies       | 43.4           |
| Depreciation                                   | -315.4         |
| Disposals, impairment losses and other changes | -14.0          |
| <b>Total</b>                                   | <b>818.4</b>   |

Capital expenditure for the year of the core business (€ 1,103.4 million, of which € 1,063.4 million for the Parent, € 40.0 million for TELAT) comprises, in particular, expenditure on the Italian transmission grid, owned by the Parent, which mainly regarded: the completion of the laying of submarine cable of the second SA.PE.I. connection hub (Sardinia-Italian peninsula) for a total of 425 km (€ 168.6 million); the opening of work yards and the preparation of materials for the long-distance power line in alternating current “Sorgent Rizziconi” as well as the realization of civil works relative for the conversion stations Scilla, Villafranca and Sorgente (€ 61.1 million); the works relative to the realization of the 380/150 kV stations for the connection to new wind-power production plants between Foggia and Benevento (€ 47.5 million); progress of works for the rationalization of the city of Turin (€ 34.0 million); progress of works for rationalization activities within the province of Lodi and the opening of work yards for the construction of two new electrical stations of 380 kV within the communes of Chignolo Po and Maleo as well as the construction of a new connection in double cable groups along the line “La Casella-Caorso” (overall € 31.7 million); the completion of activities relative to the connection Casellina-Tavarnuzze-S. Barbara (partly aerial line) of 380 kV (€ 22.1 million); the progress of preliminary activities which aim to realize the Italia Montenegro connection (€ 19.5 million).

Following the application – as at 1 January 2010 - of IFRIC 12 (discussed in more detail in section “A. Accounting policies”), the property, plant and equipment identified within the realm of application of IFRIC 12 as dispatching activities have been reclassified to the “Infrastructure rights” item within intangible assets; accordingly, the corresponding amounts in the balance sheet at 31 December 2009 have also been reclassified in the same way. In particular, the carrying amount at 31 December 2009 of the infrastructure relating to the concession arrangements covered by IFRIC 12 (€ 85.4 million) has been reclassified from “Property, plant and equipment” to “Intangible assets”.

In terms of assets under construction at the end of the year, the main grid development and re-powering projects worth more than € 10 million are listed below.

| <b>Transmission lines</b>                    | <b>Euro</b> |
|--|-------------|
| Sorgente-Rizziconi 380 kV power line         | 51,131,685  |
| La Casella-Caorso                            | 37,805,526  |
| Valcamonica (Phase A1)                       | 28,630,604  |
| C.P. Ionadi                                  | 19,654,889  |
| Italy-Montenegro Interconnections            | 18,085,441  |
| Turin rationalisation – 220 kV               | 16,928,576  |
| S. Barbara-Tavarnuzze-Casellina              | 15,605,272  |
| Restructuring of metropolitan area of Rome   | 14,493,937  |
| Torino-Lacchiarella 380 kV power line        | 13,515,059  |
| <b>Transformation stations</b>               |             |
| Scilla 380/150 kV station                    | 27,903,075  |
| ATR-TR National Reserve                      | 20,991,370  |
| Deliceto 380/150 kV station                  | 17,138,783  |
| Troia 380 kV station                         | 16,410,241  |
| SA.PE.I. station (Fiumesanto and Latina)     | 16,018,275  |
| Station of Cardano-Nuovi armoured department | 15,312,537  |
| Villafranca 380/150 kV station               | 15,156,195  |
| Sorgente 380/220 kV station                  | 14,119,881  |
| Augusta 150 kV station                       | 11,412,581  |
| Villanova 380 kV station                     | 10,982,357  |
| Casuzze 150 kV station                       | 10,291,129  |

## 14. Goodwill – € 190,2 million

Goodwill amounted to € 190.2 million and it is unchanged as compared to the balance of the previous year.

### Impairment testing

#### Cash Generating Unit – Terna

The recoverable amount of the goodwill (recognised as a result of the merger of RTL into Terna in 2008) with respect to the Terna Cash Generating Unit (CGU) booked in the financial statements, € 88.6 million, was estimated using the unlevered version of the discounted cash flow method; the latter estimates future cash flows and applies an appropriate discount rate. The discounting of the cash flows was performed with respect to the period 2010-2020 and the final value was assumed to be equal to the RAB (Regulatory Asset Base) in 2020. In particular, cash flows were determined, up to 2015, on the basis of the approved business plan, drawing on the forecasts and assumptions it uses for developments in Terna's performance and financial position, while for subsequent years the cash flow projection was based on the development of investments provided in the most recently approved Grid Development Plan and assuming business development operations in line with the last year of the business plan. The discount rate was set at a WACC of 4.78%.

The value in use thus determined was higher than the carrying amount.

#### Cash Generating Unit – TELAT

The recoverable amount of the goodwill recognised in the financial statements, € 101.6 million, recognised as a result of the acquisition of TELAT was also estimated by applying the unlevered version of the discounted cash flow method to the Cash Generating Unit (CGU) – TELAT.

Cash flow forecasts were implemented, even for this year, across the 2011-2020 time period on the basis of the forecasts and assumptions contained within the business plan and by assuming – from 2016 – a growth in operations which is in line with the last year of this plan. The final value was assumed to be equal to the RAB (Regulatory Asset Base) at the end of 2020 and the adopted discount rate was equal to 4.78%.

The value in use thus determined was higher than the carrying amount.

## 15. Intangible assets – € 280.4 million

Changes during the year in intangible assets are detailed below:

| In millions of euros               | Infrastructure rights | Concessions  | Other assets | Assets under construction and advances | Total        |
|------------------------------------|-----------------------|--------------|--------------|--|--------------|
| <b>Balance at 31 December 2009</b> | <b>98.7</b>           | <b>112.1</b> | <b>35.1</b>  | <b>21.5</b>                            | <b>267.4</b> |
| Investment                         | -                     | -            | 0.0          | 58.3                                   | 58.3         |
| Entry into use                     | 32.4                  | -            | 17.7         | -50.1                                  | 0.0          |
| Amortisation                       | -23.7                 | -5.6         | -15.8        | -                                      | -45.1        |
| Other changes (grants)             | -0.2                  | -            | -            | -                                      | -0.2         |
| Reclassifications                  | -0.8                  | -            | 0.8          | -                                      | 0.0          |
| <b>Balance at 31 December 2010</b> | <b>106.4</b>          | <b>106.5</b> | <b>37.8</b>  | <b>29.7</b>                            | <b>280.4</b> |
| Cost                               | 239.6                 | 135.4        | 111.9        | 29.7                                   | 516.6        |
| Accumulated amortisation           | -133.2                | -28.9        | -74.1        | -                                      | -236.2       |
| <b>Balance at 31 December 2010</b> | <b>106.4</b>          | <b>106.5</b> | <b>37.8</b>  | <b>29.7</b>                            | <b>280.4</b> |

Intangible assets amount to € 280.4 million (€ 267.4 million at 31 December 2009). This item, in particular, includes:

- the infrastructure used for the dispatching service, recognised as of 1 January 2010 in application of IFRIC 12 (discussed in more detail in section “A. Accounting policies”), with a net carrying amount at 31 December 2010 of € 106.4 million for infrastructure already in use and € 25.1 million for the infrastructure under construction classified under “assets under construction and advances” caption, and a net carrying amount at 31 December 2009, of € 98.7 million for infrastructure already in use and € 18.5 million for the infrastructure under construction classified in the “assets under construction and advances” caption;
- the licensing for the provision of electricity transmission and dispatching services in Italy (with a net carrying amount of € 106.5 million at 31 December 2010), recognised initially during 2005 at fair value and subsequently measured at cost.

The other intangible assets comprise application software developed internally or purchased when implementing systems development projects.

The increase of intangible assets with respect to the prior year (€ 13.0 million) is due to routine movements during the period, regarding mainly to investments (€ 58.3 million, including € 38.6 million in Infrastructure rights) – mainly in application software – and amortisation (€ 45.1 million, of which € 23.7 million in relation to dispatching infrastructure and € 5.6 million relative to licensing).

Investments for the year in intangible assets (€ 58.3 million, of which € 57.0 million refer to the Parent and € 1.3 million to the subsidiary TELAT) included expenditure on the development and evolution of software for the remote management system for dispatching (€ 12.7 million), for the Power Exchange (€ 9.5 million) and for the protection of the electrical system (€ 0.6 million), as well as general applications and software licenses (€ 17.8 million).

## 16. Equity-accounted investees – € 23.6 million

This item amounts to € 23.6 million and relate to the shareholdings of Terna S.p.A.:

- in the associate CESI S.p.A. (€ 23.3 million), representing a stake of 39.91%;
  - in the associate CORESO S.A. (€ 0.3 million), which was acquired in November 2010, representing a stake of 22.485%.
- CESI S.p.A. operates in the construction and management of laboratories and plants for tests, inspections, studies and experimental research relating to the electro-technical field in general and technical and scientific developments in that area. The value of the shareholding increased on previous year as a result of the recognition of the cost incurred for the acquisition (completed by the Parent in December 2010) of additional interests in the associate CESI (€ 5.3 million) from Ansaldo Trasmissione & Distribuzione S.p.A., amounting to 9%, and the adjustment of the investment to the share of equity held by the Group at the end of the year (€ 3.2 million).

As permitted by current regulations, CESI opted not to apply IFRS to the preparation of its financial statements at 31 December 2010. Consequently, its financial statements at 31 December 2010 were prepared in accordance with Italian GAAP. The company CORESO S.A. is the first technical centre owned by various electrical energy transmission companies which implements joint TSO technical coordination activities in order to improve and strengthen security and coordination of the electrical system in central/western Europe; it prepares daily forecasts and analyses in real of energy flows in the region, identifying potentially critical areas and promptly notifying the TSO's which are affected. For more information, please see the section “Significant events”.



The carrying amount of the 50% investment in the joint venture ELMED Études Sarl was fully impaired with respect to the carrying amount at 31 December 2009 due to the impairment losses on the investment itself (-€ 0.7 million) which were recognised as a result of the changed political situation in Tunisia which occurred during the year and which currently makes the investment difficult to recover.

In April 2009, ELMED Études Sarl was established. This limited-liability company is an equally-held joint venture between Terna and Société Tunisienne de l'Electricité et du Gaz (STEG) whose main purpose is the study and preliminary consulting concerning the preparation of documents for the Tunisian government's call for tenders for the construction and management of the power generation hub in Tunisia for the Italy-Tunisia interconnection project.

The main figures of the above-mentioned associate, restated in accordance with the presentation and measurement criteria applied by Terna Group, are as follows:

| Company              | Assets  |             | Liabilities |             | Equity | Revenue | Profit for the year |
|----------------------|---------|-------------|-------------|-------------|--------|---------|---------------------|
|                      | current | non-current | current     | non-current |        |         |                     |
| In millions of euros |         |             |             |             |        |         |                     |
| CESI                 | 72.8    | 45.0        | 28.8        | 30.2        | 58.8   | 76.4    | 10.9                |
| CORESO               | 0.8     | 1.9         | 1.4         | -           | 1.3    | 3.5     | 0.1                 |
| ELMED Études         | 1.4     | -           | 0.1         | -           | 1.3    | 0.1     | -0.1                |

## 17. Financial assets

The following table details financial assets recognised in the consolidated financial statements:

| In millions of euros                | Carrying amount |              | Change        |
|-------------------------------------|-----------------|--------------|---------------|
|                                     | 31 Dec. 2010    | 31 Dec. 2009 |               |
| FVH derivatives                     | 200.3           | 123.2        | 77.1          |
| Other investments                   | 0.5             | 0.0          | 0.5           |
| <b>Non-current financial assets</b> | <b>200.8</b>    | <b>123.2</b> | <b>77.6</b>   |
| Other current financial assets      | 0.5             | 501.0        | -500.5        |
| <b>Current financial assets</b>     | <b>0.5</b>      | <b>501.0</b> | <b>-500.5</b> |

At 31 December 2010 "Non-current financial assets", equal to 200.8 million, reported the value of fair value hedge derivatives hedging against of bonds as well as the value of other shareholding of the Parent.

The increase in the fair value of the derivatives (€ 77.1 million) compared with 31 December 2009 is essentially attributable to the decline in market interest rates during the course of 2010 and is offset by the fair value increase of the bonds recorded within financial liabilities.

The value of "Other investments" refers to the quotas owned by Terna S.p.A. in the share capital of DESERTEC Industrial Initiative ("DII") and equal to 5.6% (€ 0.1 million), as well as in the share capital of CASC CWE S.A., equal to 8.3% (€ 0.3 million); the latter were respectively acquired during the months of September and November 2010. This item also includes the advance paid by Terna (€ 0.1 million) on 7 December 2010, in accordance with contractual agreements, for the founding of the company MEDGRID S.A.S. which occurred on 7 January 2011 with a shareholding of 5% of the share capital.

For more information, please see the section "Significant events".

"Other current assets" amount to € 0.5 million (€ 501.0 million at 31 December 2009) and mainly relate to deferred financial assets. The decrease with respect to the previous year, equal to € 500.5 million, is primarily due to the redemption – during the course of 2010 – of securities undersigned with UBS and MPS in 2009 (-€ 500.0 million).

## 18. Other assets

“Other assets” are analysed below:

| In millions of euros              | 31 Dec. 2010 | 31 Dec. 2009 | Change       |
|-----------------------------------|--------------|--------------|--------------|
| Receivables due from others:      |              |              |              |
| - loans and advances to employees | 5.9          | 5.1          | 0.8          |
| - deposits with third parties     | 0.4          | 0.4          | 0.0          |
| <b>Other non-current assets</b>   | <b>6.3</b>   | <b>5.5</b>   | <b>0.8</b>   |
| <b>Other tax assets</b>           | <b>4.6</b>   | <b>17.9</b>  | <b>-13.3</b> |
| Receivables due from others:      |              |              |              |
| - advances to employees           | 0.2          | 0.2          | 0.0          |
| - others                          | 15.5         | 9.5          | 6.0          |
| <b>Other current assets</b>       | <b>20.3</b>  | <b>27.6</b>  | <b>-7.3</b>  |

**Other non-current assets** (€ 6.3 million) – which are reported in the table above – are essentially unchanged since the end of last year (€ 5.5 million) and mainly comprise loans and advances paid to employees of the Parent (€ 5.9 million).

The item **Other current assets**, equal to € 20.3 million and whose composition is reported in the previous statement, decreased by € 7.3 million compared to 31 December 2009 and is essentially due to the following factors:

- other minor tax assets (€ 13.3 million), mainly related to:
  - a reimbursement of receivables due to the Greek tax authorities for indirect taxes relative to activities implemented by the branch company of Terna in Greece (-€ 8.8 million);
  - decreased withholding taxes on interest income accrued on investments (-€ 1.6 million);
- receivables from others (€ 6.0 million), mainly regarding:
  - increased quotas of previously paid costs which accrue in subsequent years (€ 1.7 million) and which are primarily ascribable to insurance premiums;
  - the booking of revenues which accrued during the year and which were not yet collected on the date of the financial statements (€ 2.0 million) and relative to power line rentals from Enel Distribuzione;
  - increased receivables for insurance reimbursements accrued in the year but still not paid (about € 1.9 million).

## 19. Inventories – € 11.4 million

Current asset inventories (€ 11.4 million) refer to a balance that entirely refers to the Parent and which has not undergone any significant changes with respect to the previous year (€ 11.7 million); it relates to materials and devices allocated for operational, maintenance and construction activities of plants in Italy.

## 20. Trade receivables – € 1,495.8 million

Trade receivables are analysed as follows:

| In millions of euros              | 31 Dec. 2010   | 31 Dec. 2009   | Change       |
|-----------------------------------|----------------|----------------|--------------|
| Energy-related receivables        | 1,117.0        | 843.9          | 273.1        |
| Grid transmission fees receivable | 304.8          | 284.6          | 20.2         |
| Other trade receivables           | 74.0           | 40.6           | 33.4         |
| <b>Trade receivables</b>          | <b>1,495.8</b> | <b>1,169.1</b> | <b>326.7</b> |

Trade receivables amount to € 1,495.8 million. The increase (€ 326.7 million) with respect to the previous year mainly comprises pass-through amounts deriving from the electricity dispatching activities carried out by the Parent. Receivables are measured net of impairment losses, relating to items considered uncollectible and recognised as an adjustment in the allowance for impairment (€ 16.8 million for energy items and € 6.7 million for other items in 2010, compared with € 22.3 million for energy-related items and € 4.7 million for other items in 2009).

#### **Energy-related receivables – € 1,117.0 million**

They mainly include receivables in relation to pass-through energy items arising in respect of dispatching activities. This item also includes receivables for fees payable by market operators for dispatching activities (DIS fee as per AEEG Resolution no. 237/04 and its subsequent amendments and supplements).

The increase in this caption of € 273.1 million with respect to the previous year was mainly due to:

- additional receivables for the accrued incentives associated with the reduction in volumes procured from the dispatching service market, made available under AEEG Resolution 213/09 (+€ 77.0 million compared with the incentive reported in the previous year on the basis of Resolution ARG/elt 206/08);
- Increased receivables from the sale of electrical energy within the power exchange (€ 105.7 million) which were primarily due to the net effect of increased receivables for the uplift component (€ 136.1 million) as well as the booking of receivables for virtual interconnection activities (€ 35.2 million), the compensation used to cover the costs for modulating wind production (in accordance with article 44-*bis* of AEEG resolution 111/06, totalling € 19.5 million), the dispatching of electrical energy produced by non-programmable renewable resources pursuant to resolution ARG/elt 5/10 (€ 11.6 million) and the increased receivables generated from the increase in volumes of resources attained from the energy market (€ 21.3 million); these were partly compensated by the decreased receivables generated from the reduction of quantities and the reduction in valuation prices of the imbalance as well as the advance invoicing of balances required by resolution AEEG 34/09 (€ 60.4 million) and decreased receivables (€ 58.3 million) which, in particular, refer to the mechanism for compensating costs correlated to energy transmissions across foreign electrical networks and the balance for delayed adjustments relative to 2008 on the basis of resolution ARG/elt 111/10;
- Increased receivables from the sale of electrical energy outside of the power exchange (€ 81.4 million) which essentially refer to the dispatching service for energy collection; these are due from market operators.

#### **Grid transmission fees receivable – € 304.8 million**

The receivable relative to grid transmission fees, equal to € 304.8 million, refer to the compensation due to the Parent and other owners for utilization of the National Transmission Grid from distributors of electrical energy; it primarily refers to the fee which accrued in the last two months of the year, with a normal expiration date in the months of the January and February 2011. The above-mentioned receivable reported a positive change equal to € 20.2 million compared to the previous year; this was primarily due to the effect of the incentive from CCSE on the remuneration of investments in strategic transmission infrastructures (resolution ARG/elt 87/10 – +€ 16.8 million) as well as rate adjustments.

#### **Other trade receivables – € 74.0 million**

Other trade receivables mainly regard receivables due from clients of the diversified businesses; they reported an increase of € 33.4 million with respect to the previous year and primarily due to:

- increased receivables due from Italian customers of the Parent (+€ 15.9 million) and which are primarily derived from orders underway with third party customers in relation to stations and connections;
- increased trade receivables due from third parties to the subsidiary TELAT (+€ 7.7 million) and which are primarily due to contributions against plant investments which were invoiced at the end of the year for line interventions/changes (€ 5.8 million, of which € 5.5 million for the contributions invoiced for the restructuring of the electrical network in the Vesuvian area) as well as the receivable due from A2A Reti Elettriche for the lump-sum compensation relative to the September-December period (€ 0.8 million) as well as the receivables brought by the acquired company Rete Trasmissione Brescia and deriving from orders from third party customers (€ 1.2 million);
- receivables for invoices to be issued by the Parent for the sale, in accordance with specific contractual agreements, of photovoltaic panels (€ 15.3 million) to contracting companies entrusted with the realization of photovoltaic plants owned by the subsidiary RTR.

This item also includes receivables for contract work in progress (€ 1.1 million) relative to works of multi-year duration which the Parent has been implementing with third party customers and which decreased with respect to the previous year by € 1.5 million.

The guarantees given to third parties by Terna at 31 December 2010 totalled € 19.6 million. They comprise payable sureties issued to secure the contractual obligations arising in relation to operating activities.





## 21. Cash and cash equivalents – € 150.1 million

Cash and cash equivalents 31 December 2010 refer entirely to the Parent and total € 150.1 million, of which € 150.0 million as liquidity invested in deposits which are available in the short term and € 0.1 million as cash provisions provided to territorial operational areas.

## 22. Tax assets - € 16.8 million

Tax assets totalled € 16.8 million and refer to deferred tax assets which accrued as a result of the exemption of goodwill arising in the merger of the subsidiary RTL into Terna (€ 12.6 million) and the recognition, pursuant to art. 6 of the Law of 28 January 2009, of the receivable due from tax authorities for excess income taxes paid in previous years as a result of not deducting IRAP in the amount provided for under the law (€ 4.2 million).

The decrease of € 1.6 million in this item with respect to the previous year is exclusively due to the release of the quota of the year of the substitute tax paid under art. 15 of Legislative Decree no.185/2008 to release the goodwill that arose on the merger by incorporation of RTL.

## Liabilities

## 23. Equity attributable to the owners of the Parent – € 2,760.6 million

### Share capital – € 441.0 million

The share capital of the Parent is represented by 2,004,395,700 ordinary shares, par value € 0.22 each. The increase of € 0.8 million with respect to the previous year reflects the issue of 3,486,900 shares, during the period, to service the Stock Option Plan described later in this report.

### Legal reserve - € 88.0 million

Terna S.p.A.'s Shareholders' Meeting that met on 13 May 2011 and approved Terna's financial statement, resolved to allocate the 2010 net profits to legal reserve up to its reaching 20% of the share capital.

### Other reserves - € 719.0 million

Other reserves have increased by € 48.3 million due to the effect of:

- other items of the comprehensive income statement (€ 41.9 million): adjustment to fair value of derivatives hedging floating-rate loans of the Parent and RTR (held for sale): cash flow hedges net of the related tax effect (€ 25.9 million and € 16.0 million, respectively);
- transactions with shareholders (€ 6.4 million): increase in the share price premium reserve (€ 6.8 million) and decrease in the stock option reserve (-€ 0.4 million) to reflect the stock options exercised during the period.

### Retained earnings - € 1,059.4 million

The increase of the year of the item "Retained Earnings" of € 387.7 million essentially refers to the allocation of the residual amount of the Group's profit for 2009 after the distribution of the 2009 dividend on the part of the Parent (€ 380.5 million).

### Interim dividend

After receiving the report of the independent auditors required by art. 2433-*bis* of the Italian Civil Code, on 18 October 2010 the Parent's Board of Directors approved the distribution of an interim dividend of € 160.4 million, equal to € 0.08 per share, which is payable on the upcoming 25 November, with an ex dividend date (coupon 13) of 22 November 2010.

### Equity attributable to non-controlling interests - € 0.2 million

Equity attributable to non-controlling interests refers to the subsidiary Valmontone Energia S.r.l. 1.5% of which is not owned by the Group.

### Terna S.p.A. Stock Option Plans

On 21 December 2005, based on proposals presented by the Remuneration Committee, the Parent's Board of Directors approved a Stock Option Plan for 2006 applicable to those senior managers of the Terna Group who hold key roles in terms of achieving the Group's strategic objectives.

This plan is aimed at giving the Terna Group – in line with international best practices and that of the leading Italian companies listed on the stock exchange – a management incentive and loyalty tool that imbues key employees with a sense of belonging to the corporate team, while ensuring they are constantly focused on creating value, with a view to melding the interests of shareholders and management.

The features of the 2006 Stock Option Plan are outlined below:

#### Rules governing the 2006 Stock Option Plan (approved on 21 December 2005)

The plan provides for the distribution of a maximum of 10,000,000 options to about 20 Terna managers holding the most important positions in terms of achieving the Company's strategic targets, including the CEO, as a senior manager of the Company.

Under the approved rules governing the Stock Option Plan:

- the strike price of each share shall be the arithmetic mean of the reference price of Terna ordinary share observed on the electronic stock exchange operated by Borsa Italiana S.p.A. in the period between the date of the offer and the same day of the previous calendar month;
- the exercise of the options and, consequently, the right to subscribe newly-issued Terna ordinary shares depends on achieving two performance parameters. In particular:
  - Terna EBITDA for the grant year (2006) must be greater than that established in the budget approved by the Board of Directors;
  - the 2006 performance of each beneficiary must be positively assessed by the CEO, with a provision for a 50% reduction in the options that the individual beneficiary can exercise, should this second condition not be met;
- if the exercise conditions are met, individual beneficiaries can exercise, their options by 31 March 2010 up to the following maximum quantities:
  - up to 30% of vested options, beginning from the date specified in the notice announcing that the exercise conditions have been met;
  - up to 60% of vested options, beginning from the first day of the first calendar year subsequent to that in which the notice announcing that the exercise conditions have been met is issued;
  - up to 100% of vested options, beginning from the first day of the second calendar year subsequent to the year in which the notice announcing that the exercise conditions have been met is issued.

On 22 April 2009, the Extraordinary Shareholders' Meeting voted to extend the time limit for exercising the options under option plan by three years until 31 March 2013, and to amend art. 5 of the Bylaws.

Options can be exercised only on a stock exchange trading day during the last 10 days of each month. However, options cannot in any case be exercised in the following days:

- in the period between the third-to-last trading day and the last trading day before the ex dividend date;
- in the period between the date scheduled for the approval of the financial statements of the year by the Board of Directors and the same day of the previous month;
- in the period between the date scheduled for the approval of the half-year report by the Board of Directors and the same day of the previous month.

The 2006 Stock Option Plan entailed the granting, on 21 December 2005, of 9,992,000 options with a strike price of € 2.072 to 17 managers of the Company. The Board of Directors verified that the conditions for exercise were met when it approved the financial statements of 31 December 2006.

At 31 December 2010, the changes in the options granted under this plan are summarised as follows:

|                                      |           |
|--------------------------------------|-----------|
| Outstanding at the start of the year | 9,083,200 |
| Unopted during the year              | 5,596,300 |
| Exercised during the year            | 3,486,900 |
| Outstanding at the end of the year   | 5,596,300 |
| Exercisable at the end of the year   | 5,596,300 |



The weighted average prices of the shares at their exercise dates were:

€ 3.226 <sup>(\*)</sup> on 22 March 2010;  
€ 3.226 <sup>(\*)</sup> on 23 March 2010;  
€ 3.218 <sup>(\*)</sup> on 24 March 2010;  
€ 3.224 <sup>(\*)</sup> on 29 March 2010;  
€ 3.216 <sup>(\*)</sup> on 31 March 2010;  
€ 3.048 <sup>(\*)</sup> on 30 April 2010;  
€ 3.062 <sup>(\*)</sup> on 31 May 2010;  
€ 3.061 <sup>(\*)</sup> on 21 June 2010;  
€ 3.292 <sup>(\*)</sup> on 29 October 2010.

(\*) Source: Bloomberg

Fair value at the grant date was determined using the Cox-Rubinstein pricing method, which takes account of Terna's stock price at the grant date, the volatility of the security, and the rate curve at the grant date considering the term of the plan. The following pricing parameters were used:

- Closing price (underlying or spot price) for the stock on the grant date (source Bloomberg) of € 2.058;
- Strike price of € 2.072;
- Rate curve for calculating the discount factors at the grant date (source Reuters);
- Historical volatility of the stock identified 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 and General Managers:

| Name and Surname | Position | Number of options |
|------------------|----------|-------------------|
| Flavio Cattaneo  | CEO      | 2,115,000         |

Other information on the Stock Option Plan:

|  |           |
|--|-----------|
| Other beneficiaries of the Stock Option Plan | 3,481,300 |
|--|-----------|

## 24. Loans and financial liabilities

The following table details loans and financial liabilities recognised in the consolidated financial statements at 31 December 2010:

| In millions of euros   | Carrying amount |                | Change       |
|--|-----------------|----------------|--------------|
|  | 31 Dec. 2010    | 31 Dec. 2009   |              |
| Bonds  | 2,728.2         | 2,643.5        | 84.7         |
| Bank loans   | 2,419.3         | 1,555.7        | 863.6        |
| <b>Long-term loans</b>   | <b>5,147.5</b>  | <b>4,199.2</b> | <b>948.3</b> |
| CFH derivatives  | 47.1            | 82.6           | -35.5        |
| <b>Non-current financial liabilities</b>                       | <b>47.1</b>     | <b>82.6</b>    | <b>-35.5</b> |
| Short-term loans   | 73.1            | 40.0           | 33.1         |
| Current portion of long-term loans                             | 59.7            | 59.7           | 0.0          |
| <b>Short-term loans and current portion of long-term loans</b> | <b>132.8</b>    | <b>99.7</b>    | <b>33.1</b>  |
| <b>Total</b>   | <b>5,327.4</b>  | <b>4,381.5</b> | <b>945.9</b> |

Gross debt for the year increased with respect to the previous year by € 945.9 million to € 5,327.4 million.

The increase in the carrying amounts of bonds (€ 84.7 million) comprises the change in the fair value of the hedged risk, € 75.9 million, and capitalization of the inflation for the period net of the amortised-cost effect, € 8.8 million. The change linked to the hedging of interest-rate risk comprises € 17.4 million in relation to the inflation-linked bonds, € 39.3 million to the 2014-2024 bonds and € 19.2 million to the private placement, and offsets the increase in the fair value of the derivatives recognised as financial assets, € 77.1 million.

The fair value of bonds is determined by discounting the expected cash flows with the market rates in effect on the date of reference. The official quotes of issued bonds which were registered in the Stock Exchange of Luxembourg are detailed below for the last quote:

- bond maturing 2024, 2010 price: 104.23; 2009 price: 102.29;
- bond maturing 2014, 2010 price: 105.70; 2009 price: 104.34;
- bond maturing 2023, 2010 price: 96.57; 2009 price: 102.60;
- bond maturing 2019, 2010 price: 105.00; 2009 price: 103.56.

Source: Reuters

Consequently, compared with the total carrying amount of € 2,782.2 (€ 2,643.5 million at 31 December 2009), the market value is € 2,609.7 (€ 2,600.3 at 31 December 2009).

As regards debt originally bearing floating rates, the increase of € 896.7 million is due to:

- a -€ 59.7 million reduction in European Investment Bank loans and other financing following repayments made on outstanding loans;
- the collection in March of an EIB loan totalling € 73 million;
- the collection in November of an EIB loan totalling € 300 million;
- an increase in other loans of € 550 million as a result of drawing on the 2006 revolving credit facility;
- the establishment of a short-term loan totalling € 50 million;
- decrease in the use of overdraft facilities in the amount of -€ 16.9 million.

Movements include the issue, on 25 March 2010, of the previously cited EIB financing of € 73 million which has a term of 20 years and will be repaid in semi-annual instalments as of the fifth year at 6-month Euribor uplifted by 40 basis points. Note should also be made of the issue, on 24 November 2010, of the previously cited EIB financing of € 300 million which has a term of 20 years and will be repaid in semi-annual instalments as of the fifth year at 6-month Euribor uplifted by 39 basis points.

## Long-term loans

The following table reports the carrying amounts of long-term debt and the repayment plan as of 31 December 2010, broken down by loan type, including amounts falling due within one year and average interest rate at year-end:

|                            | Maturity  | 31 Dec.<br>2009 | 31 Dec. 2010   | Due<br>within<br>one year | Due<br>beyond<br>one year | 2012        | 2013         | 2014         | 2015         | After          | Average<br>interest<br>rate as of<br>31 Dec. 2010 |
|----------------------------|-----------|-----------------|----------------|---------------------------|---------------------------|-------------|--------------|--------------|--------------|----------------|---|
| In millions of euros       |           |                 |                |                           |                           |             |              |              |              |                |   |
| Bonds -                    |           |                 |                |                           |                           |             |              |              |              |                |   |
| 10y and 20y                | 2014-2024 | 1,479.5         | 1,518.8        | 0.0                       | 1,518.8                   | 0.0         | 0.0          | 636.5        | 0.0          | 882.3          | 4.62%   |
| Bonds -                    |           |                 |                |                           |                           |             |              |              |              |                |   |
| Inflation Linked           | 2023      | 563.5           | 589.7          | 0.0                       | 589.7                     | 0.0         | 0.0          | 0.0          | 0.0          | 589.7          | 4.42%   |
| Bonds -                    |           |                 |                |                           |                           |             |              |              |              |                |   |
| Private Placement          | 2019      | 600.5           | 619.7          | 0.0                       | 619.7                     | 0.0         | 0.0          | 0.0          | 0.0          | 619.7          | 4.88%   |
| <b>Total fixed rate</b>    |           | <b>2,643.5</b>  | <b>2,728.2</b> | <b>0.0</b>                | <b>2,728.2</b>            | <b>0.0</b>  | <b>0.0</b>   | <b>636.5</b> | <b>0.0</b>   | <b>2,091.7</b> |   |
| EIB                        | 2014-2030 | 766.9           | 1,080.1        | 59.7                      | 1,020.4                   | 59.7        | 69.4         | 79.2         | 76.9         | 735.2          | 1.03%   |
| Club Deal                  | 2015      | 648.5           | 648.9          | 0.0                       | 648.9                     | 0.0         | 0.0          | 0.0          | 648.9        | 0.0            | 1.31%   |
| RCF 2006                   | 2013      | 200.0           | 750.0          | 0.0                       | 750.0                     | 0.0         | 750.0        | 0.0          | 0.0          | 0.0            | 1.04%   |
| <b>Total floating rate</b> |           | <b>1,615.4</b>  | <b>2,479.0</b> | <b>59.7</b>               | <b>2,419.3</b>            | <b>59.7</b> | <b>819.4</b> | <b>79.2</b>  | <b>725.8</b> | <b>735.2</b>   |   |
| <b>Total</b>               |           | <b>4,258.9</b>  | <b>5,207.2</b> | <b>59.7</b>               | <b>5,147.5</b>            | <b>59.7</b> | <b>819.4</b> | <b>715.7</b> | <b>725.8</b> | <b>2,826.9</b> |   |

The repayment of the nominal amount of the 2014, 2024, and 2019 bonds, equal to € 2,000.0 million, will entail payment of € 600.0 million on 28 October 2014, € 800.0 million on 28 October 2024 and € 600 million on 3 October 2019; the inflation-linked bonds will be repaid at maturity, on 15 September 2023, with the nominal value adjusted to reflect inflation. All other financial debt items are stated at their nominal value along with the related repayment plan.

The total loans at 31 December 2010 of the Terna Group, all of which pertain to the Parent, amount to € 5,207.2 million, including loans of € 5,147.5 million due after one year and € 2,826.9 million due after the fifth year.

The table shows the average interest rate for each type of financial liability. Below we also comment on the Group's hedging operations against interest rate fluctuations.

As regards the 2014-2024 bonds, with an average coupon of 4.62%, if FVH hedging operations are taken into account, the average interest rate is equal to 1.42%.

For the inflation-linked bonds- and taking hedges into account - and assuming a 1.68% inflation rate, the average interest rate paid in the year was 1.03%.

In line with financial risk management policies, the fixed-rate private placement was synthetically transformed to a floating rate security by means of derivative contracts with the same maturity. Consequently, the average interest rate paid in the year was 2.31%.

With regard to floating rate loans covered by fluctuations in interest rates - and taking into account the effect of derivative financial instruments booked as cash flow hedges - an average rate of 4.46% is reported for EIB financing while for the Club Deal financing totalling € 650 million the average rate was 4.70% and for the RCF financing the average rate was 2.17%.

The following table reports changes in long-term debt for the year:

| Type of loan<br>In millions of euros | Nominal debt<br>at<br>31 Dec. 2009 | Carrying<br>amount at<br>31 Dec. 2009 | Repayment<br>and<br>capitalisation | New<br>issues | Delta Fair Value<br>31 Dec. 2009<br>31 Dec. 2010 | Change in<br>carrying<br>amount | Nominal debt<br>at<br>31 Dec. 2010 | Carrying<br>amount at<br>31 Dec. 2010 |
|--------------------------------------|------------------------------------|---------------------------------------|------------------------------------|---------------|--|---------------------------------|------------------------------------|---------------------------------------|
| Listed fixed-rate bonds              | 1,400.0                            | 1,479.5                               | 0.0                                | 0.0           | 39.3   | 39.3                            | 1,400.0                            | 1,518.8                               |
| Listed IL bond                       | 521.0                              | 563.5                                 | 8.8                                | 0.0           | 17.4   | 26.2                            | 529.8                              | 589.7                                 |
| Private Placement                    | 600.0                              | 600.5                                 | 0.0                                | 0.0           | 19.2   | 19.2                            | 600.0                              | 619.7                                 |
| <b>Total bonds</b>                   | <b>2,521.0</b>                     | <b>2,643.5</b>                        | <b>8.8</b>                         | <b>0.0</b>    | <b>75.9</b>                                      | <b>84.7</b>                     | <b>2,529.8</b>                     | <b>2,728.2</b>                        |
| Bank loans                           | 1,616.8                            | 1,615.4                               | (59.7)                             | 923.0         | 0.3  | 863.6                           | 2,480.1                            | 2,479.0                               |
| <b>Total bank loans</b>              | <b>1,616.8</b>                     | <b>1,615.4</b>                        | <b>(59.7)</b>                      | <b>923.0</b>  | <b>0.3</b>                                       | <b>863.6</b>                    | <b>2,480.1</b>                     | <b>2,479.0</b>                        |
| <b>Total financial debt</b>          | <b>4,137.8</b>                     | <b>4,258.9</b>                        | <b>(50.9)</b>                      | <b>923.0</b>  | <b>76.2</b>                                      | <b>948.3</b>                    | <b>5,009.9</b>                     | <b>5,207.2</b>                        |

At 31 December 2009, long-term debt has increased overall by € 948.3 million, comprising € 550 million drawn from the Revolving Credit Facility, € 373 million in the form of two new loans from the EIB, € 8.8 million on the capitalisation of inflation for the period in relation to the IL bond, and € 75.9 million on the increase in the fair value of the bonds due to the decline in interest rates, net of € 59.7 million in instalment payments on the EIB loans.

At 31 December 2010, Terna has unused lines of credit exceeding € 1,697.6 million, of which more than € 697.6 million in short-term credit lines and € 1,000.0 million in medium-term credit lines.

#### Non-current financial liabilities

The table below reports the amount and changes in non-current financial liabilities with respect to value at the end of 2010:

| In millions of euros | 31 Dec. 2010 | 31 Dec. 2009 | Change       |
|----------------------|--------------|--------------|--------------|
| CFH derivatives      | 47.1         | 82.6         | -35.5        |
| <b>Total</b>         | <b>47.1</b>  | <b>82.6</b>  | <b>-35.5</b> |

“Non-current financial liabilities” include the fair value of cash flow hedges.

Fair value was measured by discounting the expected cash flows using the market yield curve at the reporting date. The change with respect to 31 December 2009 was equal to -€ 35.5 million.

#### Short-term loans

Short-term loans, equal to € 73.1 million, consist of drawings on overdraft facilities for € 23.1 million and short-term loans for € 50.0 million.

### Current financial liabilities

Current financial liabilities, which are generated by the net financial expense accrued on financial instruments but not yet settled, decreased on the previous year by € 1.3 million; this was primarily due to current financial liabilities for private placement (-€ 7.4 million) and the relative derivatives (€ 2.9 million) which were partially compensated by the greater amount of loans in force in 2010 (€ 3.2 million).

The following table details deferred liabilities on the basis of the financial liabilities to which they relate:

| In millions of euros            | 31 Dec. 2010 | 31 Dec. 2009 | Change      |
|---------------------------------|--------------|--------------|-------------|
| <b>Deferred liabilities on:</b> |              |              |             |
| Derivatives                     |              |              |             |
| - <i>hedging</i>                | -6.5         | -9.4         | 2.9         |
| Bond                            |              |              |             |
| - <i>IL</i>                     | 4.3          | 4.3          | 0.0         |
| - <i>private placement</i>      | 7.2          | 14.6         | -7.4        |
| - <i>ten-year</i>               | 4.5          | 4.5          | 0.0         |
| - <i>twenty-year</i>            | 7.0          | 7.0          | 0.0         |
| <b>Total</b>                    | <b>23.0</b>  | <b>30.4</b>  | <b>-7.4</b> |
| Loans                           | 7.7          | 4.5          | 3.2         |
| <b>Total</b>                    | <b>24.2</b>  | <b>25.5</b>  | <b>-1.3</b> |

### Net financial position

Pursuant to the CONSOB Communication of 28 July 2006, and in compliance with the CESR Recommendation of 10 February 2005 for the consistent implementation of the Commission regulation on prospectuses, the net financial position of the Company is as follows:

| In millions of euros                                     | Carrying amount<br>31 Dec. 2010 |
|--|---------------------------------|
| A. Cash  | 0.1                             |
| B. Other liquidity                                       | 150.0                           |
| <b>C. Liquidity (A) + (B)</b>                            | <b>150.1</b>                    |
| D. Current portion of long-term debt                     | 59.7                            |
| E. Short-term loans                                      | 73.1                            |
| <b>F. Current financial debt (D) + (E) + (F)</b>         | <b>132.8</b>                    |
| <b>G. Net current financial debt (G) - (C)</b>           | <b>-17.3</b>                    |
| H. Non-current bank debt                                 | 2,419.3                         |
| I. Bonds issued  | 2,728.2                         |
| J. Derivative financial instruments in portfolio         | -153.2                          |
| <b>K. Net non-current financial debt (I) + (J) + (K)</b> | <b>4,994.3</b>                  |
| <b>L. Net financial debt (H) + (L)</b>                   | <b>4,977.0</b>                  |

For more detail on the composition of the items in this table, please see notes 17 and 21, as well as the information presented here in note 24.

For more information on the contractual provisions of outstanding loans at 31 December 2010, please see the notes to the financial statements of Terna S.p.A.

## 25. Employee benefits – € 122.3 million

The Group provides benefits to its employees during their period of employment (termination benefits), at the termination of their employment (termination benefits, additional month's pay and indemnity for lack of notice), and in the period after the termination of employment (electricity discount and the ASEM health plan).

The loyalty bonus is awarded to employees and managers of the Group when they reach certain seniority levels (25 and 35 years of service).

The benefits granted at the termination of employment are recognised for all employees (termination indemnities), managers hired or appointed before 28 February 1999 (indemnity for lack of notice), and employees (production workers, office staff and junior managers) hired before 24 July 2001 (additional month's pay indemnity).

Post-employment benefits consist of the following:

- discount on electrical energy consumed for domestic use. This benefit is offered to all employees hired before 30 June 1996 (electricity discount);
- a healthcare plan complementing the national health service, as agreed under the terms of the national contract for industrial managers (the Asem health plan).

The composition of termination benefits and other employee-related provisions at 31 December 2010, pertaining entirely to the Parent, is detailed below along with changes in the year:

| In millions of euros                                   | 31 Dec. 2009 | Provision   | Interest cost | Utilisations and other changes | 31 Dec. 2010 |
|--|--------------|-------------|---------------|--------------------------------|--------------|
| <b>Benefits payable to employees</b>                   |              |             |               |                                |              |
| Loyalty bonus  | 4.9          | 0.0         | 0.2           | -0.9                           | 4.2          |
| <b>Total</b>   | <b>4.9</b>   | <b>0.0</b>  | <b>0.2</b>    | <b>-0.9</b>                    | <b>4.2</b>   |
| <b>Benefits payable upon termination of employment</b> |              |             |               |                                |              |
| Termination benefits                                   | 71.5         | 11.0        | 2.6           | -17.2                          | 67.9         |
| Additional months' pay                                 | 7.3          | 0.4         | 0.2           | -1.2                           | 6.7          |
| Indemnities for lack of notice and similar             | 3.3          | 0.0         | 0.1           | -0.4                           | 3.0          |
| <b>Total</b>   | <b>82.1</b>  | <b>11.4</b> | <b>2.9</b>    | <b>-18.8</b>                   | <b>77.66</b> |
| <b>Post-employment benefits</b>                        |              |             |               |                                |              |
| Energy discount  | 26.7         | 1.4         | 1.5           | -0.3                           | 29.3         |
| ASEM   | 11.4         | 0.0         | 0.3           | -0.5                           | 11.2         |
| <b>Total</b>   | <b>38.1</b>  | <b>1.4</b>  | <b>1.8</b>    | <b>-0.8</b>                    | <b>40.5</b>  |
| <b>Total</b>   | <b>125.1</b> | <b>12.8</b> | <b>4.9</b>    | <b>-20.5</b>                   | <b>122.3</b> |

The item, equal to € 122.3 million at 31 December 2010 (€ 125.1 million at 31 December 2009), decreased by € 2.8 million on the previous year, due to the utilisations of the year (€ 20.5 million), partially offset by the allocations and the recognition of the discounting charge for the period (€ 17.7 million in total).

Costs for liabilities in respect of employee benefits recognised in the income statement break down as follows:

| In millions of euros    | Termination benefits | Indemnities for lack of notice and similar | Additional months' pay | Loyalty bonus | ASEM        | Energy discount | Total        |
|-------------------------|----------------------|--|------------------------|---------------|-------------|-----------------|--------------|
| <b>31 December 2009</b> | <b>71.5</b>          | <b>3.3</b>                                 | <b>7.3</b>             | <b>4.9</b>    | <b>11.4</b> | <b>26.7</b>     | <b>125.1</b> |
| Provision               | 11.0                 | 0.0  | 0.4                    | 0.0           | 0.0         | 1.4             | 12.8         |
| Financial expense       | 2.6                  | 0.1  | 0.2                    | 0.2           | 0.3         | 1.5             | 4.9          |
| Payments and transfers  | -17.2                | -0.4                                       | -1.2                   | -0.9          | -0.5        | -0.3            | -20.5        |
| <b>31 December 2010</b> | <b>67.9</b>          | <b>3.0</b>                                 | <b>6.7</b>             | <b>4.2</b>    | <b>11.2</b> | <b>29.3</b>     | <b>122.3</b> |

The main assumptions made in the actuarial estimate of employee benefit obligations are as follows:

| Percentage figures                    | 2010        | 2009        |
|---------------------------------------|-------------|-------------|
| Discount rate                         | 4.1%        | 4.1%        |
| Rate of increase in personnel expense | 2.0% - 4.0% | 2.0% - 4.0% |
| Rate of increase in healthcare costs  | 3.0%        | 3.0%        |

## 26. Provisions for risks and charges – € 171.6 million

The items and changes of the provisions for risks and charges at 31 December 2010 are set out below:

| In millions of euros               | Provision for disputes and litigation | Provisions for other risks and charges | Provision for early retirement incentives | Total        |
|------------------------------------|---------------------------------------|--|---|--------------|
| <b>Balance at 31 December 2009</b> | <b>16.1</b>                           | <b>121.1</b>                           | <b>12.2</b>                               | <b>149.4</b> |
| Provision                          | 0.9                                   | 47.3                                   | 2.3                                       | 50.5         |
| Utilisations and other changes     | -0.3                                  | -26.5                                  | -1.5                                      | -28.3        |
| <b>Balance at 31 December 2010</b> | <b>16.7</b>                           | <b>141.9</b>                           | <b>13.0</b>                               | <b>171.6</b> |

### Provision for disputes and litigation - € 16.7 million

The provision is accrued to cover the liabilities at year end that may arise from lawsuits and out-of-court disputes relating to Group activities. The amount accrued takes into account the opinions both of internal and external legal counsel. Compared with the previous year, the item reported a net increase of € 0.6 million, consisting of net allocations of € 0.7 million by the Parent.

Litigation for which no potential charge can reasonably be calculated are described under “Commitments and risks”.

### Provision for other risks and charges - € 141.9 million

The provision reported a net increase of € 20.8 million with respect to the previous year, ascribable to allocations of € 47.3 million and utilisations of € 26.5 million in the course of the year. More specifically:

- a net allocation of € 10.2 million relating to “Projects for urban and environmental renewal”, the aim of which is to offset the environmental impact of the construction of power lines;
- a net allocation of € 1.5 million for incentive plans for management personnel and social security disputes with INPS;
- net utilisations on the part of the Parent (€ 1.9 million) for charges which are payable to distributing companies for power failures of the transformation plants linked to the NTG (in accordance with Resolution 341/07 - € 0.7 million) as well as for the sharing of indemnities due to final users (€ 0.2 million) in addition to the issue of allocations implemented in the previous year for the contribution that is payable to the Exceptional Events Fund. The latter is part of the Compensation Fund of the Electrical Sector established by Resolution 333/07 for power failure events (€ 2.8 million);
- allocations implemented by TELAT in relation to general equalization results (resolution 348/07 and its subsequent amendments, € 4.9 million);
- an exchange rate adjustment (€ 5.6 million) of the provisions allocated in 2009 for probable charges in respect of contractual and tax obligations related to the disposal of the controlling stake in Terna Participações.

### Provision for early retirement incentives - € 13.0 million

This provision reflects the estimated extraordinary charges related to the voluntary early termination of the working relationship of employees of the Parent who are eligible for retirement. The caption shows substantially no change on the previous year.





## 27. Deferred tax liabilities – € 330.3 million

The changes in this provision are analysed below:

|   | 31 Dec. 2009 | Contribution of newly acquired companies | Impact recognised in profit or loss |              | Impact recognised in equity | 31 Dec. 2010 |
|---|--------------|--|-------------------------------------|--------------|-----------------------------|--------------|
| In millions of euros                        |              |  | Provisions                          | Utilisations |                             |              |
| <b>Deferred tax liabilities</b>             |              |  |                                     |              |                             |              |
| Property, plant and equipment               | 423.0        | 2.8                                      | 0.0                                 | -43.7        | 0.0                         | 382.1        |
| Employee benefits and financial instruments | 3.5          | 0.0                                      | 0.0                                 | 0.0          | 0.0                         | 3.5          |
| <b>Total deferred tax liabilities</b>       | <b>426.5</b> | <b>2.8</b>                               | <b>0.0</b>                          | <b>-43.7</b> | <b>0.0</b>                  | <b>385.6</b> |
| <b>Deferred tax assets</b>                  |              |  |                                     |              |                             |              |
| Provisions for contingencies and charges    | 15.1         | 0.0                                      | 5.4                                 | -4.2         | 0.0                         | 16.3         |
| Allowance for impairment                    | 3.1          | 0.0                                      | 0.0                                 | 0.0          | 0.0                         | 3.1          |
| Employee benefits                           | 21.5         | 0.0                                      | 8.4                                 | -7.0         | 0.0                         | 22.9         |
| FVH-CHF derivatives                         | 22.7         | 0.0                                      | 0.0                                 | 0.0          | -9.8                        | 12.9         |
| Other                                       | 0.3          | 0.0                                      | 0.1                                 | -0.3         | 0.0                         | 0.1          |
| <b>Total deferred tax assets</b>            | <b>62.7</b>  | <b>0.0</b>                               | <b>13.9</b>                         | <b>-11.5</b> | <b>-9.8</b>                 | <b>55.3</b>  |
| <b>Net deferred tax liabilities</b>         | <b>363.8</b> | <b>2.8</b>                               | <b>-13.9</b>                        | <b>-32.2</b> | <b>9.8</b>                  | <b>330.3</b> |

This balance, € 330.3 million, reflects the net movements in the Group's deferred tax assets and liabilities.

Deferred tax liabilities (€ 385.6 million) decreased by € 40.9 million, mainly attributable to:

- utilisation of prior period allocations covering the accelerated depreciation recorded by the parent Terna and the subsidiary TELAT in excess of the tax-allowable amounts (€ 27.4 million and € 3.4 million, respectively), including the amount released in relation to the depreciation charge for the period associated with merger differences allocated to property, plant and equipment at the time of the mergers carried out in prior years (€ 1.7 million);
- release of the period element (€ 8.7 million) of the provision for deferred IRAP liabilities governed by Law no. 244 dated 24/12/2007 (the 2008 Financial Act), recorded in prior years in relation to technical/economic rates;
- release of the period element of the deferred taxes calculated on the excess cost paid for the acquisition of TELAT following its allocation to the transmission plant and other intangible assets (totalling € 4.3 million, after considering the effect of plant transfers from TELAT to the Parent);
- value of the merger contribution of deferred taxes due to the deferred tax effect calculated in the process of allocation of the purchase price of Rete Trasmissione Brescia to the fair value of the property, plant and equipment (€ 2.8 million, net of accrued depreciation).

Deferred tax assets came to € 55.3 million, an increase of € 7.4 million, mainly attributable to the following changes:

- provisions of € 9.8 million, attributable to the tax effect, which has no impact on the income statement, in respect of changes in cash flow hedge instruments;
- net allocation of € 1.4 million relative to movements in provisions for employee benefits;
- an increase of € 1.2 million in net allocations of the year to the provisions for risks and charges.

## 28. Other non-current liabilities – € 141.8 million

This item (€ 141.8 million at 31 December 2010) reports the deferred portion of grants related to assets (€ 139.6 million) as well as the deferred portion of grid transmission fees of the Parent remunerating future costs in respect of the safety plan for the NTG (€ 2.3 million).

The increase of € 9.8 million in the item with respect to the previous year regards:

- the release, in the amount of € 1.0 million, of the portions of grants related to assets in connection with depreciation for the year applicable to the plants involved;
- the recognition, in the amount of € 8.8 million, of the accrued portion of the grid transmission fees to cover the costs of the year of the National Transmission Grid safety plan, essentially due to the adjustment of the useful life of the intangible assets at the rates specified by the AEEG for rate purposes.

## 29. Current liabilities

Current liabilities are analysed as follows at 31 December 2010:

| In millions of euros                   | 31 Dec. 2010   | 31 Dec. 2009   | Change       |
|--|----------------|----------------|--------------|
| Short-term loans (*)                   | 73.1           | 40.0           | 33.1         |
| Current portion of long-term loans (*) | 59.7           | 59.7           | 0.0          |
| Trade payables                         | 1,542.2        | 1,482.0        | 60.2         |
| Tax liabilities                        | 69.6           | 44.0           | 25.6         |
| Current financial liabilities (*)      | 24.2           | 25.5           | -1.3         |
| Other current liabilities              | 135.7          | 95.3           | 40.4         |
| <b>Total</b>                           | <b>1,904.5</b> | <b>1,746.5</b> | <b>158.0</b> |

(\*) See the comments in note 24 "Loans and financial liabilities".

### Trade payables – € 1,542.2 million

Trade payables are analysed as follows at 31 December 2010:

| In millions of euros                   | 31 Dec. 2010   | 31 Dec. 2009   | Change      |
|--|----------------|----------------|-------------|
| Suppliers                              |                |                |             |
| - Energy-related payables              | 1,068.5        | 1,100.7        | -32.2       |
| - Non energy-related payables          | 466.7          | 372.9          | 93.8        |
| Associates                             | 5.0            | 8.0            | -3.0        |
| Payables for contract work in progress | 2.0            | 0.4            | 1.6         |
| <b>Total trade payables</b>            | <b>1,542.2</b> | <b>1,482.0</b> | <b>60.2</b> |

### Suppliers

#### Energy-related payables

This item reports the effects on the balance sheet of payables for "pass-through" costs not ascribable to the Parent, and refers mostly to purchase of energy relative to dispatching activities and the transport fee due to the owners of other sections of the National Transmission Grid.

The decrease of € 32.2 million compared with the previous year is essentially attributed to the net effect of:

- decreased payables (€ 39.0 million) relative to "pass-through items" which are primarily ascribable to the joint effect of:
  - the decrease in payables for the acquisition of electrical energy outside of the power exchange (€ 122.7 million) which is essentially due to the lower balance of net payables for capacity payment (€ 54 million), the decrease in debt items awaiting definition on the part of the AEEG – in particular the availability of productive capacity (PC), totalling € 27.5 million – as well as the reduction in payables for the essential units for safety of the electrical system (EUSES), totalling € 32.7 million.
  - the increase of payables for the acquisition of electrical energy within the power exchange (€ 83.7 million) which is essentially due to virtual interconnection activities (€ 121.1 million) and the dispatching of electrical energy produced by non-programmable renewable resources pursuant to resolution ARG/elt 5/10 (€ 17.9 million) as well as the increase in volumes of resources attained from the energy market (€ 14.9 million); these were partly compensated by the decreased payables generated from the reduction of quantities and the reduction in valuation prices of the imbalance as well as the advance invoicing of balances required by resolution AEEG 34/09 (€ 66.6 million).

- booking of payables not ascribable to the Parent (€ 6.8 million) due to the Compensation Fund for the Electrical Sector and relative to charges payable to the Exceptional Events Fund for power failures which occurred during the year (€ 2.0 million), in accordance with Resolution 333/07 and its subsequent amendments as well as the reimbursement of the grid transmission fees balance for 2008 (€ 4.8 million) which was partially compensated by the receivable booked by the Parent for the same amount, as described in the paragraph relative to “Receivables for grid transmission fees” under trade receivables.

#### Non energy-related payables

Amounts due to suppliers refer to invoices both already received and yet to be received for tenders, services and the purchase of materials and equipment.

The increase with respect previous year (€ 93.8 million) is essentially due to purchases and services in respect of increased capital expenditure in the last quarter of 2010 – primarily associated with Hub 2 of SA.PE.I. - compared with the same period of 2009 by the Parent (€ 91.6 million) and new capital expenditure by TELAT (€ 2.8 million).

#### Associates

This item amounts to € 5.0 million and relates to payables to CESI for services provided to the Parent in the construction and management of laboratories and plants for tests, inspections, studies and experimental research in the general field of electricity technology and scientific progress. The decrease (€ 3.0 million) compared with 31 December 2009 is the result of an increase in services delivered in the final part of the year.

Group commitments with suppliers totalled about € 2,228.9 million and refer to purchase commitments relating to normal operating activities for the period 2011-2016.

#### Payables for contract work in progress

This caption amounted to € 2.0 million at 31 December 2010 and was substantially in line with the balance at 31 December 2009 with an increase of € 1.6 million. It is composed as follows:

| In millions of euros | Payments on account | Contract value | Balance at 31 Dec. 2010 | Payments on account | Contract value | Balance at 31 Dec. 2009 |
|----------------------|---------------------|----------------|-------------------------|---------------------|----------------|-------------------------|
| Other                | -23.2               | 21.2           | -2.0                    | -3.0                | 2.6            | -0.4                    |
| <b>Total</b>         | <b>-23.2</b>        | <b>21.2</b>    | <b>-2.0</b>             | <b>-3.0</b>         | <b>2.6</b>     | <b>-0.4</b>             |

#### Tax liabilities – € 69.6 million

The caption refers to the Group’s tax liabilities for the financial year and refers to:

- the Parent in the amount of € 69.1 million;
- the subsidiary TELAT in the amount of € 0.3 million;
- the subsidiary SunTergrid in the amount of € 0.2 million.

This item reported an increase of € 25.6 million with respect to the previous year which was essentially ascribable to the Parent (+€ 48.3 million) for decreased payables booked in the previous year and partly compensated by the decrease booked by the subsidiary TELAT (-€ 22.9 million) for the greater payable booked in 2009.

#### Other current liabilities - € 135.7 million

Other current liabilities are analysed as follows:

| In millions of euros                     | 31 Dec. 2010 | Due within one year | Due beyond one year | 31 Dec. 2009 | Change      |
|--|--------------|---------------------|---------------------|--------------|-------------|
| Payments on account                      | 30.7         | 1.9                 | 28.8                | 10.0         | 20.7        |
| Other tax liabilities                    | 7.5          | 7.5                 | -                   | 7.1          | 0.4         |
| Payables to social security institutions | 22.4         | 22.4                | -                   | 23.6         | -1.2        |
| Payables to employees                    | 38.9         | 38.9                | -                   | 36.3         | 2.6         |
| Others payables                          |              |                     |                     |              |             |
| - Third parties                          | 36.2         | 3.7                 | 32.5                | 18.3         | 17.9        |
| <b>Total</b>                             | <b>135.7</b> | <b>74.4</b>         | <b>61.3</b>         | <b>95.3</b>  | <b>40.4</b> |

#### Payments on account

The item (€ 30.7 million) reports grants related to assets received by the Group (€ 29.3 million for the Parent and € 1.4 million for TELAT) for investments pending at 31 December 2010.

Compared to the 2009 carrying amount (€ 10 million), there is an increase of € 20.7 million, mainly due to the net effect of new payments on account for € 33.1 million and a decrease of € 12.4 million in the grants reducing the carrying amounts of assets entered in service during the period; in particular there are advances received in accordance with the mandate contract for the design of interconnection networks with abroad (€ 15.6 million, in accordance with ARG/elt 179/09 Resolution and its subsequent amendments).

#### Other tax liabilities

Other tax liabilities, equal to € 7.5 million, essentially regard payables for withholding taxes retained by the Parent.

This item reported an increase of € 0.4 million which was essentially in line with the previous year.

#### Payable to social security institutions

Payables due to social security institutions – and which are essentially relative to payables due to INPS from the Parent – are equal to € 22.4 million (€ 23.6 million at 31 December 2009); this item also includes the payable relative to the Social Security Fund for Electricians (€ 4.9 million).

#### Payable to employees

Payables to employees, which came to € 38.9 million (€ 36.3 million at 31 December 2009 for continuing operations), pertain to the Parent and mainly regard:

- accruals made for staff incentives to be paid the following year (€ 25.8 million);
- payments due to employees for unused holiday time and abolished public holidays (€ 8.7 million);
- termination indemnities due to employees whose employment was terminated before 31 December 2010 (€ 2.6 million).

#### Other payables to third parties

Other payables, equal to € 36.2 million (€ 18.3 million at 31 December 2009), mainly regard security deposits (€ 32.5 million) received from electricity market operators securing their obligations in respect of dispatching contracts. This item reports an increase of € 17.9 million which is essentially attributable to caution money provided as a guarantee of contractual obligations (+€ 17.4 million) in connection with dispatching and virtual interconnection contracts.

### 30. Assets and liabilities held for sale

The items “Assets held for sale” and “Liabilities held for sale” include balance sheet balances of the company Rete Rinnovabile S.r.l. and its subsidiary Valmontone Energia S.r.l., re-classified below as a result of the previously mentioned agreement for the sale of the quota held by SunTergrid S.p.A.

The company RTR is the owner of photovoltaic plants – mostly located across the Italian regions – which are in various stages of development. Of these plants – which generally benefit from the rates relative to the 2010 Energy Account - the company Valmontone Energia S.r.l. is the owner of the license (the so-called “Licensing Agreement”) relative to surface rights on land owned by the Commune of Valmontone and the so-called EPC (“Engineering Procurement Construction”) tender contract required by the Agreement itself for the planning, implementation and management of the photovoltaic plants with an overall power of 6,985.44 KWp.

On 18 October 2010 Terna, SunTergrid and Terra Firma Investments (GP) 3 Limited (wholly-owned by Terra Firma Capital Partners III, L.P.) signed a preliminary agreement to transfer 100% of the quota capital of Rete Rinnovabile S.r.l. (and of the latter's subsidiaries).

The compensation for the operation was agreed in a modular fashion (in terms of Enterprise Value) on the basis of the plants which, on the closing date (31 March 2011), alternatively benefited from the incentives of the 2010 Energy Account or the Energy Account of the first four months of 2011.

Furthermore, the agreement sets out that Terna will supply maintenance, surveillance and monitoring services on the plants according to multiyear contracts defined in the context of the sales transaction and that, at the end of the individual rental contracts, Terna will regain possession of the leased areas.

Within the scope of sector reporting included in paragraph “B. Operating Segments”, and to which reference is made - the companies RTR and Valmontone are allocated to a specific segment called “Discontinued operations and assets held for sale”.

The item “Discontinued operations”, at 31 December 2009, included the residual value of the shareholding in Terna Participações (equal to 10,000 units) which was sold from Terna as part of the previously mentioned Public Tender Offer implemented on 6 May 2010.

### Assets held for sale

In summary, the items included within “Assets held for sale” are as follows:

| In millions of euros                       | 31 Dec. 2010 | 31 Dec. 2009 | Change       |
|--|--------------|--------------|--------------|
| Contract work in progress                  | 509.0        | -            | 509.0        |
| Goodwill                                   | 1.4          | -            | 1.4          |
| Non-current financial assets               | 22.1         | -            | 22.1         |
| Current financial assets                   | -            | 0.1          | -0.1         |
| Trade receivables and other current assets | 37.1         | -            | 37.1         |
| Cash and cash equivalents                  | 6.2          | -            | 6.2          |
| <b>Total assets held for sale</b>          | <b>575.8</b> | <b>0.1</b>   | <b>575.7</b> |

### Contract work in progress

This item essentially includes the valuation of photovoltaic plants on 31 December 2010 (€ 501.7 million) which are being constructed for Terra Firma Investments (GP) 3 Limited; the remaining part of the item (€ 7.3 million) refers to advances and work order inventories. As previously noted, in fact, the Terna Group – by means of the preliminary sales contract stipulated with this company – committed itself to the construction of a group of photovoltaic plants with specific characteristics and which are defined in the same preliminary sales agreement and agreed upon with the buyer. The relative sales price is established on these characteristics. Given this situation, and in application of IAS 11 which regulates construction contracts, the work order for the construction of the photovoltaic plants at 31 December 2010 was evaluated on the basis of the state of progress of the works and the overall costs sustained during the year compared to those which are overall ascribable to the work order in question.

### Goodwill

This item, equal to € 1.4 million, is essentially due (for € 1.2 million) to the merger by incorporation of RTR into the company Reno Solar (acquired on 22 July 2010) and which includes the deferred fiscal effects of the greater price paid with respect to the fair value of the assets and liabilities of the acquired company and which was allocated to the plants.

### Non-current financial assets

Non-current financial assets, equal to € 22.1 million, include the valuation of the cash flow hedge derivative stipulated by Rete Rinnovabile in order to cover the financing stipulated on 28 January 2011 for an amount equal to € 593.8 million and which aims to reinforce – on a non-recourse project financing basis the investments sustained for the realization of the portfolio of owned photovoltaic plants.

### Trade receivables and other current assets

Trade receivables, equal to € 11.1 million, are primarily composed of receivables for invoices to be issued from Rete Rinnovabile and relative to the sale of photovoltaic panels (€ 10.2 million) which will be utilized for the construction of a plant. Other current assets, equal to € 26.0 million, primarily refer to the VAT receivable which accrued during the year (€ 23.9 million) by the two companies.

### Cash and cash equivalents

This item includes the balance of the bank account of Valmontone Energia (€ 6.2 million).

### Liabilities held for sale

The items included under “Liabilities held for sale” are as follows:

| In millions of euros                         | 31 Dec. 2010 | 31 Dec. 2009 | Change       |
|--|--------------|--------------|--------------|
| Deferred tax liabilities                     | 8.5          | -            | 8.5          |
| Provision for risks and charges              | 0.2          | -            | 0.2          |
| Trade payables and other current liabilities | 140.0        | -            | 140.0        |
| <b>Total liabilities</b>                     | <b>148.7</b> | <b>-</b>     | <b>148.7</b> |



### Deferred tax liabilities

Deferred tax liabilities relative to assets held for sale totalled € 8.5 million, and are essentially composed of liabilities of Rete Rinnovabile; they include:

- € 6.1 million, attributable to the tax effect, which has no impact on the income statement, in respect of changes in cash flow hedge instruments;
- the booking, for € 1.2 million, of the deferred fiscal effect relative to the timing differences generated from the allocation of the price paid for the acquisition of Reno Solar as part of company plants, and subsequent incorporation of this company;
- the allocation of advance taxes within the financial statements of RTR for a total of € 1.0 million.

### Provisions for risks and charges

The balance of the item, equal to € 0.2 million, refer to the net allocation to “Projects for urban and environmental renewal”, the aim of which is to offset the environmental impact of the construction of photovoltaic plants.

### Trade payables

This item, equal to € 140.0 million, is essentially represented by payables due to suppliers for contracts and services provided to third parties for the construction of the photovoltaic plants of Rete Rinnovabile S.r.l. and Valmontone Energia S.r.l., totalling € 126.5 million and € 13.5 million, respectively.

### Cash flow

The consolidated statement of cash flows – which reports cash flows of the assets of the photovoltaic project which are held for sale – is illustrated below:

| In millions of euros   | Cash flow<br>31 Dec. 2010 | Cash flow<br>31 Dec. 2009 |
|--|---------------------------|---------------------------|
| <b>Opening balance of cash and cash equivalents</b>                | <b>0.0</b>                | <b>0.0</b>                |
| <b>Self-financing</b>  | <b>155.5</b>              | <b>0.0</b>                |
| Change in net working capital                                      | 102.9                     | 0.00                      |
| <b>Cash flows from operating activities</b>                        | <b>258.4</b>              | <b>0.0</b>                |
| Contract works in progress   | -509.0                    | 0.0                       |
| Goodwill   | -1.4                      | 0.0                       |
| <b>Total cash flows used in investing activities</b>               | <b>-510.4</b>             | <b>0.0</b>                |
| Change in financing  | 232.5                     | 0.0                       |
| Other movements in equity attributable to the owners of the Parent | 16.0                      | 0.0                       |
| Equity attributable to non-controlling interests                   | 0.2                       | 0.0                       |
| Consolidation cancellations  | 9.5                       | 0.0                       |
| <b>Total cash flows from financing activities</b>                  | <b>258.2</b>              | <b>0.00</b>               |
| <b>Total cash flows of the year</b>                                | <b>6.2</b>                | <b>0.0</b>                |
| <b>Closing balance of cash and cash equivalents</b>                | <b>6.2</b>                | <b>0.0</b>                |

The cash flows generated from the continuing operations of Rete Rinnovabile and Valmontone Energia were equal to € 258.4 million. In particular, the net income of the year was equal to € 146.8 million and the allocations to provisions were equal to € 8.7 million. The change in the net working capital, equal to € 102.9 million, is essentially due to payables due to suppliers for construction activities pertaining to photovoltaic plants (€ 140.0 million), net of trade receivables (€ 37.1 million). The cash flows from monetary investment activities essentially refer to the resources which were used in the program for creating the construction contracts (€ 509.0 million).

The net change in cash flows from financing activities (€ 258.2 million) is primarily due to the joint effect of:

- the funds disbursed from Terna in order to finance the investments sustained for the realization of a portfolio of photovoltaic plants (€ 254.6 million);
- the measurement of the cash flow hedge derivative stipulated by Rete Rinnovabile (€ 22.1 million) whose impact on equity was equal to € 16.0 million.

In conclusion, the financial resources which are required for the construction of the photovoltaic plants resulted in financial requirements of the year which were equal to € 510.4 million; this requirement was partially covered by the liquidity generated by ordinary operations (€ 258.4 million) while the residual quota was financed with new debt.



## E. Commitments and risks

### Risk management

#### Market and financial risks for the Group

In the conduct of its operations, the Terna Group is exposed to various financial risks: market risk (namely exchange rate risk, interest rate risk and inflation risk), liquidity risk and credit risk.

This section provides information regarding the Terna Group's exposure to all the above risks, along with a presentation of the objectives, policies and processes for managing those risks and the methods used to measure them, with further quantitative disclosures concerning the 2010 financial statements.

The Group's risk management policies seek to identify and analyse the risks the Group is exposed to, establishing appropriate limits and controls and monitoring risks and compliance with such limits. These policies and the related systems are reviewed on a regular basis in order to take account of any changes in market conditions or in the operations of the Group companies.

The exposure of the Terna Group to the aforementioned risks is substantially represented by the exposure of the Parent. As a part of the financial risk management policies approved by the Board of Directors, Terna has established the responsibilities and operating procedures for financial risk management, specifically as concerns the instruments to be used and the precise operating limits in managing them.

#### Market risks

Market risk is the risk that the fair value or future cash flows of a financial instrument may fluctuate as a result of changes in financial market conditions. Market risks comprise three forms of risk: exchange rate risk, interest rate risk and inflation risk. Risk management must be performed with the objective of maximising financial income and minimising the related risks by selecting counterparties and instruments compatible with the corporate risk management policy. Speculative activity is not envisaged in the corporate mission.

Terna S.p.A. seeks to adopt a dynamic approach to financial risk management. This approach is characterised by risk aversion, aiming at minimising risk through continuous monitoring of financial markets in order to plan hedging transactions in favourable market conditions. The dynamic approach makes it possible to take action to improve existing hedges where changes in market conditions or in the hedged item make the latter unsuitable or excessively expensive. The concept of hedging transaction is not restricted to those hedges that qualify for hedge accounting, but rather encompasses the objective of total or partial hedging of the income statement or statement of financial position item from interest rate risk. 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 fair value of financial derivatives reflects the estimated amount that Terna would pay or receive in order to extinguish contracts at the closing date.

The fair value of instruments is determined in accordance with the fair value hierarchy envisaged under IFRS 7 (Level 2) by means of appropriate valuation techniques for each category of financial instrument, using market data as at the closing date (such as interest rates, exchange rates, volatility) and discounting projected cash flows on the basis of the market yield curve and inflation at the reporting date.

The financial assets and liabilities in respect of derivative instruments in place during the year can be classified as:

- cash flow hedge derivatives, essentially related to hedging the risk of changes in the cash flows associated with long-term floating-rate loans;
- fair value hedge derivatives, essentially related to hedging the exposure to changes in the fair value of a financial asset or liability associated with fluctuations in interest rates (fixed-rate bonds).

### Interest rate risk

Interest rate risk is represented by the uncertainty associated with interest rate fluctuations. This is the risk that a change in market rates may produce effects on the fair value or future cash flows of financial instruments.

In conducting its operations, Terna is exposed to the risk of fluctuations in interest rates. Its main source of interest rate risk is associated with items of net financial debt and the related hedging positions in derivative instruments that generate financial expense. Terna's borrowing strategy focuses on long-term loans whose term reflects the useful life of company assets. It pursues an interest rate risk hedging policy that aims to reconcile this approach with the regulatory framework, which every four years establishes the cost of debt as part of the formula to set the return on the Regulatory Asset Base (RAB). Accordingly, the hedging instruments used, at various maturity dates, include both derivatives that transform fixed rates into floating rates and derivatives that transform floating rates into fixed rates.

In order to reduce the amount of financial debt exposed to the risk of fluctuations in interest rates and to optimise the temporal correlation between average cost of debt and regulatory rate used in the WACC formula, various types of plain vanilla derivatives are used, such as interest rate swaps and interest rate collars.

Interest rate swaps are used in order to reduce the volume of debt exposed to fluctuations in interest rates and to reduce the volatility of borrowing costs. With an interest rate swap, Terna agrees with a counterparty to exchange, at specific intervals, the floating-rate cash flows on a specified notional amount against the fixed-rate (agreed between the parties) cash flows, or *vice versa*.

Interest rate collars are used to lower the impact of the volatility of interest rates on the cost of the debt. They are considered appropriate in times of uncertainty about future developments in interest rates.

The following table shows the financial instruments entered into by Terna, classified according to the type of interest rate (fixed or floating):

| In millions of euros                 | Carrying amount |                | Change         |
|--------------------------------------|-----------------|----------------|----------------|
|                                      | 31 Dec. 2010    | 31 Dec. 2009   |                |
| Fixed-rate financial instruments:    |                 |                |                |
| Assets                               | 0               | 0              | 0              |
| Liabilities                          | 2,775.3         | 2,726.1        | 49.2           |
| Floating-rate financial instruments: |                 |                |                |
| Assets                               | 350.4           | 623.3          | -272.9         |
| Liabilities                          | 2,552.1         | 1,655.4        | 896.7          |
| <b>Total</b>                         | <b>4,977.0</b>  | <b>3,758.2</b> | <b>1,218.8</b> |

### Sensitivity to interest rate risk

As regards the management of interest rate risk, Terna has, on the one hand, entered into fixed-to-floating interest rate swaps (FVH) to hedge the fair value of the fixed-rate risk bonds and, on the other, floating-to-fixed interest rate swaps (CFH) to hedge the expected cash flows in respect of all other floating-rate debt.

Since the hedging relationship between the derivative and the hedged item is formally documented and the effectiveness of the hedge, as verified initially and periodically over its life, is high (between 80% and 125%), the Company has elected to use hedge accounting to ensure the perfect temporal matching of the hedge and the hedged item. The aim of hedge accounting is to recognise the effects of the hedges and the hedged items in the income statement at the same time.

Accordingly, for FVH derivatives, any changes in the fair value of the hedged item attributable to the risk being hedged must be booked in the income statement, thereby offsetting the changes in the fair value of the derivative booked in the income statement. For CFH derivatives, the changes in the fair value of the derivative must be booked under equity (recognising any ineffective portion of the hedge directly in the income statement) and then reversed through the income statement in the same period in which the cash flows of the hedged instrument materialise. The characteristics of the CFH derivatives mirror those of the underlying hedged asset so the related cash flows will materialise at the same maturities as the interest on the debt, with no impact of the changes in fair value on the income statement.

The following table reports the amounts booked in the income statement and equity for positions that are sensitive to changes in interest rates, the theoretical value of the positions following a positive or negative shift in the yield curve and the differential impact booked in the income statement and equity of such changes. A hypothetical 10% variation in interest rates with respect to market interest rates at the reporting date has been assumed:

| In millions of euros  | Income statement      |                               |                       | Equity                |                               |                       |
|---|-----------------------|-------------------------------|-----------------------|-----------------------|-------------------------------|-----------------------|
|   | Current rates<br>+10% | Current rates<br>31 Dec. 2009 | Current rates<br>-10% | Current rates<br>+10% | Current rates<br>31 Dec. 2009 | Current rates<br>-10% |
| <b>31 December 2010</b>   |                       |                               |                       |                       |                               |                       |
| Positions sensitive to interest rate variations (FVH, Bonds, CFH) | 2.9                   | 2.2                           | 1.7                   | -44.5                 | -47.1                         | -49.9                 |
| <i>Hypothetical change</i>  | 0.7                   | -                             | -0.5                  | 2.6                   | -                             | -2.8                  |
| <b>31 December 2009</b>   |                       |                               |                       |                       |                               |                       |
| Positions sensitive to interest rate variations (FVH, Bonds, CFH) | 1.6                   | 1.2                           | 0.8                   | -76.8                 | -82.6                         | -88.3                 |
| <i>Hypothetical change</i>  | 0.4                   | -                             | -0.4                  | 5.7                   | -                             | -5.8                  |

### Inflation risk

As regards inflation rate risk, the rates established by regulators to remunerate Terna S.p.A.'s activities are determined so as to allow coverage of the sector's recognised costs. Such cost components are updated on an annual basis to consider the accrued impact of inflation. In 2007, the Company used an inflation-linked bond issue to obtain an effective hedge of profit for the year; any decrease in expected revenue due to a decrease in the inflation rate would be offset by lower financial expense.

### Exchange rate risk

Generally Terna hedges exchange rate risk through the forward sale or purchase of currencies (forward contracts) or the use of options. Currency options give Terna the right or the obligation to buy or sell predetermined amounts of a currency at a specific exchange rate at the end of a specific period of time. Normally, both forward contracts and options have maturities of no more than 12 months.

Such contracts have a notional amount and maturity date less than or equal to that of the underlying financial liability, or the expected cash flows, so that any change in the fair value and/or estimated cash flows deriving from an appreciation or depreciation of the euro against other currencies is fully offset by a corresponding change in the fair value and/or estimated cash flows of the underlying position.

As at 31 December 2010 (and as at 31 December 2009), no financial instruments exposed to exchange rate risk were present.

### Liquidity risk

The liquidity risk is the risk Terna might encounter difficulty in discharging its obligations in respect of its financial liabilities and operational cycle. Liquidity risk management seeks to ensure adequate coverage of financial needs by obtaining adequate lines of credit and appropriate management of any surplus liquidity. At 31 December 2010 Terna had € 1,000 million in medium-term credit lines and € 697.6 million in short-term credit lines. Such amount is sufficient to refinance the debt falling due discussed in the section on long-term loans (€ 59.7 million).

### Credit risk

Credit risk is the risk a customer or one of the counterparties to a transaction in financial instruments could cause a financial loss by failing to discharge an obligation. It is mainly generated by trade receivables and the financial investments of the Company.

The credit risk originated by open positions on transactions in financial derivatives is considered to be marginal since the counterparties, in compliance with financial risk management policies, are leading international credit institutions with high ratings and such transactions are diversified in compliance with specific concentration limits.

Terna provides its services to counterparties considered solvent by the market, which therefore have a high credit standing, and does not have highly concentrated credit risk.

Credit risk management is guided by the provisions of AEEG Resolution no. 111/06, which, in art. 49, introduced instruments for the limitation of risks related to the insolvency of dispatching customers, both on a preventive basis and in the event of actual insolvency. In particular, the resolution establishes three instruments to safeguard the electricity market: a guarantee system (bank guarantees provided by individual dispatching customers, based on their revenue), the option of terminating dispatching contracts (in the event of insolvency or failure to replace enforced guarantees) and, finally, the possibility of recovering uncollected debts, after having taken all other possible collection actions, through a specific fee defined by the Authority.

The following table summarises the exposure to such risk as at the reporting date:

| In millions of euros      | Carrying amount |                | Change       |
|---------------------------|-----------------|----------------|--------------|
|                           | 31 Dec. 2010    | 31 Dec. 2009   |              |
| FVH derivatives           | 200.3           | 123.2          | 77.1         |
| Cash and cash equivalents | 150.1           | 0.1            | 150.0        |
| Trade receivables         | 1,495.6         | 1,177.1        | 318.5        |
| <b>Total</b>              | <b>1,846.0</b>  | <b>1,300.4</b> | <b>545.6</b> |

The total value of the exposure to credit rate risk at 31 December 2010 is represented by the carrying amount of financial assets (current and non-current), trade receivables and cash and cash equivalents.

The following tables provide qualitative information on customer receivables that are not past due and have no impairment:

#### GEOGRAPHICAL DISTRIBUTION

| In millions of euros | Carrying amount |                |
|----------------------|-----------------|----------------|
|                      | 2010            | 2009           |
| Italy                | 1,482.6         | 1,165.9        |
| Euro-area countries  | 8.9             | 10.1           |
| Other countries      | 4.1             | 1.1            |
| <b>Total</b>         | <b>1,495.6</b>  | <b>1,177.1</b> |

#### CUSTOMER TYPOLOGY

| In millions of euros   | Carrying amount |                |
|--|-----------------|----------------|
|  | 2010            | 2009           |
| Distributors (*)   | 243.9           | 209.4          |
| Electricity Equalisation Fund (**)   | 71.7            | 88.9           |
| Input dispatching contractors  | 310.2           | 380.5          |
| Withdrawal dispatching contractors (non distributors)  | 765.3           | 455.1          |
| Parties which have undersigned virtual import contracts and virtual import services (interconnectors and shippers) | 35.2            | -              |
| Receivables from unregulated activities  | 69.3            | 43.2           |
| <b>Total</b>   | <b>1,495.6</b>  | <b>1,177.1</b> |

(\*) Includes receivable accrued in respect of TELAT grid transmission fees;

(\*\*) of which € 45.1 million from volume effect on grid transmission fees.

The following table breaks down customer receivables by age, reporting any potential impairment losses:

| In millions of euros        | 2010                    |                | 2009                    |                |
|-----------------------------|-------------------------|----------------|-------------------------|----------------|
|                             | Provision for bad debts | Gross          | Provision for bad debts | Gross          |
| Not yet past due            | -                       | 1,430.9        | -2.0                    | 1,134.3        |
| 0-30 days past due          | -                       | 38.5           | -                       | 18.6           |
| 31-120 days past due        | -                       | 3.5            | -0.6                    | 15.6           |
| More than 120 days past due | -23.5                   | 46.2           | -24.4                   | 35.6           |
| <b>Total</b>                | <b>-23.5</b>            | <b>1,519.1</b> | <b>-27.0</b>            | <b>1,204.1</b> |

Changes in the allowance for impairment in the course of the year were as follows:

| In millions of euros          | 2010         | 2009       |
|-------------------------------|--------------|------------|
| Balance at 1 January          | -27          | -11.7      |
| Reversal of provision         | 3.5          | -          |
| Impairment losses of the year | -            | -15.3      |
| <b>Balance at 31 December</b> | <b>-23.5</b> | <b>-27</b> |

The value of guarantees received from eligible electricity market customers is illustrated below:

| In millions of euros                  | 2010           | 2009           |
|---------------------------------------|----------------|----------------|
| Input dispatching activity            | 220.5          | 251.3          |
| Withdrawal dispatching activity       | 831.3          | 851.3          |
| Grid transmission fees - distributors | 173.7          | 172.3          |
| Virtual importing                     | 338.0          | -              |
| <b>Balance at 31 December</b>         | <b>1,563.5</b> | <b>1,274.9</b> |

### Default risk and debt covenants

This risk is associated with the possibility that the loan contracts or bond rules to which the Company is party may contain provisions authorising counterparties to call in such loans immediately upon the occurrence of certain events, thereby generating liquidity risk. For more information on the contractual provisions of outstanding loans at 31 December 2010 please see the section "Loans and financial liabilities" in the notes to the separate financial statements of Terna S.p.A.

## Legal disputes

The main unrecognised commitments and contingencies of Terna and TELAT at 31 December 2010 are discussed below. The other subsidiaries had no unrecognised commitments and contingencies at that date.

### Environmental and urban planning litigation

Environmental litigation originates from the installation and operation of electrical plants and primarily involves damages which could be derived from exposure to electrical and magnetic fields that are generated by power lines. The Parent and the subsidiary TELAT are involved in various civil and administrative suits requesting the transfer or change in operations of allegedly-harmful power lines, even though they were installed in full compliance with applicable legislation (Law n. 36 of 22 February 2001 and Prime Minister Decree of 8 July 2003). Only a very small number of cases include claims for damages for harm to health caused by electromagnetic fields.

In sporadic cases, adverse judgements have been issued against the Parent. These have been appealed and the appeals are still pending; adverse decisions are considered unlikely.

In addition, a number of cases relating to urban planning and environmental issues are pending in respect of the construction and operation of certain transmission lines. The possible effects of any unfavourable outcome to these cases are unpredictable and, accordingly, have not been considered when determining the "Provision for disputes and other contingencies".

In a limited number of cases, the possibility of an adverse outcome cannot be entirely ruled out. The possible consequences could, in addition to the award of damages, include, inter alia, the costs of modifying lines and the temporary suspension of their use. In any case, any unfavourable outcome would not jeopardise line operations.

Examination of the above litigation, having regard for the information provided by the external legal consultants, suggests that the likelihood of adverse outcomes is remote.

### Litigation concerning licensing activities

Given that it has been the licensee for transmission and dispatching activities since 1 November 2005, the Parent has been involved in a number of cases appealing AEEG, MAP and/or Terna measures relating to activities operated under the license. Only in those cases in which the plaintiffs not only claim defects in the measures, but also allege that Terna violated the rules established by such Authorities has the Company appeared in court. Within the scope of this litigation, although a number of cases have seen the resolutions of AEEG struck down in the first and/or second-level court, together with the consequent measures adopted by Terna, it is felt that there is little risk of adverse outcomes for Terna, since the matters generally regard pass-through items. This position is supported by the information provided by the external legal counsel representing the Company in the cases involved. As the licensee for transmission and dispatching activities, the measures taken by the Company when applying the Resolutions adopted by the Authority are sometimes the subject of challenges. In appropriate circumstances, the economic costs of such challenges may be borne by the Authority.

## F. Business combinations

### Purchase of Retrasm (Rete di Trasmissione Brescia S.r.l.)

On 5 August 2010, according to the purchase contract signed on 22 December 2009 and as a result of the approval by the Antitrust Authorities, Terna S.p.A. and TELAT S.r.l. finalised the purchase of the entire share capital of Reti Trasmissione Energia Elettrica ASM S.r.l. ("Retrasm") from A2A S.p.A. The stipulation of the agreement occurred after the transfer to Retrasm - by way of the partial demerger of A2A Reti Elettriche S.p.A. (A2A Reti Elettriche), a company entirely controlled by A2A - of the high-voltage lines (classified as distribution lines) owned by A2A Reti Elettriche S.p.A. The assets transferred included 108 kilometres of power lines (at 132 kilovolts) and the bays related to these lines which were inserted within the NTG by means of the Decree of the Minister of Economic Development on 26 April 2010.

The amount paid for Retrasm's entire share capital was € 28.0 million.

Retrasm – renamed "Rete Trasmissione Brescia S.r.l." – owns a portion of the Rete di Trasmissione Nazionale (RTN) of approximately 288 km of lines and relative bays, and a 220/130 kV power station.

On 10 November 2010, the merger by incorporation of Rete Trasmissione Brescia S.r.l. into TELAT S.r.l. became effective, as deliberated by the administrative bodies of the companies on 22 September 2010; the accounting and fiscal effects are retroactive to the date of acquisition of the share capital of the incorporated company, i.e. 5 August 2010.

Below we set out the amount recognised, at the purchase date, corresponding to the Company's assets and liabilities measured at fair value at such date, and the IFRS carrying amounts immediately before the combination. The difference between the price paid to purchase Retrasm, approximately € 28.0 million, and the fair value of the assets and liabilities taken on and incurred, approximately € 34.0 million, is accounted for as revenue from purchase at bargain price, in the item "other revenue and income" of the Group (€ 6.0 million). This allocation, which is currently still provisional, has been accounted on the basis of specific valuation by independent professionals.

| In thousands of euros                          | IFRS carrying amounts<br>before combination | Fair value    |
|--|---|---------------|
| <b>Non-current assets</b>                      | <b>34,568</b>                               | <b>43,357</b> |
| Property, plant and equipment                  | 34,561                                      | 43,350        |
| Deferred tax assets                            | 4   | 4             |
| Other non-current assets                       | 3   | 3             |
| <b>Current assets</b>                          | <b>3,385</b>                                | <b>3,385</b>  |
| Trade receivables                              | 2,649                                       | 2,649         |
| Other current assets                           | 736   | 736           |
| <b>Total assets</b>                            | <b>37,953</b>                               | <b>46,742</b> |
| <b>Non-current liabilities</b>                 | <b>3,841</b>                                | <b>6,601</b>  |
| Long-term loans                                | 3,656                                       | 3,656         |
| Employee benefits                              | 55  | 55            |
| Deferred tax liabilities                       | 0   | 2,760         |
| Non-current financial liabilities              | 130   | 130           |
| <b>Current liabilities</b>                     | <b>6,085</b>                                | <b>6,085</b>  |
| Short-term loans                               | 3,215                                       | 3,215         |
| Current portion of long-term loans             | 1,001                                       | 1,001         |
| Trade payables                                 | 1,524                                       | 1,524         |
| Tax liabilities                                | 270   | 270           |
| Other current liabilities                      | 75  | 75            |
| <b>Total liabilities</b>                       | <b>9,926</b>                                | <b>12,686</b> |
| <b>Net identifiable assets and liabilities</b> | <b>28,027</b>                               | <b>34,056</b> |
| Gain from purchase at bargain prices           |   | -6,044        |
| <b>Consideration</b>                           | <b>28,012</b>                               | <b>28,012</b> |

Revenue achieved by the company Rete di Trasmissione Brescia up until the date of acquisition - measured on the basis of IFRS accounting principles, is € 4.7 million, whilst the Company, recorded, profit of € 0.8 million.

The measurement of the fair values of acquired assets and liabilities has resulted in the following amounts being recognised:

- property, plant and equipment +€ 8.8 million;
- deferred tax liabilities +€ 2.8 million.

Compensation for the acquisition operation was, on the other hand, defined in a manner which is substantially equal to the net carrying amount of the acquired equity.

Therefore the gain from an acquisition at bargain prices, i.e. the merger surplus deriving from the business combination, amounts to € 6.0 million.

## Acquisition of Reno Solar

On 22 July 2010 and as part of the Solar Energy Project, Terna S.p.A. finalised the purchase – through Rete Rinnovabile S.r.l. (RTR), a subsidiary of Terna S.p.A. through SunTergrid S.p.A. – of the entire share capital of Reno Solar S.r.l. (“Reno Solar”) from Tre S.p.A. Tozzi Renewable Energy.

The amount paid for Reno Solar’s entire quota capital was € 8.8 million.

Reno Solar is the owner of the project relative to constructing and running a solar energy plant of approximately 35 MWp and relative concessions to the RTN in the Alfonsine Municipality (RA).

On 23 December 2010, the merger by incorporation deed of Reno Solar S.r.l. into RTR S.r.l. was stipulated, effective at 28 December 2010. The merger did not result in any change in the share capital of the incorporating company nor any share exchange ratio nor any cash compensation. The accounting and fiscal effects of the merger of Reno Solar are retroactively effective at January 2010 (i.e. the date of founding of the company).

Below we set out the amount recognised, at the purchase date, corresponding to the Company’s assets and liabilities measured at fair value at such date, and the IFRS carrying amounts immediately before the combination.



The difference between the price paid to purchase Reno Solar, € 8.8 million, and the fair value of assets and liabilities taken on and incurred, € 7.5 million, is accounted for as goodwill (€ 1.3 million). This allocation is to be considered provisional at the moment.

| In thousands of euros                          | IFRS carrying amounts<br>before combination | Fair value   |
|--|---|--------------|
| <b>Non-current assets</b>                      | <b>4,718</b>                                | <b>8,731</b> |
| Property, plant and equipment                  | 4,718                                       | 8,731        |
| <b>Other current assets</b>                    | <b>19</b>                                   | <b>19</b>    |
| Other current assets                           | 19  | 19           |
| <b>Total assets</b>                            | <b>4,737</b>                                | <b>8,750</b> |
| <b>Non-current liabilities</b>                 | <b>-</b>                                    | <b>1,260</b> |
| Deferred tax liabilities                       | -   | 1,260        |
| <b>Total liabilities</b>                       | <b>-</b>                                    | <b>1,260</b> |
| <b>Net identifiable assets and liabilities</b> | <b>4,737</b>                                | <b>7,490</b> |
| Goodwill                                       |   | 1,260        |
| <b>Consideration</b>                           | <b>8,750</b>                                | <b>8,750</b> |

The measurement of the fair values of acquired assets and liabilities has resulted in the following amounts being recognised:

- property, plant and equipment: € 4.0 million;
- deferred tax liabilities: € 1.3 million.

Goodwill from business combination is therefore € 1.3 million.

## Acquisition of Valmontone Energia

On 25 October 2010 the company RTR completed the acquisition of the shares representing overall 98.5% of the share capital of Valmontone Energia S.r.l. from Troiani & Ciarrocchi S.r.l. and C.I.EL. S.p.A.

The sellers, as consortium winners of the tender for the building lease to realise solar power plants on land owned by the Valmontone Municipality, founded the company Valmontone Energia S.r.l. on 1 October as set out by the relative licensing agreement. The business objects of the company is to design, install and manage a solar power network. Valmontone Energia S.r.l. is the owner of the project relative to constructing and running a solar energy plant of approximately 7 MWp and relative licenses to the RTN in the Valmontone Municipality (RM).

The compensation for the sale was equal to € 0.3 million, corresponding to 98.5% of the previously paid shareholding quotas (25% of the share capital) and € 0.8 million directly in favour of the company for payments of the share capital underwritten by RTR and still due. On 8 November 2010, even the shareholders Troiani & Ciarrocchi S.r.l. and C.I.EL. completed the capital payments which were still due (overall equal to 1.5% of the share capital). Troiani & Ciarrocchi and C.I.EL. granted RTR the irrevocable right to purchase the entire residual interest held by them in the company's capital, which can be exercised after commissioning and testing of the solar power plants.

In thousands of euros

IFRS carrying amounts  
before combination

Fair value

### Non-current assets

|                   |   |   |
|-------------------|---|---|
| Intangible assets | 5 | 5 |
|-------------------|---|---|

### Current assets

|                           |              |              |
|---------------------------|--------------|--------------|
| Cash and cash equivalents | 284          | 284          |
| Other current assets      | 852          | 852          |
| <b>Total assets</b>       | <b>1,141</b> | <b>1,141</b> |

### Current liabilities

|                           |   |   |
|---------------------------|---|---|
| Other current liabilities | 6 | 6 |
|---------------------------|---|---|

### Total liabilities

|          |          |
|----------|----------|
| <b>6</b> | <b>6</b> |
|----------|----------|

### Net identifiable assets and liabilities

|              |              |
|--------------|--------------|
| <b>1,135</b> | <b>1,135</b> |
|--------------|--------------|

|  |    |    |
|--|----|----|
| Equity attributable to non-controlling interests | 17 | 17 |
| Goodwill   |    | -  |

### Consideration

|              |              |
|--------------|--------------|
| <b>1,118</b> | <b>1,118</b> |
|--------------|--------------|

The company – in the period between the founding date and 31 December 2010 – did not report revenues. As a result, its contribution to the consolidated profit for 2010 is also zero.

## G. Related party transactions

As previously noted in the relative paragraph of the Directors' Report (to which reference is made), transactions with related parties carried out by the Terna Group during the year are as follows:

- **continuing operations:** relations with CDP S.p.A., the associate CESI S.p.A., the retirement funds for employees (Fondenel and Fopen) as well as – along with the companies belonging to the GSE Group – the Enel Group, the Eni Group, the national railways group "Ferrovie dello Stato" and the company Anas S.p.A.;
- **assets held for sale:** relations linked to the development of the solar energy business, including with the company CESI S.p.A., GSE S.p.A. and the companies of the Enel Group.

Transactions with related parties during the year 2010 essentially regarded services rendered as part of ordinary operations that were settled on an arm's length basis. The following table sets out the nature of the Terna Group's financial sale and purchase transactions with related parties, as well as the relevant revenue and expenses for the year and receivables and payables at 31 December 2010.

| Related party                           | Revenue transactions   | Expense transactions   |
|---|--|--|
| <b>CONTINUING OPERATIONS</b>            |  |  |
| <b>Cassa Depositi e Prestiti S.p.A.</b> |  | <b>Non energy- related items</b><br>Commission for loans to be granted.  |
| <b>CESI S.p.A.</b>                      | <b>Non energy- related items</b><br>Lease of laboratories and similar structures for specific purposes.  | <b>Non energy- related items</b><br>Technical consultancy, studies and research, projects and experimentation.   |
| <b>GSE Group</b>                        | <b>Energy- related items</b><br>Remuneration of the grid and MIS component, energy sale, rights of withdrawal, rights to use transport capacity for interconnections<br><br><b>Non energy- related items</b><br>Specialist services (remote console), leases, IT services.   | <b>Energy- related items</b><br>Energy purchases, rights to use transport capacity for interconnections.   |
| <b>Enel Group</b>                       | <b>Energy- related items</b><br>Remuneration of NTG and metering aggregation, energy sales, rights of withdrawal, coverage of transmission costs, rights to use transport capacity for interconnections.<br><br><b>Non energy- related items</b><br>Leases and rentals, line maintenance on property lines, optic fibre housing on property lines, grants for working on live power lines. | <b>Energy- related items</b><br>Metering aggregation, energy purchases, right to use transport capacity for interconnections, coverage of joint management, joint management fees.<br><br><b>Non energy- related items</b><br>Restitution of electric power discount, building services, supply of MV power to new stations, specialist services for connection to Terna control and protection systems, technical services and restructuring of plants. |
| <b>ENI Group</b>                        | <b>Energy- related items</b><br>Withdrawal rights, energy sale, right to use transport capacity for interconnections, coverage of transmission costs, remuneration of grid.<br><br><b>Non energy- related items</b><br>Interventions and line maintenance.   | <b>Energy- related items</b><br>Energy purchase, coverage of joint management, remuneration of NTG.  |
| <b>Ferrovie Group</b>                   | <b>Energy- related items</b><br>Remuneration of NTG.<br><br><b>Non energy- related items</b><br>Line moving, connection grants.  | <b>Energy- related items</b><br>Remuneration of NTG.<br><br><b>Non energy- related items</b><br>Right-of-way fees.   |
| <b>ANAS S.p.A.</b>                      | <b>Non energy- related items</b><br>Line moving, connection grants.  |  |
| <b>Fondenel and Fopen</b>               |  | <b>Non energy- related items</b><br>Pension contributions borne by the Terna Group.  |
| <b>ASSETS HELD FOR SALE</b>             |  |  |
| <b>CESI S.p.A.</b>                      |  | <b>Non energy- related items</b><br>Specialist services for the realization of photovoltaic plants.  |
| <b>GSE Group</b>                        | <b>Non energy- related items</b><br>Dedicated collection of energy from photovoltaic plants, incentives for energy production from photovoltaic source   |  |
| <b>Enel Group</b>                       |  | <b>Non energy- related items</b><br>Connection to the MW grid of photovoltaic plants, interventions on the lines   |

| Company<br>in millions of euros      | Income statement                         |                              |                              |  |                              |                              |
|--------------------------------------|--|------------------------------|------------------------------|--|------------------------------|------------------------------|
|                                      | Revenues                                 |                              |                              | Expenses                                 |                              |                              |
|                                      | CTR and other<br>energy-related<br>items | Pass-through<br>energy items | Non energy-<br>related items | CTR and other<br>energy-related<br>items | Pass-through<br>energy items | Non energy-<br>related items |
| Continuing operations:               |  |                              |                              |  |                              |                              |
| De facto parent                      |  |                              |                              |  |                              |                              |
| CDP                                  | -  | -                            | -                            | -  | -                            | 1.3                          |
| <b>Total de facto parent</b>         | <b>-</b>                                 | <b>-</b>                     | <b>-</b>                     | <b>-</b>                                 | <b>-</b>                     | <b>1.3</b>                   |
| Associated:                          |  |                              |                              |  |                              |                              |
| CESI S.p.A.                          | -  | -                            | 0.3                          | -  | -                            | 2.6                          |
| <b>Total associated companies</b>    | <b>-</b>                                 | <b>-</b>                     | <b>0.3</b>                   | <b>-</b>                                 | <b>-</b>                     | <b>2.6</b>                   |
| Other related companies:             |  |                              |                              |  |                              |                              |
| GSE Group                            | 14.6                                     | 1,078.8                      | 0.4                          | -  | 475.1                        | -                            |
| Enel Group                           | 1,148.6                                  | 751.6                        | 4.7                          | 5.9                                      | 1,235.9                      | 6.5                          |
| Eni Group                            | 2.1                                      | 197.2                        | 0.5                          | -  | 145.0                        | 0.1                          |
| Ferrovie Group                       | 0.8                                      | 34.3                         | 0.1                          | 7.0                                      | 3.4                          | 0.1                          |
| ANAS S.p.A.                          | -  | -                            | -                            | -  | -                            | -                            |
| <b>Total other related companies</b> | <b>1,166.1</b>                           | <b>2,061.9</b>               | <b>5.7</b>                   | <b>12.9</b>                              | <b>1,859.4</b>               | <b>6.7</b>                   |
| Pension funds:                       |  |                              |                              |  |                              |                              |
| Fondenel                             |  |                              |                              |  |                              | 0.4                          |
| Fopen                                |  |                              |                              |  |                              | 1.7                          |
| <b>Total pension funds</b>           | <b>-</b>                                 | <b>-</b>                     | <b>-</b>                     | <b>-</b>                                 | <b>-</b>                     | <b>2.1</b>                   |
| <b>Total continuing operations</b>   | <b>1,166.1</b>                           | <b>2,061.9</b>               | <b>6.0</b>                   | <b>12.9</b>                              | <b>1,859.4</b>               | <b>12.7</b>                  |
| <b>Assets held for sale</b>          |  |                              |                              |  |                              |                              |
| Associated companies:                |  |                              |                              |  |                              |                              |
| CESI S.p.A.                          | -  | -                            | -                            | -  | -                            | -                            |
| <b>Total associated companies</b>    | <b>-</b>                                 | <b>-</b>                     | <b>-</b>                     | <b>-</b>                                 | <b>-</b>                     | <b>-</b>                     |
| Other related companies:             |  |                              |                              |  |                              |                              |
| GSE Group                            | -  | -                            | 1.7                          | -  | -                            | -                            |
| Enel Group                           | -  | -                            | -                            | -  | -                            | -                            |
| <b>Total other relate companies</b>  | <b>-</b>                                 | <b>-</b>                     | <b>1.7</b>                   | <b>-</b>                                 | <b>-</b>                     | <b>-</b>                     |
| <b>Total assets held for sale</b>    | <b>-</b>                                 | <b>-</b>                     | <b>1.7</b>                   | <b>-</b>                                 | <b>-</b>                     | <b>-</b>                     |

| Company<br>In millions of euros      | Statement of financial position  |                                 |                                   |                |
|--------------------------------------|----------------------------------|---------------------------------|-----------------------------------|----------------|
|                                      | Property, plant<br>and equipment | Receivables<br>and other assets | Payables<br>and other liabilities | Guarantees (*) |
|                                      | Capitalized costs                |                                 |                                   |                |
| Continuing operations:               |                                  |                                 |                                   |                |
| De facto parent                      |                                  |                                 |                                   |                |
| CDP                                  | -                                | 0.4                             | 2.4                               | -              |
| <b>Total de facto parent</b>         | <b>-</b>                         | <b>0.4</b>                      | <b>2.4</b>                        | <b>-</b>       |
| Associated companies:                |                                  |                                 |                                   |                |
| CESI S.p.A.                          | 19.4                             | -                               | 5.0                               | 3.5            |
| <b>Total associated companies</b>    | <b>19.4</b>                      | <b>-</b>                        | <b>5.0</b>                        | <b>3.5</b>     |
| Other related companies:             |                                  |                                 |                                   |                |
| GSE Group                            | -                                | 15.7                            | 1.7                               | -              |
| Enel Group                           | 19.6                             | 134.8                           | 43.1                              | 435.4          |
| Eni Group                            | -                                | 2.1                             | 10.9                              | 30.3           |
| Ferrovie Group                       | -                                | 1.3                             | 0.8                               | 22.0           |
| ANAS S.p.A.                          | -                                | 0.6                             | 0.6                               | -              |
| <b>Total other related companies</b> | <b>19.6</b>                      | <b>154.5</b>                    | <b>57.1</b>                       | <b>487.7</b>   |
| Pension funds:                       |                                  |                                 |                                   |                |
| Fondenel                             | -                                | -                               | -                                 | -              |
| Fopen                                | -                                | -                               | 1.4                               | -              |
| <b>Total pension funds</b>           | <b>-</b>                         | <b>-</b>                        | <b>1.4</b>                        | <b>-</b>       |
| <b>Total continuing operations</b>   | <b>39.0</b>                      | <b>154.9</b>                    | <b>65.9</b>                       | <b>491.2</b>   |
| <b>Assets held for sale</b>          |                                  |                                 |                                   |                |
| Associated companies:                |                                  |                                 |                                   |                |
| CESI S.p.A.                          | 0.5                              | -                               | -                                 | -              |
| <b>Total associated companies</b>    | <b>0.5</b>                       | <b>-</b>                        | <b>-</b>                          | <b>-</b>       |
| Other related companies:             |                                  |                                 |                                   |                |
| GSE Group                            | -                                | 0.8                             | -                                 | -              |
| Enel Group                           | 0.4                              | -                               | 0.3                               | -              |
| <b>Total other relate companies</b>  | <b>0.4</b>                       | <b>0.8</b>                      | <b>0.3</b>                        | <b>-</b>       |
| <b>Total assets held for sale</b>    | <b>0.9</b>                       | <b>0.8</b>                      | <b>0.3</b>                        | <b>-</b>       |

(\*) The guarantees refer to the bank guarantees received on contracts.







## H. Significant non-recurring events and operations, atypical or unusual transactions

No significant, non-recurring, atypical or unusual transactions – with the exception of those described above – were carried out during 2010, either with third parties or with related parties.

## I. Notes to the consolidated statement of cash flows

The cash flows generated from **continuing operations** in the year amounted to around € 773.4 million, which reflects around € 1,374.1 million in cash from operating activities (self-financing) and around € 600.7 million in financial resources generated by the management of net working capital.

**Investing activities** also absorbed net financial resources of around € 1,702.4 million, including € 1,092.2 million invested in property, plant and equipment (€ 1,104.4 million net of grants related to assets totalling € 12.2 million received in the period), and € 58.1 million invested in intangible assets (€ 58.3 million net of grants related to assets totalling € 0.2 million received in the period). In this context also:

- fair value of property, plant and equipment from the purchase (on 5 August 2010) of investment in Rete di Trasmissione Brescia S.r.l., € 43.4 million;
- the value for the year for photovoltaic plant construction contracts for assets held for sale, equal to € 503.5 million, is based essentially on the value of investments sustained during the year and increased by the margin accrued pursuant to the conditions - with particular reference to the Enterprise Value – that were contractually defined in the preliminary sales agreement of the subsidiary RTR.

The net increase in cash flows from **financing activities**, € 1,085.2 million, essentially reflects the combined effect of the rise in financial payables (+€ 948.3 million/long-term, including the short-term portion and net of the FVH derivatives, and +€ 33.1 million short-term) and the decrease in short-term financial investments (€ 500.0 million) ascribable to realisation of securities issued by UBS and MPS (€ 500.0 million), as offset by payment of the final dividend for 2009 to the Parent's shareholders (€ 240.4 million) and the advance on the 2010 dividend (€ 160.4 million). The changes in equity (+€ 7.2 million in total) also include the effects deriving from the exercise of stock options during the year.

Consequently, the financial resources used in for investing activities and the remuneration of equity amounted to € 2,098.6 million in the year, part of which (€ 773.4 million) was covered by the cash flows generated by operating activities, while the balance came from new debt.

## L. Events after the reporting date

### Continuing operations

#### Acquisition of the shareholding in CGES and agreement for the construction of the electrical connection between Italy-Montenegro

On **23 November 2010** Terna signed the definitive agreement for the strategic partnership with the transmission operator of Montenegro, CrnoGorski Elektroprenosni Sistem AD ("CGES"), and the government of Montenegro, acting in the capacity of majority shareholder of CGES; this agreement refers to the construction of the new electrical connection between Italy-Montenegro and the strategic Terna-CGES partnership. The transaction was completed in January following the occurrence of the conditions precedent. The stipulation was completed following the approval, on the part of the shareholders of CGES, of the share capital increase for Terna and the adoption of new Bylaws. Terna therefore became the shareholder of CGES with 22.09% of the share capital and, in its capacity as the new shareholder, undersigned the shareholders' agreement relative to the new governance system and the industrial contract for investments.

The agreement represents the end point of a process of industrial and country cooperation and is part of the intergovernmental agreements between Italy and Montenegro which were initiated on 19 December 2007 with the start-up of activities of the Italy-Montenegro Work Group and consolidated on 6 February 2010 by means of the contract which ratified the commitment at an institutional level for the construction of a new submarine electrical connection and the implementation of partnerships with national transmission operators.

It is forecasted that the overall investment of Terna for the first “power linkage” with the Balkans will total circa € 760 million. The investment of CGES for the connection to the existing grid and the reinforcement of the local grid will total circa € 100 million.

### 2011-2015 Business Plan

On **14 February 2011** Terna presented to financial analysts the Company’s 2011-2015 business plan, after approval of the plan by the Board of Directors on that same date.

The 2011-2015 plan of the Terna Group follows five main guidelines:

traditional regulated activities: Increase of investments from € 4.3 to circa € 5 billion (+15%) in order to modernize the grid; development investments for which incentive-based remuneration is planned represents circa 82% of the total and increased from € 3.3 billion to € 4 billion: non-traditional activities. Investment activities were tripled for these activities, with planned allocations of up to € 1 billion. In particular, the development of an additional set of photovoltaic projects of circa 50 MWp is planned for the course of 2011. In addition, investment opportunities will be evaluated, including those in the sector for energy efficiency in addition to those relative to the construction and management of grid infrastructures for connecting the local grid of renewable energy sources within the Balkan area as well as systems for energy storage and batters in the Italian grid;

- improved margins: increasing revenue and containing costs will improve Group profitability from the current 74% to 78% at the end of the period covered by the plan;
- solid financial structure: during the period of the business plan, a commitment to maintain the ratio between debt and regulated invested capital (RAB) below 60%;
- confirmation of dividend policy: the 2011-2015 Strategic Plan confirms the dividend policy. As had previously occurred with the sale of Terna Participações, part of the capital gains attained with the sale of non-traditional assets may integrate the above-mentioned policy which provides for an annual growth of 4%, assuming the year 2008 as the year of reference.

### Founding of new companies of the Group

On **8 March 2011**, the subsidiary SunTergrid S.p.A. formed “Nuova Rete Solare S.r.l.” (“NRTS S.r.l.”) with a share capital of € 10,000. The corporate purpose of this new company is to design, install, manage, develop and maintain grids and other infrastructure connected to such grids, as well as plant and equipment for the transmission and dispatching of electricity, and for other segments of the energy sector and similar, related or connected sectors, together with plant for the generation of electricity from renewable or other sources, for self consumption or for sale.

### 10-year bond issue for € 1.25 billion

On **8 March 2011**, Terna launched a bond in Euro on the market, with a fixed rate and 10-year maturity, for a total of € 1.25 billion, as part of its Euro Medium Term Notes (EMTN) program; this bond was rated A+ by Standard and Poor’s, A2 by Moody’s and A+ by Fitch.

The bond’s maturity is set for 15 March 2021 with an annual coupon of 4.750% and an issue price of 99.245. The security was priced with a spread of 130 base points with respect to the mid swap.

The securities are listed within the Luxembourg Stock Exchange.

The operation – which targets Institutional Investors – was placed by a banking syndicate composed of Banca Akros S.p.A., MPS Capital Services S.p.A., Natixis, UniCredit Bank AG and WestLB AG acting in the capacity of joint-lead managers and joint-bookrunners.

The transaction is intended to finance the grid development investments envisaged in the Parent’s business plan.

### The new “SA.PE.I.” power line which connects Sardinia and the Italian peninsula was inaugurated

On **17 March 2011**, Terna inaugurated the new SA.PE.I. power line, an acronym for “SArdegna-PENisola-Italiana”, (Sardinia-Italian peninsula); this power line is the first direct electrical connection between Sardinia and the continent and it is the most important and technologically advanced high voltage power line that has ever been constructed in Italy. The infrastructure broke numerous records, including: it is the longest “power line” in the world with a power of 1,000 megawatt; it is the deepest in the world, crossing 435 km between Fiumesanto, in Sardinia, and Latina, in Lazio, at a depth of 1,640 m; it is the largest investment: totalling € 750 million, it is the most significant investment ever completed in Italy for a single electrical infrastructure.

The project was financed for more than 50% by Terna with its own equity while the remaining portion was financed with an allocation of € 373 million from the European Investment Bank (EIB) given its elevated strategic value. It has multiple economic, electrical and environmental benefits. This work, in fact, allows for savings of € 70 million per year for the electrical system due to the removal of “bottlenecks” between the Sardinia region and the rest of the electrical market. It also allows for an increase in the safety of the Sardinian electrical system and a more secure coverage of the power requirements of Lazio and central Italy due to the utilization of more efficient energy even from Sardinia.

## Assets held for sale

### Financing Contract

On **28 January 2011**, the company RTR – in light of the sale – signed a re-financing contract with a duration of 18 years. The overall maximum amount of the re-financing operation totals € 593.8 million (including 521.3 in cash loans and 72.5 in endorsement loans) and aims to re-finance – on a non-recourse project financing basis – the investments sustained for the realization of the portfolio of photovoltaic plants owned by Rete Rinnovabile.

The operation was completed with a pool of seven banks that include Banca Popolare di Milano, Gruppo Credito Valtellinese, Meliorbanca and Banca Popolare dell'Emilia Romagna, MPS Capital Services (which will also act in the capacity of Facility Agent), Natixis, Unicredit Corporate Banking and West LB.

### Capital contribution payment in favour of Valmontone Energia S.r.l.

On **4 February 2011** RTR completed a payment of € 10.0 million to Valmontone Energia S.r.l. as a capital contribution payment in order to complete the photovoltaic plant.

### Sale of Rete Rinnovabile S.r.l. completed

In implementation of the agreement signed on 18 October 2010 by Terna S.p.A., SunTergrid S.p.A. and Terra Firma Investments (GP) 3 Limited (wholly owned by Terra Firma Capital Partners III, L.P.), on **31 March 2011**, the transfer to RTR Acquisition S.r.l. (an indirect subsidiary of Terra Firma Investment (GP) 3 Limited) of 100% of the share capital of Rete Rinnovabile S.r.l. ("RTR S.r.l.") was completed.

RTR S.r.l. owns 62 photovoltaic plants, located in 11 different regions of Italy, for a total capacity of 143.7 MWp, of which 101.6 MWp will benefit from the 2010 Energy Account tariffs for the 1<sup>st</sup> quarter 2011. The sale of the investment in RTR S.r.l. has resulted in total net income of around € 204 million and a reduction in the effective net financial debt of continuing operations of the Terna Group for more than € 200 million.

The completion of the sale confirmed the effect on the 2010 consolidated income statement, booked as the contract margin in terms as compared with total costs sustained during the year, on the basis of works progress, as described in full previously, amounts to € 147 million. The difference will instead be recognized on an accruals basis in 2011.

It is also specified that in addition to renting the land, Terna will also provide RTR S.r.l. with plant maintenance, surveillance and monitoring services, according to multiyear contracts defined in the context of the sale. At the end of the individual rental contracts, Terna will regain possession of the leased areas.

## Information pursuant to art. 149-duodecies of the CONSOB Issuers Regulations

The following table, prepared in accordance with art. 149-duodecies of the CONSOB Issuers Regulations, reports the fees for 2010 for the audit and non-audit services provided to the Terna Group by the same independent auditors.

| Euros                | Entity providing service | Amounts due for the year |
|----------------------|--------------------------|--------------------------|
| Auditing services    | KPMG S.p.A.              | 673,274.60               |
| Attestation services | KPMG S.p.A.              | 169,370.30               |
| <b>Total</b>         |                          | <b>842,644.90</b>        |

***Certification of the consolidated financial statement pursuant to art. 81-ter of Consob Regulation n. 11971 dated May 14, 1999 and subsequent amendments and additions***

1. The undersigned Flavio Cattaneo as CEO and Luciano di Bacco as Executive in Charge of preparing the accounting documents of Terna S.p.A. , also pursuant to art. 154-bis paragraphs 3 and 4 of Legislative Decree n. 58 dated February 24, 1998 hereby certify:
  - the adequacy with regard to the characteristics of the company and
  - the actual implementation of the administrative and accounting procedures for preparing the consolidated financial statement for 2010.
2. With regard to the above, nothing significant emerged.
3. It is also certified that
  - 3.1. the consolidated financial statement as of December 31, 2010:
    - a) was prepared in compliance with the applicable international accounting standards recognized by the European Community pursuant to regulation (EC) n. 1606/2002 of the European Parliament and of the Council, dated July 19, 2002 as well as with the provisions implementing art. 9 of Legislative Decree n. 38/2005.
    - b) corresponds to the results of the books and of the accounting records.
    - c) provides a truthful and correct representation of the statement of assets and liabilities and of the economic and financial situation of the issuer and of all the companies included in the consolidation.
  - 3.2. The Report on the management includes an accurate and faithful analysis of the management trend and results and of the issuer's situation, and of all the companies included in the consolidation, together with the description of the principal risks and uncertainties faced.

Rome, March 31, 2011

Delegated administrative bodies

The Executive in Charge  
of preparing the Company's accounting documents

Flavio Cattaneo

Luciano Di Bacco

*(Signed on the original)*

*This report has been translated into the English language solely for the convenience of international readers.*





Report





KPMG S.p.A.  
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(Translation from the Italian original which remains the definitive version)

## Report of the auditors in accordance with articles 14 and 16 of Legislative decree no. 39 of 27 January 2010

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 2010, comprising the income statement, statement of comprehensive income, statement of financial position, statement of changes in equity, statement of cash flows and notes thereto. The parent's directors are responsible for the preparation of these financial statements in accordance with the International Financial Reporting Standards endorsed by the European Union and the Italian regulations implementing article 9 of Legislative decree no. 38/05. 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.

The consolidated financial statements present the prior year corresponding figures and the statement of financial position as at 1 January 2009 for comparative purposes. As disclosed in the notes, following the application of IFRIC 12 *Service Concession Arrangements* to electricity dispatching activities carried out under concession, the parent's directors restated some of the corresponding figures included in the prior year consolidated financial statements and statement of financial position as at 1 January 2009, which derives from the consolidated financial statements at 31 December 2008. We audited the 2009 and 2008 consolidated financial statements and issued our reports thereon on 9 April 2010 and 31 March 2009, respectively. We have examined the methods used to restate the prior year corresponding figures and related disclosures for the purposes of expressing an opinion on the consolidated financial statements at 31 December 2010.

KPMG S.p.A. è una società per azioni di diritto italiano e fa parte del network KPMG di entità indipendenti affiliate a KPMG International Cooperative ("KPMG International"), entità di diritto svizzero.

Ancona Asolo Bari Bergamo  
Bologna Bolzano Brescia Cagliari  
Cagliari Como Firenze Genova  
Lecce Milano Napoli Novara  
Padova Palermo Parma Perugia  
Pesaro Roma Torino Trento  
Treviso Udine Varese Verona

Società per azioni  
Capitale sociale  
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Partita IVA 00789600159  
VAT number IT00789600159  
Sede legale: Via Vittor Pisani, 25  
20134 Milano MI (ITALY)





- 3 In our opinion, the consolidated financial statements of the TERNA Group as at and for the year ended 31 December 2010 comply with the International Financial Reporting Standards endorsed by the European Union and the Italian regulations implementing article 9 of Legislative decree no. 38/05. Therefore, they are clearly stated and give a true and fair view of the financial position of the TERNA Group as at 31 December 2010, the results of its operations and its cash flows for the year then ended.
- 4 The directors of TERNA S.p.A. are responsible for the preparation of a directors' report on the financial statements and a report on the corporate governance and ownership structure in accordance with the applicable laws and regulations. Our responsibility is to express an opinion on the consistency of the directors' report and the information required by article 123-bis.1.c/d/f/l/m and article 123-bis.2.b of Legislative decree no. 58/98 disclosed in the report on the corporate governance and ownership structure with the financial statements to which they refer, as required by the law. For this purpose, we have performed the procedures required by the Italian Standard on Auditing 001 issued by the Italian Accounting Profession and recommended by Consob. In our opinion, the directors' report and the information required by article 123-bis.1.c/d/f/l/m and article 123-bis.2.b of Legislative decree no. 58/98 disclosed in the report on the corporate governance and ownership structure are consistent with the consolidated financial statements of the TERNA Group as at and for the year ended 31 December 2010.

Rome, 18 April 2011

KPMG S.p.A.

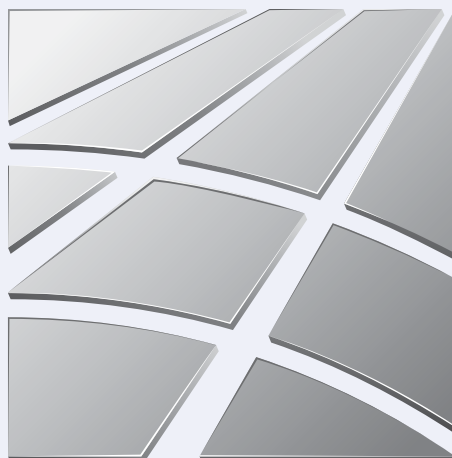
(signed on the original)

Marco Maffei  
Director of Audit









**Separate financial statements**  
as at and for the year ended 31 December 2010

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Separate financial statements

# Income statement

| In euros   | Note | 2010   | 2009  |
|--|------|--|---|
| <b>A. Revenue</b>  |      |  |   |
| 1. Revenue from sales and services<br><i>of which: related parties</i>   | 1    | 1,459,126,551<br>1,420,000,250                         | 1,282,690,152<br>1,303,984,808                          |
| 2. Other revenue and income<br><i>of which: related parties</i>  | 2    | 45,943,205<br>4,073,007                                | 42,014,718<br>2,362,640                                 |
| <b>Total revenue</b>   |      | <b>1,505,069,756</b>                                   | <b>1,324,704,870</b>                                    |
| <b>B. Operating expenses</b>   |      |  |   |
| 1. Raw materials and consumables<br><i>of which: related parties</i>   | 3    | 36,666,582<br>80,650                                   | 19,921,629<br>127,032                                   |
| 2. Services<br><i>of which: related parties</i>  | 4    | 166,471,383<br>7,479,433                               | 147,996,859<br>7,944,583                                |
| 3. Personnel expense<br>- <i>personnel expense, gross</i><br>- <i>personnel expense, capitalised</i><br><i>of which: related parties</i> | 5    | 214,836,298<br>276,400,504<br>-61,564,206<br>3,554,549 | 186,228,445<br>244,066,884<br>-57,838,439<br>3,352,2155 |
| 4. Amortisation, depreciation and impairment losses  | 6    | 318,768,336  | 296,288,921   |
| 5 Other operating expenses<br><i>of which: related parties</i>   | 7    | 17,808,652<br>246,904                                  | 19,902,206<br>626,025                                   |
| <b>Total operating expenses</b>  |      | <b>754,551,251</b>                                     | <b>670,338,060</b>                                      |
| <b>A-B Operating profit</b>  |      | <b>750,518,505</b>                                     | <b>654,366,810</b>                                      |
| <b>C. Net financial expense</b>  |      |  |   |
| 1. Financial income<br><i>of which: related parties</i>  | 8    | 29,180,259<br>17,960,646                               | 31,420,051<br>5,333,666                                 |
| 2. Financial expense<br><i>of which: related parties</i>   | 8    | -116,919,577<br>1,353,972                              | -180,531,811<br>1,318,345                               |
| <b>D. Pre-tax profit</b>   |      | <b>662,779,187</b>                                     | <b>505,255,050</b>                                      |
| E. Income taxes  | 9    | 230,524,539  | 179,443,183   |
| <b>F. Profit from continuing operations</b>  |      | <b>432,254,648</b>                                     | <b>325,811,867</b>                                      |
| <b>G. Profit from discontinued operations and assets held for sale</b>   | 10   | <b>1,433,700</b>                                       | <b>464,231,668</b>                                      |
| <b>H. Profit for the year</b>  |      | <b>433,688,348</b>                                     | <b>790,043,535</b>                                      |

## Statement of comprehensive income

| In euros                                | Note | 2010               | 2009               |
|---|------|--------------------|--------------------|
| <b>Profit for the year</b>              |      | <b>433,688,348</b> | <b>790,043,535</b> |
| Other comprehensive income              |      |                    |                    |
| - Cash flow hedges net of tax effect    | 21   | 25,917,385         | -11,938,311        |
| <b>Comprehensive income of the year</b> |      | <b>459,605,733</b> | <b>778,105,224</b> |

# Statement of financial position

## Assets

| In euros   | Note | at 31 Dec. 2010       | at 31 Dec. 2009      | at 1 Jan. 2009       |
|--|------|-----------------------|----------------------|----------------------|
| <b>A. Non-current assets</b>                               |      |                       |                      |                      |
| 1. Property, plant and equipment                           | 11   | 6,687,666,965         | 5,890,992,393        | 5,332,424,362        |
| <i>of which: related parties</i>                           |      | 48,665,342            | 15,340,771           | 21,102,250           |
| 2. Goodwill  | 12   | 88,577,142            | 88,577,142           | 88,577,142           |
| 3. Intangible assets                                       | 13   | 274,008,599           | 261,548,444          | 250,388,206          |
| 4. Deferred tax assets                                     | 25   | 0                     | 0                    | 0                    |
| 5. Non-current financial assets                            | 14   | 1,284,012,471         | 1,198,860,941        | 331,526,685          |
| <i>of which: related parties</i>                           |      | 500,000,000           | 500,000,000          | 0                    |
| 6. Other non-current assets                                | 15   | 6,295,263             | 5,539,468            | 4,644,397            |
| <b>Total non-current assets</b>                            |      | <b>8,340,560,440</b>  | <b>7,445,518,388</b> | <b>6,007,560,792</b> |
| <b>B. Current assets</b>                                   |      |                       |                      |                      |
| 1. Inventories   | 16   | 11,353,045            | 11,707,939           | 16,640,688           |
| 2. Trade receivables                                       | 17   | 1,495,632,378         | 1,177,146,436        | 1,705,981,614        |
| <i>of which: related parties</i>                           |      | 157,663,489           | 130,665,643          | 102,310,484          |
| 3. Current financial assets                                | 14   | 2,921,817             | 503,278,695          | 6,739,656            |
| <i>of which: related parties</i>                           |      | 2,816,880             | 2,684,770            | 0                    |
| 4. Cash and cash equivalents                               | 18   | 168,718,782           | 81,468               | 689,183,999          |
| <i>of which: related parties</i>                           |      | 18,604,996            | 0                    | 0                    |
| 5. Tax assets  | 19   | 16,797,638            | 18,372,343           | 25,848,954           |
| 6. Other current assets                                    | 15   | 18,643,499            | 26,521,078           | 21,096,407           |
| <i>of which: related parties</i>                           |      | 761,928               | 1,088,319            | 0                    |
| <b>Total current assets</b>                                |      | <b>1,714,067,159</b>  | <b>1,737,107,959</b> | <b>2,465,491,318</b> |
| <b>C. Discontinued operations and assets held for sale</b> |      |                       |                      |                      |
|  | 20   | <b>504,591,056</b>    | <b>57,367</b>        | <b>00</b>            |
| <b>Total assets</b>  |      | <b>10,559,218,655</b> | <b>9,182,683,714</b> | <b>8,473,052,110</b> |

## Statement of financial position

### Liabilities and equity

| In euros  | Note      | at 31 Dec. 2010       | at 31 Dec. 2009      | at 1 Jan. 2009       |
|---|-----------|-----------------------|----------------------|----------------------|
| <b>D. Equity</b>  |           |                       |                      |                      |
| 1. Share capital  |           | 440,967,054           | 440,199,936          | 440,199,936          |
| 2. Other reserves   |           | 791,002,191           | 758,627,068          | 770,565,378          |
| 3. Retained earnings  |           | 1,029,032,957         | 619,512,997          | 600,365,600          |
| 4. Interim dividend   |           | -160,351,656          | -140,063,616         | -118,453,801         |
| 5. Profit for the year  |           | 433,688,348           | 790,043,535          | 335,290,988          |
| <b>Total equity</b>   | <b>21</b> | <b>2,534,338,894</b>  | <b>2,468,319,920</b> | <b>2,027,968,101</b> |
| <b>E. Non-current liabilities</b>   |           |                       |                      |                      |
| 1. Long-term loans  | 22        | 5,147,465,361         | 4,199,231,857        | 3,646,940,434        |
| 2. Employee benefits  | 23        | 122,338,330           | 125,067,204          | 153,929,935          |
| 3. Provisions for risks and charges   | 24        | 165,009,275           | 147,861,138          | 81,603,585           |
| 4. Deferred tax liabilities   | 25        | 248,908,985           | 276,355,306          | 310,821,642          |
| 5. Non-current financial liabilities  | 22        | 47,126,002            | 82,553,826           | 66,685,904           |
| 6. Other non-current liabilities  | 26        | 136,604,167           | 151,567,857          | 150,381,569          |
| <i>of which: related parties</i>  |           | 0                     | 0                    | 783,412              |
| <b>Total non-current liabilities</b>  |           | <b>5,867,452,120</b>  | <b>4,982,637,188</b> | <b>4,410,363,069</b> |
| <b>F. Current liabilities</b>   |           |                       |                      |                      |
| 1. Short-term loans   | 22        | 73,118,084            | 42,632,206           | 503,487              |
| <i>of which: related parties</i>  |           | 0                     | 2,640,220            | 503,487              |
| 2. Current portion of long-term loans                                       | 22        | 59,689,067            | 59,689,067           | 44,617,297           |
| 3. Trade payables   | 27        | 1,552,764,668         | 1,487,642,509        | 1,874,362,814        |
| <i>of which: related parties</i>  |           | 67,626,377            | 45,910,293           | 52,218,309           |
| 4. Tax liabilities  | 27        | 69,094,800            | 20,825,680           | 0                    |
| 5. Current financial liabilities  | 22        | 24,240,177            | 25,524,303           | 32,510,479           |
| <i>of which: related parties</i>  |           | 2,423,611             | 1,156,250            | 0                    |
| 6. Other current liabilities  | 27        | 133,146,671           | 95,412,841           | 82,726,863           |
| <i>of which: related parties</i>  |           | 3,143,863             | 5,517,902            | 6,981,501            |
| <b>Total current liabilities</b>  |           | <b>1,912,053,467</b>  | <b>1,731,726,606</b> | <b>2,034,720,940</b> |
| <b>G. Liabilities from discontinued operations and assets held for sale</b> |           |                       |                      |                      |
|   | 20        | 245,374,174           | 0                    | 0                    |
| <b>Total liabilities and equity</b>   |           | <b>10,559,218,655</b> | <b>9,182,683,714</b> | <b>8,473,052,110</b> |

# Statement of changes in equity

31 DECEMBER 2009-31 DECEMBER 2010

SHARE CAPITAL AND RESERVES OF TERNA S.P.A.

| In millions of euros  | Share/quota capital | Legal reserve | Share premium reserve | Hedging reserve | Other reserves | Retained earnings | Interim dividend | Profit for the year | Equity         |
|---|---------------------|---------------|-----------------------|-----------------|----------------|-------------------|------------------|---------------------|----------------|
| <b>Equity at 31 December 2009 (*)</b>                                 | <b>440.2</b>        | <b>88.0</b>   | <b>1.8</b>            | <b>-61.2</b>    | <b>730.1</b>   | <b>619.5</b>      | <b>-140.1</b>    | <b>790.0</b>        | <b>2,468.3</b> |
| <b>Profit for the year</b>  |                     |               |                       |                 |                |                   |                  | <b>433.7</b>        | <b>433.7</b>   |
| <b>Other comprehensive income:</b>                                    |                     |               |                       |                 |                |                   |                  |                     |                |
| Change in fair value of cash flow hedge derivatives net of tax effect |                     |               |                       | 25.9            |                |                   |                  |                     | 25.9           |
| <b>Total other comprehensive income</b>                               | <b>0.0</b>          | <b>0.0</b>    | <b>0.0</b>            | <b>25.9</b>     | <b>0.0</b>     | <b>0.0</b>        | <b>0.0</b>       | <b>0.0</b>          | <b>25.9</b>    |
| <b>Comprehensive income</b>   | <b>0.0</b>          | <b>0.0</b>    | <b>0.0</b>            | <b>25.9</b>     | <b>0.0</b>     | <b>0.0</b>        | <b>0.0</b>       | <b>433.7</b>        | <b>459.6</b>   |
| <b>Transactions with equity owners:</b>                               |                     |               |                       |                 |                |                   |                  |                     |                |
| Allocation of 2009 profit   |                     |               |                       |                 |                |                   |                  |                     |                |
| - 2009 dividend   |                     |               |                       |                 |                |                   | 140.1            | -380.5              | -240.4         |
| - Retained earnings 2009  |                     |               |                       |                 |                | 409.5             |                  | -409.5              | 0.0            |
| Exercise of stock options   | 0.8                 |               | 6.8                   |                 | -0.4           |                   |                  |                     | 7.2            |
| 2010 interim dividend   |                     |               |                       |                 |                |                   | -160.4           |                     | -160.4         |
| <b>Total transactions with equity owners</b>                          | <b>0.8</b>          | <b>0.0</b>    | <b>6.8</b>            | <b>0.0</b>      | <b>-0.4</b>    | <b>409.5</b>      | <b>-20.3</b>     | <b>-790.0</b>       | <b>-393.6</b>  |
| <b>Equity at 31 December 2010</b>                                     | <b>441.0</b>        | <b>88.0</b>   | <b>8.6</b>            | <b>-35.3</b>    | <b>729.7</b>   | <b>1,029.0</b>    | <b>-160.4</b>    | <b>433.7</b>        | <b>2,534.3</b> |

(\*) The retrospective application of IFRIC 12 - Service concession arrangements had no effect on opening equity at 31 December 2009.

31 DECEMBER 2008-31 DECEMBER 2009

SHARE CAPITAL AND RESERVES OF TERNA S.P.A.

| In millions of euros  | Share/quota capital | Legal reserve | Share premium reserve | Hedging reserve | Other reserves | Retained earnings | Interim dividend | Profit for the year | Equity         |
|---|---------------------|---------------|-----------------------|-----------------|----------------|-------------------|------------------|---------------------|----------------|
| <b>Equity at 31 December 2008</b>                                     | <b>440.2</b>        | <b>88.0</b>   | <b>1.8</b>            | <b>-49.3</b>    | <b>730.1</b>   | <b>600.4</b>      | <b>-118.5</b>    | <b>335.3</b>        | <b>2,028.0</b> |
| <b>Profit for the year</b>  |                     |               |                       |                 |                |                   |                  | <b>790.0</b>        | <b>790.0</b>   |
| <b>Other comprehensive income:</b>                                    |                     |               |                       |                 |                |                   |                  |                     |                |
| Change in fair value of cash flow hedge derivatives net of tax effect |                     |               |                       | -11.9           |                |                   |                  |                     | -11.9          |
| <b>Total other comprehensive income</b>                               | <b>0.0</b>          | <b>0.0</b>    | <b>0.0</b>            | <b>-11.9</b>    | <b>0.0</b>     | <b>0.0</b>        | <b>0.0</b>       | <b>0.0</b>          | <b>-11.9</b>   |
| <b>Comprehensive income</b>   | <b>0.0</b>          | <b>0.0</b>    | <b>0.0</b>            | <b>-11.9</b>    | <b>0.0</b>     | <b>0.0</b>        | <b>0.0</b>       | <b>790.0</b>        | <b>778.1</b>   |
| <b>Transactions with equity owners:</b>                               |                     |               |                       |                 |                |                   |                  |                     |                |
| Allocation of 2008 profit   |                     |               |                       |                 |                |                   |                  |                     |                |
| - 2008 dividend   |                     |               |                       |                 |                |                   | 118.5            | -316.2              | -197.7         |
| - Retained earnings 2008  |                     |               |                       |                 |                | 19.1              |                  | -19.1               | 0.0            |
| Exercise of stock options   |                     |               |                       |                 |                |                   |                  |                     | 0.0            |
| 2009 interim dividend   |                     |               |                       |                 |                |                   | -140.1           |                     | -140.1         |
| <b>Total transactions with equity owners</b>                          | <b>0.0</b>          | <b>0.0</b>    | <b>0.0</b>            | <b>0.0</b>      | <b>0.0</b>     | <b>19.1</b>       | <b>-21.6</b>     | <b>-335.3</b>       | <b>-337.8</b>  |
| <b>Equity at 31 December 2009</b>                                     | <b>440.2</b>        | <b>88.0</b>   | <b>1.8</b>            | <b>-61.2</b>    | <b>730.1</b>   | <b>619.5</b>      | <b>-140.1</b>    | <b>790.0</b>        | <b>2,468.3</b> |



## Statement of cash flows (\*)

| In millions of euros   | 31 Dec. 2010    | 31 Dec. 2009    |
|--|-----------------|-----------------|
| <b>Profit for the year</b>   | <b>433.7</b>    | <b>790.0</b>    |
| <b>Adjustments for:</b>  |                 |                 |
| Amortisation, depreciation, impairment losses/(reversals of impairment losses) on property, plant and equipment and intangible assets (**) | 310.2           | 272.9           |
| Provisions (including employee-related provisions) and impairment losses   | 58.0            | 114.0           |
| (Gains)/Losses on disposals of property, plant and equipment   | -3.1            | -1.9            |
| Net financial income   | 81.4            | 123.9           |
| Income taxes   | 235.5           | 184.7           |
| <b>Cash flows generated by operating activities, before changes in net working capital</b>   | <b>1,115.7</b>  | <b>1,483.6</b>  |
| Decrease in provisions (including employee-related and tax provisions)   | -48.6           | -72.7           |
| (Increase)/decrease in inventories   | 0.3             | 4.9             |
| (Increase)/decrease in trade receivables and other current assets  | -286.9          | 537.3           |
| Increase/(decrease) in other non-current liabilities   | -6.4            | 9.6             |
| Increase/(decrease) in other non-current assets  | -205.2          | -143.4          |
| (Increase)/decrease in trade payables and other liabilities  | 199.7           | -309.0          |
| Interest income and other financial income received  | 127.4           | 139.4           |
| Interest expense and other financial expense paid  | -215.9          | -227.1          |
| Income taxes paid  | -209.1          | -174.0          |
| <b>Cash flows generated by operating activities [a]</b>  | <b>471.0</b>    | <b>1,248.6</b>  |
| Investments in property, plant and equipment, net of recognised grants   | -1,051.3        | -806.4          |
| Revenue from sale of property, plant and equipment and intangible assets   | 4.4             | 7.4             |
| Investments in intangible assets, net of recognised grants   | -56.8           | -51.0           |
| Intra-group purchases  | -21.2           | 0.0             |
| (Increase)/decrease in investments   | -8.0            | -359.7          |
| <b>Cash flows used in investing activities [b]</b>   | <b>-1,132.9</b> | <b>-1,209.7</b> |
| Increase/(decrease) in share capital   | 0.8             | 0.0             |
| Increase/(decrease) in reserves  | 6.4             | 0.3             |
| Dividends paid   | -400.8          | -337.8          |
| Changes in short- and medium/long-term financial payables and loans (including short-term portions) (***)                                  | 978.7           | 109.5           |
| Change in short-term financial investments   | 500.0           | -500.0          |
| Assets held for sale   | -254.6          | 0.0             |
| <b>Cash flows generated by (used in) financing activities [c]</b>  | <b>830.5</b>    | <b>-728.0</b>   |
| <b>Increase/(decrease) in cash and cash equivalents [a+b+c]</b>  | <b>168.6</b>    | <b>-689.1</b>   |
| Opening cash and cash equivalents  | 0.1             | 689.2           |
| Closing cash and cash equivalents  | 168.7           | 0.1             |

(\*) For comments on the statement of cash flows, please see the section "Notes to the statement of cash flows" in the notes to the financial statements;

(\*\*) net of grants related to assets taken to income statement for the year;

(\*\*\*) net of FVH derivatives.





Notes to the separate financial statements

# A. Accounting policies

## Foreword

Terna S.p.A., which operates in the electrical energy transmission and dispatching sector, is a public limited company headquartered in Viale Egidio Galbani 70, Rome, Italy.

The Directors authorized the publication of these separate financial statements on 31 March 2011.

The separate financial statements as at and for the year ended 31 December 2010 are available upon request at Terna S.p.A.'s offices in Viale Egidio Galbani, 70 Rome and on the website [www.terna.it](http://www.terna.it).

## Compliance with IFRS

The separate financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS), International Accounting Standards (IAS) and the interpretations of the International Financial Reporting Interpretations Committee (IFRIC) and the Standing Interpretations Committee (SIC), endorsed by the European Commission (IFRS-EU) at that date.

These financial statements have also been prepared considering the provisions of Legislative Decree no. 38 of 28 February 2005, the Italian Civil Code and CONSOB Resolutions nos. 15519 (*"Provisions governing financial statements in implementation of art. 9, paragraph 3, of Legislative Decree no. 38/2005"*) and 15520 (*"Amendments to the implementing rules for Legislative Decree no. 58/1998"*), both of 27 July 2006, as well as CONSOB Communication no. DEM/6064293 of 28 July 2006 (*"Disclosure requirements for listed issuers and issuers of financial instruments that are widely held among the public referred to in art. 116 of the Consolidated Law on Financial Intermediation"*).

The separate financial statements have been prepared on a historic cost basis, modified where necessary for certain financial instruments, as well as on a going concern basis. The Company has determined that, despite the challenging economic and financial environment, it does not face material uncertainties (as defined in paragraph 25 of IAS 1) that might cast doubt on its ability to continue as a going concern.

## Basis of presentation

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

In the statement of financial position, assets and liabilities are classified on a "current/non-current" basis, with separate reporting of assets and liabilities held for sale. Current assets, which include cash and cash equivalents, are those held for realisation, sale or consumption in the Group's normal operating cycle. Current liabilities are those expected to be settled in the Group's normal operating cycle or within one year from the reporting date.

The income statement is classified on the basis of the nature of costs. The income statement is now presented as two statements, the first of which (income statement) presents the components of profit or loss for the year; while the second (statement of comprehensive income) starts with the result for the year and then presents the revenue and expense items (including reclassification adjustments) that are recognised in equity rather than profit or loss for the year.

The statement of cash flows has been prepared using the indirect method.

The separate financial statements are accompanied by the Directors' Report for Terna S.p.A. and the Terna Group, which, as from the 2008 financial year, has been prepared as a single document, exercising the option granted under Legislative Decree no. 32 of 2 February 2007, which amended art. 40 (Directors' Report) of Legislative Decree no. 127 of 9 April 1991. 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 recognised at fair value in accordance with IFRS-EU, as indicated in the accounting policies for each caption.

## Rights on the infrastructure

IFRIC 12 - Service concession arrangements came into force on 1 January 2010. IFRIC 12 specifies the accounting treatment of service concession arrangements, not expressly governed by any specific accounting standard, in order to ensure the consistency and comparability of the financial statements of companies that hold concessions for the delivery of public services. More specifically, the interpretation sets out rules for accounting for the infrastructure used to provide the services under concession, for the costs associated with developing and maintaining such infrastructure, and for the revenue generated by the overall provision of the services. IFRIC 12 does not apply to all arrangements. Its scope is limited to service concession arrangements between public bodies and private operators in which the grantor: (1) controls the use of the infrastructure and governs which services are to be provided, the manner in which they have to be provided and the prices of such services and (2) controls any residual interest in the infrastructure at the end of the concession period. The interpretation also applies to infrastructure constructed by or obtained from third parties for the provision of services under the concession, and to existing infrastructure that the grantor makes available to the operator in order to provide such services. It does not apply to infrastructure owned and accounted for as property, plant and equipment by the operator prior to entering into the service concession arrangement.

Assisted by external consultants, Terna has performed a detailed study of the applicability of IFRIC 12 and the effects of its adoption on the financial statements, identifying that this interpretation does not apply to the transmission activities aspect of Terna's concession. In particular, neither the concession nor related legislation envisage the NTG's return to public ownership, either via the payment of an indemnity or otherwise. Accordingly, the public sector does not control, whether as owner or as holder of beneficial interests or other rights, any significant residual interest in the NTG's infrastructure at the end of the concession period.

By contrast, the Ministry is entitled to reclaim the operating assets employed directly in dispatching activities at the end of the concession. As such, the Group considers that IFRIC 12 does apply to its dispatching infrastructure since the relevant criteria apply: the services provided are regulated and control exists over the residual interest. In particular, having regard for the tariff regime that remunerates dispatching activities, the Intangible Asset model envisaged by IFRIC 12 has been applied. Consequently, the property, plant and equipment and intangible assets employed in the dispatching activities, carried out under concession, are classified as "Intangible assets", in the "Infrastructure rights" caption, with application of the original amortisation schedule.

The revenue and costs relating to the investment in dispatching activities are recognised with reference to the contracts concerned on a stage-of-completion basis; revenue recognised during the construction phase is limited to the amount of the internal and external construction costs incurred, considering that the fair value of the construction services is equivalent to the construction cost recognised to third-party contractors plus the internal cost of the technical personnel employed on such construction activities.

By contrast, tariff revenue continues to be recognised in accordance with IAS 18 and borrowing costs continue to be capitalised pursuant to IAS 23R.

As envisaged in IFRIC 12, Terna has adopted the interpretation on a retrospective basis from 1 November 2005, when the TSO line of business was acquired from GRTN, and the provision of dispatching services commenced under concession. The retrospective application of IFRIC 12 has had no effect on equity at 1 January 2009 and 31 December 2009, or on the comprehensive income for 2009 presented for comparative purposes in these separate financial statements at 31 December 2010.

Following the approach described above, the investment carried out during 2009 has therefore been reclassified to the income statement via the separate recognition of construction costs and revenue.

In conclusion, the application of IFRIC 12 to the corresponding information provided has involved the reclassification of intangible assets of property, plant and equipment totalling € 83.2 million at 1 January 2009 and € 85.4 million at 31 December 2009 (including the reclassification of work in progress amounting to € 13.2 million), and the recognition of construction costs and revenue for the six months ended 31 December 2009, of € 29.5 million.

## Use of estimates

The preparation of the statement of financial position and income statement in accordance with the IFRS-EU 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 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 periodically and the effects of any changes are recognised in the income statement for the period, if they relate solely to that period. If changes affect both that period and future periods, the related effects are recognised over time, commencing from the accounting period in which the estimate is revised.

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

### **Employee benefits**

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

### **Provisions for risks and charges**

Accruals to the provisions for contingencies and charges are recognised 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 financial effect of the passage of time is material, accruals are measured by discounting the estimated outflow at a pre-tax discount rate that reflects current market assessments of the time value of money (free risk) and, if applicable, the risks specific to the liability. Any increase in provisions associated with the passage of time is taken to the income statement under "Financial expense".

### **Allowance for impairment accounts**

Trade receivables are initially recognised at fair value net of any impairment losses relating to sums considered non recoverable, which are taken to the specific allowance for impairment. 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 analysed 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 in entities over which Terna has the power to directly or indirectly govern financial and operating policies so as to obtain benefits from their activities. Investments in associates are those in entities 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 is reinstated within the limits of the impairment losses, and the reversal is taken to profit or loss.

In the event that an investee's losses attributable to the shareholders of the Parent exceed that investments' carrying amount, any excess is recognised 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 S.p.A. prepares its financial statements in euros, which is also the functional currency. In these financial statements, all transactions in currencies other than the functional currency are recognised at the exchange rate prevailing on the date of the transaction. Monetary assets and liabilities in currencies other than the functional currency are subsequently adjusted at the exchange rate prevailing at year end. Any exchange rate differences are taken to profit or loss.

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

## Business combinations

The Company books business combinations, in compliance with the updated version of IFRS 3 - Business combinations, endorsed on 3 June 2009 by the European Commission with Regulation no. 495/2009 and which came into force on 1 January 2010. The change in the accounting standard has been applied prospectively and has had no significant effect on earnings per share.

Business combinations are booked using the purchase method on the date of purchase or rather on the date on which control is effectively obtained, defined as the power to determine the financial and managerial policies of an entity in order to obtain benefits from its operations. In assessing the existence of such control, the Company must consider the voting rights that can potentially be exercised.

The new provisions of IFRS 3 require, among other matters, the expensing of costs associated with business combinations, inclusive of settlement costs, and the recognition through profit or loss of any changes in contingent consideration; they also allow full recognition of the goodwill arising from the transaction, including the portion attributable to non-controlling interests (full goodwill method). The standard establishes that the potential price shall be booked at fair value on the date of purchase. If this price is classified as equity, it need not be recalculated and its subsequent repayment must be booked to equity. If not, subsequent changes to the fair value of the potential price are recognised in profit or loss for the year.

The new provisions also change the current criterion for the recognition of step acquisitions, envisaging the recognition through profit or loss of the difference, at the time of acquiring control, between the fair value of the net assets previously held and their carrying amount.

For acquisitions made subsequent to 1 January 2010, the Company measures goodwill on the date of purchase at fair value, increased by any non-controlling interests in the company acquired, including, where the combination takes place in several stages, the fair value of the interest held previously, all deducted from the net amount booked for identifiable assets purchased and identifiable liabilities assumed. When the excess, calculated in this way, is negative, the profit or loss for the year immediately recognises income deriving from a purchase made at favourable prices.

On 3 June 2009, with Regulation 494/2009 issued by the European Commission, the updated version of IAS 27 - Consolidated and separate financial statements was also endorsed. In compliance with the new standard, acquisitions of minority shares are booked as transactions implemented with shareholders, as shareholders and as such these transactions shall not give rise to the recording of goodwill. Adjustments made to non-controlling interests are based on a proportional amount of the net assets of the subsidiary. The revised version of IAS 27 requires, among other matters, that the effects deriving from the acquisition (disposal) of equity investments subsequent to the acquisition of control (without loss of control) be recognised in equity. If the partial disposal of investments held results in the loss of control, joint control or associate status, the new provisions also require that the equity investment retained be measured at fair value, and that this revaluation be included in the capital gain (loss) deriving from the disposal transaction.

The new standard does not apply retrospectively, but only in relation to any business combinations that take place subsequent to the date on which it comes into force.

## Property, plant and equipment

Property, plant and equipment are recognised at historic cost, including costs directly 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 recognised in the provisions for contingencies and charges. Borrowing costs directly attributable to the acquisition, construction or production of an asset that qualify for capitalisation pursuant to IAS 23R are capitalised as part of the cost of the asset. For more information, please see the section "Financial income and expense" below. Costs incurred after purchase are recognised as an increase in the carrying amount of the asset to which they relate if it is probable that the future benefits of that cost will flow to the Company and if the cost can be reliably measured. All other costs are recognised in profit or loss 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 recognised and depreciated separately.

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

Property, plant and equipment is 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 economic life of the asset, which is reviewed annually, with revisions applied on a prospective basis. The depreciation of assets 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 profit or loss through the depreciation of the asset.



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

#### AMORTISATION AND DEPRECIATION RATES

|  |        |
|--|--------|
| Civil and industrial buildings                       | 2.50%  |
| Transmission lines                                   | 2.50%  |
| Transformer stations:                                |        |
| - Electrical machinery                               | 2.38%  |
| - Electrical devices and equipment                   | 3.13%  |
| - Automation and control systems                     | 6.70%  |
| Central systems for remote management and control:   |        |
| - Devices, electrical equipment and ancillary plants | 5.00%  |
| - Electronic calculation equipment                   | 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 leases, through which the Company has acquired substantially all the risks and rewards of ownership, are recognised 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 recognised 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 in full to profit or loss over the term of the lease.

## Intangible assets

Intangible assets, which all have finite useful lives, are recognised at cost, having obtained the approval of the Board of Statutory Auditors, and shown net of accumulated amortisation and any impairment losses, measured as described below. Amortisation begins when the asset becomes available for use and is calculated on a straight-line basis over the estimated useful life of the related asset, which is reviewed annually. Any revisions are applied on a prospective basis.

Intangible assets substantially regard the exclusive concession to carry out electricity transmission and dispatching activities and other intangible assets. In particular, Terna S.p.A. obtained the concession for electricity transmission and dispatching activities in Italy on 1 November 2005 when it acquired the TSO business unit. As established in the Decree issued by the Ministry of Productive Activities on 20 April 2005, this concession runs for twenty-five years, renewable for another 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 S.p.A. This intangible asset was initially recognised at cost, which reflected fair value.

Other intangible assets mainly relate to the following:

- the development and innovation of application software to manage the electricity invoicing process;
- the development and innovation of application software to protect the electrical 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.

Development costs are capitalised by the Company only if all following conditions are met: costs can be reliably estimated and there are technical possibilities and intent to complete the intangible asset so as for it to be available after use; the asset can be used and it is possible to demonstrate that it will generate probable future economic benefits. All other development costs and research expenses are recognised in profit or loss when incurred.

Borrowing costs directly attributable to the acquisition, construction or production of a qualifying asset pursuant to IAS 23R are capitalised as part of the cost of the asset. For more information, please see the section "Financial income and expense" below.

These intangible assets are amortised over their estimated residual useful life, which is 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 evidence 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 at least annually.

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, 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. If the intangible asset does not generate cash inflows that are largely independent, the asset's recoverable amount is calculated as part of the CGU to which it belongs.

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

Impairment losses on CGUs are first taken as a reduction in the carrying amount of any allocated goodwill and then as a reduction in other assets of the CGU on a pro rata basis. Except for goodwill, impairment losses may be reversed up to the recoverable amount 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 recognised and measured at the lower of purchase cost and net estimated realisable value. Cost is calculated as the weighted average cost, including related charges. Net estimated realisable value stands for the estimated price of sale under normal conditions net of completion costs and the estimated costs to sell.

## Contract work in progress

When the profit or loss on a contract can be reliably estimated, the related contract costs and revenue are recognised separately in profit or loss on a percentage of completion basis. Progress is measured based on the work carried out and measured proportionally to the ratio of costs for the works carried out up to reporting date and total cost of the contract (cost-to-cost method). Differences between the value of completed contracts and payments on account received, positive or negative, are recognised under statement of financial position assets or liabilities, considering any impairment losses on the work carried out so as to take into account the risks of customers' refusal to recognise the work performed. Expected contract losses are immediately taken to profit or loss.

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 other than financial derivatives that the Company has the positive intention and ability to hold to maturity are recognised 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 amortised 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 profit or loss for the year. Financial assets are derecognised 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 recognised at fair value and subsequently measured at amortised cost, using the effective interest method, and net of any impairment losses due to sums considered non-recoverable, which are taken to the specific allowance for impairment. Impairment losses are measured on the basis of the present value of estimated future cash flows, discounted at the original 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 monetary items, i.e. amounts that are available on demand or with a very short maturity, subject to an insignificant risk and without collection costs.

### Trade payables

Trade payables are initially recognised at fair value and subsequently stated at amortised cost. If their due date falls under normal commercial terms, they are not discounted.

### Financial liabilities

Financial liabilities other than financial derivatives are initially recognised at the settlement date and measured at fair value, net of directly related transaction costs.

Subsequently, financial liabilities are measured at amortised cost, using the original effective interest method. If the liabilities are covered by fair value hedges, they are adjusted to reflect changes in fair value with respect to the hedged risk.

### Derivative financial instruments

Derivatives are recognised 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 within a range of 80% to 125%, as initially verified and periodically checked. When derivatives cover the risk of changes in the cash flows of the hedged instruments (cash flow hedges), the part of changes in the fair value qualifying as effective is initially taken to equity and subsequently to profit or loss, in line with the effects of the hedged transaction. The portion of the fair value of the hedging instrument that does not qualify as effective is taken to profit or loss.

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

Changes in the fair value of derivatives that do not meet hedge accounting requirements pursuant to the IFRS-EU are recognised in profit or loss.

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

Financial and non-financial contracts (which are not already measured at fair value) are also analysed to identify any embedded derivatives, which must be separated and measured at fair value. This analysis is conducted at the time the entity becomes party to the contract or when the contract is renegotiated in a manner that produces a material change in the original associated cash flows.

The measurement techniques used for derivatives existing at year end did not change with respect to the previous year. Accordingly, the effects of these measurement are in profit or loss and equity are essentially attributable to normal market developments, as well as new derivative contracts signed during the year.

## Employee benefits

The liability in respect of employee benefits payable upon or after termination of employment relates to defined benefit plans (termination benefits, additional month's pay, indemnity for lack of notice, energy discount, ASEM health benefits and other benefits) or other long-term employee benefits (loyalty bonus) and is recognised 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 that employees have accrued at the reporting date. The liability is recognised 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-EU) were recognised in equity. After that date, unrecognised actuarial gains and losses in excess of 10% of the greater of the present value of the defined benefit plan obligation and the fair value of plan assets are taken to profit or loss for the average expected term of service of employees participating in the plan. Otherwise, actuarial gains and losses are not recognised.

## Provisions for risks and charges

Accruals to the provisions for risks and charges are recognised when, at the reporting date, the Company has a legal or constructive obligation towards others as a result of a past event and it is probable that an outflow of resources will be required to settle the obligation and a reliable estimate can be made of the amount of the 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 assessment of the time value of money (free risk) and those risks specific to the liability, if present. Where discounting is used, the increase in the provision due to the passage of time is recognised as an interest expense. If the liability relates to property, plant and equipment (e.g. site disposal and restoration, for example), the provision is recognised as a balancing entry to the asset to which it relates. The expense is recognised in profit or loss through depreciation of the item of property, plant and equipment to which it relates.

Changes in the estimate are recognised through profit or loss for the year in which the change happens, except for those costs expected for dismantling, removal and reclamation, which come as a result of changes in the timing and use of economic resources necessary to extinguish the obligation or attributable to a material change in the discount rate, which are recognised as an increase or reduction of the related assets and recognised in profit or loss through depreciation.

## 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 recognised under personnel expense 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. Such estimate is reviewed where subsequent information indicates that the expected number of instruments representative of capital that will mature differs from the estimate previously carried out, regardless of achievement of the market conditions.

The measurement method used to calculate fair value considers all the characteristics of the options (term, price and conditions etc.), as well as the price of Terna S.p.A. shares at the grant date, the volatility of the stock and the yield curve at the grant date, in line with the term of the plan.

At the vesting date, the estimate is revised through the income statement to recognise the actual amount corresponding to the number of equity instruments that have actually vested, regardless of achievement of the market conditions.

## Grants

Grants received in relation to specific assets whose value is recognised under non-current assets are, for plants operating before 31 December 2002, recognised under other liabilities and taken to profit or loss over the depreciation period of the related assets. From 2003, grants related to assets for new plants that have entered service are recognised as a direct reduction in the value of the related asset.

Grants related to income are expensed in full when the recognition requirements are satisfied.

## Revenue

Revenue is recognised when it is probable that the economic benefits deriving from the operation will be used by the enterprise. Depending on the type of transaction, revenue is recognised on the basis of the following specific criteria:

- revenue from the sale of goods is recognised when the material risks and rewards of ownership of the goods have been transferred to the buyer and their total amount can be reliably determined and collected;
- revenue from services rendered is recognised with reference to the stage of completion of the transaction. If revenue cannot be reliably measured, it is recognised to the extent of recoverable costs;
- revenue accrued during the year in respect of contract work in progress is recognised on the basis of the payments agreed for the progress of works using the cost-to-cost method. In addition to contractual payments, project revenue includes any payments in respect of variations, price revisions and incentives, with the latter recognised where it is probable that they will actually be earned and can be reliably determined. Revenue is also adjusted for any penalties for delays attributable to the Company;
- when the recovery of an amount already recognised in revenue is uncertain, the non-recoverable value or the amount whose recovery is no longer probable is recorded as a cost, with a balancing entry in provisions for risks and charges;
- amounts collected on behalf of third parties, such as the fees paid to non-Terna grid owners, as well as revenue recognised for managing activities related to the balancing of the national electrical system, which do not increase equity, are reported net of the related costs. This presentation method, which reflects the substance of transactions by offsetting revenue with the related costs arising from the “same transaction”, is discussed in full in a specific section of the notes.

## Financial income and expense

Borrowing costs directly attributable to the acquisition, construction or production of an asset that qualifies for capitalisation are capitalised as part of the cost of the asset. The qualifying assets (property, plant and equipment and intangible assets) involved are those that require at least one year before being ready for use. The directly attributable borrowing cost is that which would not have been incurred if the expenditure for the asset had not been incurred.

Where funds are borrowed specifically, costs eligible for capitalisation are the actual costs incurred less any income earned on the temporary investment of such borrowings. Where funds are raised through general borrowing, the eligible amount is determined by applying a capitalisation rate to the expenditure on that asset. The capitalisation rate will be the weighted average of the borrowing costs applicable to the general pool, excluding any specifically borrowed funds. The amount of borrowing costs capitalised during a year shall, in any case, not exceed the amount of borrowing costs incurred during that year.

Capitalisation commences as from the date all the following conditions have been met: (a) expenditures have been incurred for the asset; (b) borrowing costs are being incurred; and (c) activities to prepare the asset for its intended use or sale are in progress.

Capitalisation ceases when the activities necessary to prepare the asset for its intended use or sale are substantially complete.

The average capitalisation rate used for 2009 is 3.12%, while that for 2010 is 2.63%.

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

## Dividends

The dividends of associates are booked when it is established that shareholders have the right to receive payment. This generally coincides with the date of the Meeting Resolution.

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.

## Income taxes

Current income taxes, recognised under “tax liabilities” net of prepayments, or under “tax assets” when there is a net credit balance, are recognised on the basis of estimated taxable income and, in accordance with current legislation, taking account of any applicable exemptions.

Deferred tax assets and liabilities are calculated on the temporary differences between the carrying amounts of assets and liabilities recognised in the separate financial statements and the corresponding amounts recognised for tax purposes, using current tax rates or the rates expected to be in effect when the temporary differences reverse, based on current

rates or those that are substantially approved at the reporting date.

Deferred tax assets are recognised when their recovery is considered probable, i.e. when future taxable income will be available against which the asset can be used. The recoverability of deferred tax assets is reviewed at each year end.

Deferred tax liabilities are recognised in any case if they exist.

Taxes in respect of components recognised directly in equity are also recognised in equity.

## Discontinued operations and non-current assets held for sale

Non-current assets (or disposal groups) whose carrying amount will be recovered principally through a sale rather than through continuing use are classified as held for sale and reported separated from other assets and liabilities in the statement of financial position. Non-current assets (or disposal groups) classified as held for sale are first measured in conformity with the IFRS applicable to each asset and liability and subsequently are measured at the lower of their carrying amount and fair value less costs to sell. The carrying amounts of each asset and liability that are not governed by the measurement rules set out in IFRS 5, but are held for sale, are remeasured on the basis of the applicable IFRS before the fair value less costs to sell is redetermined. The individual assets of the companies classified as held for sale are not depreciated/amortised, whereas financial expense and other expenses attributable to liabilities held for sale continue to be recognised. Any subsequent impairment losses are recognised directly as an adjustment to the carrying amount of the non-current assets (or disposal groups) classified as held for sale through profit or loss. The corresponding statement of financial position values for the previous year are not reclassified. A discontinued operation is a component of an entity that either has been disposed of, or is classified as held for sale, and:

- represents a separate major line of business or geographical area of operations;
- is part of a single co-ordinated plan to dispose of a separate major line of business or geographical area of operations; or
- is an operation acquired exclusively with a view to resale.

## New standards

### International Financial Reporting Standards entering into force as from 1 January 2010

The following international financial reporting standards and related interpretations took effect from 1 January 2010:

#### IFRS 3 - Business Combinations (revised in 2007)

As from 1 January 2010, the Company books business combinations in compliance with the updated version of IFRS 3 - Business combinations, endorsed on 3 June 2009 by the European Commission with Regulation no. 495/2009. The change in the accounting standard has been applied prospectively and has had no significant effect on earnings per share.

On 3 June 2009, with Regulation 494/2009 issued by the European Commission, the updated version of IAS 27 - Consolidated and separate financial statements was also endorsed.

The new standard does not apply retrospectively, but only in relation to any business combinations that take place subsequent to the date on which it comes into force. The change in the accounting standard has been applied to all minority investments prospectively, with no significant effect on the earnings per share.

This standard has not had a significant impact on the separate financial statements at 31 December 2011.

#### IFRIC 12 - Service Concession Arrangements

As previously specified, on 1 January 2010, IFRIC 12 - Service concession arrangements became effective. This interpretation has been applied for the first time to the Terna Group's interim consolidated financial statements at 31 March 2010 and in these separate financial statements in relation to the only assets related to the dispatching concession activities of the Company.

Further details about the application of IFRIC 12 and its effects on the information presented for comparative purposes are presented in the "Compliance with IAS/IFRS and basis of presentation section of these separate financial statements.

#### IFRIC 18 - Transfers of Assets from Customers

Endorsed by Regulation 1164/2009, this interpretation applied on a prospective basis to accounting periods commencing after 31 October 2009, provides clarification and guidance about the accounting for items of property, plant and equipment received from customers, or cash received from customers for the acquisition or construction of items of property, plant and equipment in order to connect them. In particular, this interpretation envisages the following accounting treatment in the financial statements of entities that receive property, plant and equipment, or cash for their construction, from customers in order to connect them to a network and/or to guarantee their on going access to a supply of goods or services (e.g. electricity, gas, water etc.):



- the asset received is recognised at fair value in accordance with the provisions of IAS 16 governing the exchange of dissimilar assets with the consequent recognition of revenue when the service is performed;
- specific accounting rules apply if the customer gives the entity an amount of cash sufficient to purchase the item of property, plant and equipment.

This standard has altered the way NTG connections are booked on the Company's financial statements, with no significant effect on the financial position and results.

#### **Amendment of IAS 39 - Financial Instruments - Recognition and Measurement: eligible hedged items**

This amendment provides guidance on two aspects of hedge accounting: the identification of inflation as the hedged risk, or a part of it, and hedging by the use of options.

This standard has not had any impact on the financial statements at 31 December 2010.

#### **Improvements to the IFRS (published in 2009)**

The 2009 version of the document contains minor amendments to previously published standards. These amendments were endorsed during the first quarter of 2010 and apply immediately; they have not had any impact on the financial statements at 31 December 2010.

#### **Practice Statement for the Directors' Report**

This came into force on 8 December 2010 at the same time as it was published by IFRS. The Practice Statement for the Directors' Report provides a non-binding framework for the presentation of the Directors' Report for financial statements prepared in compliance with the IFRS.

#### **Other amendments and interpretations of standards**

The following amendments and interpretations, governing circumstances currently not relevant to the financial statements of the Company, also came in 2010:

- IFRIC 9 - Embedded derivatives;
- amendment to IAS 39 - Reclassification of financial assets: application date;
- IFRIC 15 - Agreements for the construction of real estate;
- IFRIC 16 - Hedges of a net investment in a foreign operation;
- IFRIC 17 - Distributions of non-cash assets to owners;
- IFRS 1 Revised - First-time Adoption of IFRS;
- amendment of IAS 32 - Financial instruments - Presentation: classification of option rights (or warrants);
- revisions to IFRS 1 - Additional exemptions for entities adopting IFRS for the first time;
- revision of IFRS 1 - Limited exemptions from comparative established by IFRS for new consumers;
- amendment of IFRS 2 - Group cash-settled share-based payment transactions. The amendment clarifies the booking of transactions with share-based payments settled in cash within a group (repeals IFRIC 8 and IFRIC 11).

The above amendments and interpretations have not had any impact on the financial statements at 31 December 2010.

#### **International financial reporting standards endorsed but not yet in force**

As of the date on which these financial statements were prepared, the European Commission had endorsed the following amendments to the international accounting standards:

#### **Amendment of IAS 24 - Related Party Disclosures**

Issued on 4 November 2009, this amendment simplifies the related party disclosures to be made by entities subject to control, joint control or significant influence by a governmental body, and eliminates certain difficulties in applying the current definition of related parties. The standard comes into force on 1 January 2011.

#### **Improvements to the IFRS (published in 2010)**

The 2010 version of the document contains minor amendments to previously published standards. This group of changes was endorsed on 18 February 2011 and shall come into force as of 1 January 2011.

The following standards and interpretations have also been endorsed, governing circumstances currently not relevant to the financial statements of the Company:

- amendment of IAS 32 - Financial instruments - Presentation: classification of option rights (or warrants), which comes into force on 1 January 2011;
- amendment to IFRIC 14 - Prepayment of a minimum funding requirement;
- IFRIC 19 - Extinguishing financial liabilities.



### **International financial reporting standards not yet endorsed**

For amendments, new standards and interpretations that have not yet been endorsed by the EU, but which address issues that affect or could affect on the separate financial statements, the Company is assessing the possible impact of their application on its financial statements, taking account of the date on which they take effect. This assessment covers the standards and interpretations listed below.

#### **IFRS 9 - Financial Instruments**

On 12 November 2009 the IASB published IFRS 9 - Financial instruments on the classification and measurement of financial assets, which will take effect as from 1 January 2013. This publication is the first part of a project to replace IAS 39. In a difference from the exposure draft published last July, the scope of the standard does not include financial liabilities, as the IASB, partly in reaction to comments on the exposure draft, decided to devote further study to issues concerning the including of own credit risk in the measurement of the fair value of financial liabilities. Finally, the process of endorsing IFRS 9 is currently suspended in the European Union. Accordingly, the standard is not applicable for European companies pending the European Commission's full assessment of the entire IAS 39 replacement project.

#### **Amendment to IFRS 7 - Financial Instruments**

Issued on 7 October 2010, the amendment has the objective of integrating financial statements in order to provide more information relative to the transfer of financial assets for which part of the risk is not completely sold and the effect of such transactions on the financial position. This amendment should also increase comparability of recognition of transfers of financial assets between the IFRS and US GAAP financial statements.

#### **Amendment to IAS 12 - Deferred tax: recovery of underlying assets**

The amendment applies to all entities applying IAS 40 - Investment property using the fair value method and to those with assets recorded amongst property, plant and equipment, which are not depreciated and which are recorded with the revaluation model established by IAS 16. At present, therefore, the amendment does not govern situations current seen on our financial statements.

#### **Amendment to IFRS 1 - Severe hyperinflation and removal of fixed dates for first-time adopters**

Two amendments have been issued to IFRS 1: the first replaces the references to a fixed transaction date of 1 January 2004, "as date of transfer to IFRS", thereby eliminating the need for companies adopting the IFRS for the first time to repeat eliminations that took place prior to the date on which the move was made to IFRS. The second amendment provides indications on how an entity has to present the financial statements in compliance with the IFRS, after a period in which a party was not able to comply with the IFRS as its functional currency had been subject to severe hyperinflation.

## B. Operating segments

Consistent with the provisions of IFRS 8 - Operating segments concerning companies that publish the consolidated financial statements of a parent in the same document as the financial statements of that parent, operating segment disclosures are provided for the consolidated financial statements only. Accordingly, please see the analogous section of the notes to the consolidated financial statements of the Terna Group.

## C. Notes to the income statement

### Revenue

#### 1. Revenue from sales and services – € 1,459.1 million

The table below details “Revenue from sales and services” for 2010 and 2009:

| In millions of euros                              | 2010           | 2009           | Change       |
|---|----------------|----------------|--------------|
| Grid transmission fees                            | 1,175.0        | 1,087.7        | 87.3         |
| Adjustments for prior year grid transmission fees | -2.0           | 0.2            | -2.2         |
| Other energy revenue                              | 169.8          | 121.0          | 48.8         |
| Other revenue from sales and services             | 116.3          | 73.8           | 42.5         |
| <b>Total</b>                                      | <b>1,459.1</b> | <b>1,282.7</b> | <b>176.4</b> |

#### Grid transmission fees

This caption reports revenue from the Company’s core business, comprising fees paid to it for use of the National Transmission Grid.

The item amounted to € 1,173.0 million in 2010, an increase of € 85.1 million on 2009, attributable to:

- effects of AEEG Resolution 203/09, which revised the tariffs for 2010 (+€ 55.0 million);
- an incentive on remuneration of investments in strategic transmission infrastructures (ARG/elt 87/10 Resolution – +€ 16.8 million);
- increased grid transmission fees related to the Defence plan (+€ 15.5 million);
- negative impact for past net grid transmission fee balances (-€ 2.2 million).

#### Other energy revenue

This caption comprises the fees paid to the Company by electricity companies for dispatching services (DIS component, € 131.4 million), together with the revenue from the construction and development of dispatching infrastructure recognised pursuant to IFRIC 12 (€ 38.3 million); please note that, as specified in section “A. Accounting policies”, such revenue corresponds to the costs incurred during the same period to purchase raw materials and consumables, services and staff which are included in operating costs.

The increase with respect to 2009 - equal to € 48.8 million - reflects the revenue from increased investments during the year in dispatching infrastructures (€ 8.8 million) and, in particular, the economic effects linked to the DIS component and due to:

- the effects of AEEG Resolution 213/09 which redefined - for the period 2010-2012 - the remuneration mechanism that gives Terna incentives to procure resources from the dispatching service market (€ 77.0 million; +€ 37.0 million compared with incentives of € 40.0 million recognised in 2009 on the basis of AEEG 206/08 Resolution); more specifically, the result achieved in 2010 has been stated at fair value in view of the three-year nature of the incentives mechanism; the application of AEEG Resolution no. 204/09 concerning rates adjustment for the DIS component in 2010 (+€ 3.5 million);
- regulating providing incentives for the quality of the transmission service (AEEG Resolution 169/08 and subsequent amendments – +€ 4.4 million);
- redefinition of the compensation for grouping of measures (ARG/elt Resolution 129/10 – -€ 5.1 million).

### Other energy items - pass-through revenue/costs

This caption includes revenue and costs of a “pass-through” nature for the Group (whose balance is therefore nil). They arise in respect of daily purchases and sales with operators on the electricity market to carry out transmission and dispatching activities. To that end, the measurements at each point of input and withdrawal are taken and the differences from the energy market schedules are calculated. These differences (imbalances) are measured using algorithms established by the regulatory framework. The net charge resulting from the measurement of these imbalances and of the buying and selling transactions executed by Terna on the Ancillary Services Markets are billed on a pro rata basis to each consumer with the uplift fee.

It also includes the remuneration paid by Terna to the other owners of the grid.

The components of these transactions are detailed below.

| In millions of euros  | 2010           | 2009           | Change        |
|---|----------------|----------------|---------------|
| <b>Revenue - Power Exchange:</b>  |                |                |               |
| - foreign market – exports  | 1.1            | 4.4            | -3.3          |
| - sale of energy on the Day Ahead Market, Adjustment Market, Ancillary Services Market and others | 653.4          | 813.5          | -160.1        |
| - unbalancing and other minor items   | 928.3          | 1,597.4        | -669.1        |
| - ancillary service resources procurement   | 1,152.5        | 980.9          | 171.6         |
| - congestion rent – rights for use of transportation capacity (RTC), Res. no. 288/06              | 821.4          | 733.4          | 88.0          |
| - other items – Power Exchange  | 140.4          | 311.5          | -171.1        |
| - interconnector/shipper  | 125.6          | -              | 125.6         |
| <b>Total revenue - Power Exchange</b>   | <b>3,822.7</b> | <b>4,441.1</b> | <b>-618.4</b> |
| Revenue under Res. nos. 168/04 - 237/04 and others  | 817.3          | 613.5          | 203.8         |
| Other items (CBT and other)   | 171.4          | 47.3           | 124.1         |
| Revenue from grid transmission fees of other owners and GRTN share CIP/6                          | 157.7          | 116.5          | 41.2          |
| <b>Total revenue from outside the Power Exchange</b>  | <b>1,146.4</b> | <b>777.3</b>   | <b>369.1</b>  |
| <b>Total pass-through energy revenue</b>  | <b>4,969.1</b> | <b>5,218.4</b> | <b>-249.3</b> |
| <b>Energy purchases:</b>  |                |                |               |
| - on Day Ahead Market and Adjustment Market   | 160.3          | 9.5            | 150.8         |
| - to provide the dispatching service  | 1,664.8        | 2,431.6        | -766.8        |
| - for unbalancing   | 902.7          | 1,373.4        | -470.7        |
| - on the foreign market - imports   | 0.5            | 0.1            | 0.4           |
| - Electricity Market Operator fees  | 2.7            | 2.7            | -             |
| - congestion rent – RTC, res. no. 288/06  | 513.9          | 559.3          | -45.4         |
| - other items – Power Exchange  | 72.7           | 64.5           | 8.2           |
| - interconnector/shipper  | 505.1          | -              | 505.1         |
| <b>Total costs – Power Exchange</b>   | <b>3,822.7</b> | <b>4,441.1</b> | <b>-618.4</b> |
| Purchase of electricity market related services   | 817.3          | 613.5          | 203.8         |
| Other items (CBT and other)   | 171.4          | 47.3           | 124.1         |
| Fees to be paid to NTG owners, GRTN and other   | 157.7          | 116.5          | 41.2          |
| <b>Total services and fees</b>  | <b>1,146.4</b> | <b>777.3</b>   | <b>369.1</b>  |
| <b>Total pass-through energy costs</b>  | <b>4,969.1</b> | <b>5,218.4</b> | <b>-249.3</b> |

### Other revenue from sales and services

Other revenue from sales and services amounted to € 116.3 million and mainly relates to revenue from a variety of specialised high- and very-high-voltage services that the Company provides to third-party customers (€ 46.2 million) and the subsidiary TELAT (€ 50.9 million). The amount reflects revenue from:

- the operation, maintenance and development of the optical fibre owned by the Wind Group hosted on plants (safety cables) of the Company (€ 2.2 million);
- NTG connection services, primarily including plants for the production of energy from renewable sources (€ 4.9 million);

- the contribution due to the Company for coverage of cost incurred for electricity discounts to its employees (€ 1.6 million);
- management fee services provided to the subsidiaries TELAT (€ 7.4 million), SunTergid (€ 1.3 million) and RTR, which is being sold off (€ 1.8 million).

The increase of € 42.5 million is essentially due to work orders for the realization/expansion of electrical stations and the relative connections to the NTG's requested by third parties (+€ 16.8 million) in addition to maintenance, development and rationalisation of AT plants of the subsidiary TELAT (+€ 24.0 million, also considering the services provided to Enel Distribuzione in the 1st quarter of 2009 on these same plants, prior to the acquisition of the subsidiary by Terna).

## 2. Other revenue and income – € 46.0 million

Other revenue and income totalled € 46.0 million and break down as follows:

| In millions of euros                      | 2010        | 2009        | Change     |
|---|-------------|-------------|------------|
| Rental income                             | 17.8        | 17.9        | -0.1       |
| Sundry grants                             | 8.6         | 9.3         | -0.7       |
| Insurance settlements for losses          | 5.8         | 3.3         | 2.5        |
| Gains on the disposal of plant components | 3.4         | 4.8         | -1.4       |
| Prior period income                       | 6.6         | 4.1         | 2.5        |
| Sales to third parties                    | 2.5         | 1.0         | 1.5        |
| Other revenue                             | 1.3         | 1.6         | -0.3       |
| <b>Total</b>                              | <b>46.0</b> | <b>42.0</b> | <b>4.0</b> |

Rental income mainly refers to rent from the Wind Group for the housing of optical fibre on the grid (€ 13.2 million) and Enel Distribuzione's use of the Company's infrastructure for power line communication (€ 2.0 million); it also includes rents from the leasing of land to the subsidiaries. This land will be used for the construction of photovoltaic plants (€ 0.7 million).

The increase in "other revenue and income" (€ 4.0 million) is essentially attributable to increased insurance indemnities (€ 2.5 million), damages to plants which primarily occurred in the previous year and increased contingent assets (€ 2.5 million), which were essentially due to the net issue of past accruals to the allowance for impairment following the collection of the relative items (€ 1.9 million). It also includes the increase in revenue from sales to third parties (€ 1.5 million), mainly with reference to scrap, to a large extent offset by the negative change (€ 1.4 million) due to the greater capital gains recorded in 2009 following the sale of a building in the operative area of Padua.

## Operating expenses

### 3. Raw materials and consumables – € 36.7 million

The item totalled € 36.7 million. It comprises costs incurred for the purchase of sundry materials and equipment used in the operation and maintenance of plants. The increase of € 16.8 million on last year (€ 19.9 million as of 31 December 2009) is mainly due to the greater values recorded in application of IFRIC 12 (€ 7.1 million) and to materials used for maintenance and reorganization of plants by the subsidiary TELAT.

### 4. Services – € 166.5 million

The table below details revenue from services for 2010 and 2009:

| In millions of euros              | 2010         | 2009         | Change       |
|-----------------------------------|--------------|--------------|--------------|
| Tenders on plants                 | 52.0         | 41.1         | 10.9         |
| Maintenance and sundry services   | 62.1         | 60.8         | 1.3          |
| Insurance                         | 5.8          | 5.7          | 0.1          |
| Remote transmission and telephone | 14.2         | 12.6         | 1.6          |
| IT services                       | 21.3         | 14.4         | 6.9          |
| Leases and rentals                | 11.1         | 13.4         | -2.3         |
| <b>Total</b>                      | <b>166.5</b> | <b>148.0</b> | <b>18.55</b> |



The item “Services” refers to costs for tenders and services for routine maintenance operations and plant maintenance and expenditures for general services (a total of € 114.1 million). It also includes costs for IT services (€ 21.3 million) remote transmission and telephone services (€ 14.2 million), leases and rentals (€ 11.1 million), and insurance (€ 5.8 million). The increase (€ 18.5 million) is primarily due to the increased computer services (+€ 6.9 million, of which +€ 6.2 million for greater costs booked pursuant to IFRIC 12) and to increased technical services and tenders (+€ 10.9 million), mainly on plants pertaining to the subsidiary TELAT.

Fees paid to the Statutory Auditors of Terna S.p.A. are detailed in the following table. The table has been prepared on the basis of the term of office of the position on an accruals basis.

| Surname and Name                     | Position                                    | Term of office    | Expiry of term                        | Remuneration   | Total          |
|--------------------------------------|---|-------------------|---------------------------------------|----------------|----------------|
| Guarna Luca Aurelio                  | Chairman of the Board of Statutory Auditors | Jan. 10 - Dec. 10 | Approval of 2010 financial statements | 55,000         | 55,000         |
| Cosconati Marcello <sup>(*)</sup>    | Statutory Auditor                           | Jan. 10 - Dec. 10 | Approval of 2010 financial statements | 45,000         | 45,000         |
| Pozza Lorenzo                        | Statutory Auditor                           | Jan. 10 - Dec. 10 | Approval of 2010 financial statements | 45,000         | 45,000         |
| <b>Total Statutory Auditors fees</b> |   |                   |                                       | <b>145,000</b> | <b>145,000</b> |

(\*) Fees for the position were paid to Cassa Depositi e Prestiti.

## 5. Personnel expense – € 214.8 million

Personnel expense breaks down as follows:

| In millions of euros   | 2010         | 2009         | Change      |
|--|--------------|--------------|-------------|
| Wages, salaries and other short-term employee benefits                           | 256.0        | 248.9        | 7.1         |
| Termination indemnities, electricity discount and other post-employment benefits | 15.8         | 15.5         | 0.3         |
| Reversal of provision for electricity discount                                   | -            | -26.8        | 26.8        |
| Early retirement incentives  | 4.6          | 6.5          | -1.9        |
| <b>Personnel expense, gross</b>  | <b>276.4</b> | <b>244.1</b> | <b>32.3</b> |
| Personnel expense, capitalised   | -61.6        | -57.9        | -3.7        |
| <b>Total</b>   | <b>214.8</b> | <b>186.2</b> | <b>28.6</b> |

This caption includes the cost of wages and salaries, social security contributions and other costs incurred by the Company for voluntary early retirement 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 electricity sector.

The € 28.6 million increase in this item is mainly due to the release in 2009 of the provision for electricity discount (€ 26.8 million), for the recalculation, with Enel Servizio Elettrico of the number of retired recipients of this benefit. It also reflects the combined effect of:

- an increase in the cost of wages, salaries and other short-term benefits (€ 7.1 million), mainly as a result of the increase in personnel expense per resource, partly offset by the reduction in charges in early-requirement incentives (€ 1.9 million);
- an increase in capitalised personnel expense (€ 3.7 million) as a result of increased capital expenditure during the year.

The fees paid to the Directors of Terna S.p.A. are summarised in the following table. The table has been prepared on the basis of the term of office of the position on an accruals basis.

| Surname Name                 | Position          | Term of office     | Expiry of term                        | Remuneration     | Bonus and other incentives (***) | Other compensation (****) | Other compensation (*****) | Total            |
|------------------------------|-------------------|--------------------|---------------------------------------|------------------|----------------------------------|---------------------------|----------------------------|------------------|
| Roth Luigi                   | Chairman/Director | Jan. 10<br>Dec. 10 | Approval of 2010 financial statements | 600,000          | 150,000                          |                           | 100,000                    | 850,000          |
| Cattaneo Flavio              | CEO               | Jan. 10<br>Dec. 10 | Approval of 2010 financial statements | 200,000          | 1,200,000                        | 1,000,000                 |                            | 2,400,000        |
| Cannarsa Cristiano (*)       | Director          | Jan. 10<br>Dec. 10 | Approval of 2010 financial statements | 25,000           |                                  |                           |                            | 25,000           |
| Dal Pino Paolo               | Director          | Jan. 10<br>Dec. 10 | Approval of 2010 financial statements | 125,000          |                                  |                           |                            | 125,000          |
| Del Fante Matteo (*)         | Director          | Jan. 10<br>Dec. 10 | Approval of 2010 financial statements | 75,000           |                                  |                           |                            | 75,000           |
| Machetti Claudio (**)        | Director          | Jan. 10<br>Dec. 10 | Approval of 2010 financial statements | 25,000           |                                  |                           |                            | 25,000           |
| Machì Salvatore              | Director          | Jan. 10<br>Dec. 10 | Approval of 2010 financial statements | 135,000          |                                  |                           |                            | 135,000          |
| Polo Michele                 | Director          | Jan. 10<br>Dec. 10 | Approval of 2010 financial statements | 75,000           |                                  |                           |                            | 75,000           |
| Rispoli Vittorio             | Director          | Jan. 10<br>Dec. 10 | Approval of 2010 financial statements | 85,000           |                                  |                           |                            | 85,000           |
| <b>Total Directors' fees</b> |                   |                    |                                       | <b>1,345,000</b> | <b>1,350,000</b>                 | <b>1,000,000</b>          | <b>100,000</b>             | <b>3,795,000</b> |

(\*) Fees for the position were paid to Cassa Depositi e Prestiti;

(\*\*) fees for the position were paid to Enel S.p.A.;

(\*\*\*) this amount refers to the variable portion of fees and compensation relative to the year 2010. It also states that the CEO Flavio Cattaneo there is a way-out of about € 7 million;

(\*\*\*\*) this amount refers to executive compensation;

(\*\*\*\*\*) the amount regards compensation for position as Chairman of the Board of Directors of TELAT from 1 January 2010 to 31 December 2010.

The following table shows the number of employees by category at year end and the average number for the year:

|                     | Average number |              | Final number |              |
|---------------------|----------------|--------------|--------------|--------------|
|                     | 2010           | 2009         | 31 Dec. 2010 | 31 Dec. 2009 |
| Senior management   | 64             | 67           | 59           | 65           |
| Junior management   | 495            | 485          | 502          | 488          |
| Office staff        | 1,897          | 1,908        | 1,890        | 1,874        |
| Blue-collar workers | 1,030          | 1,058        | 1,017        | 1,020        |
| <b>Total</b>        | <b>3,486</b>   | <b>3,518</b> | <b>3,468</b> | <b>3,447</b> |

The net change in the average number of employees on the end of 2009 was an increase of -32.

Reference should be made to section "23. Employee benefits" 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. Amortisation, depreciation and impairment losses – € 318.8 million

These relate to accruals during the year calculated on the basis of amortisation and depreciation rates that reflect the useful lives of the Company's plant, property and equipment and intangible assets.

The composition of and changes in the item during the year are reported in the following table:

| In millions of euros  | 2010         | 2009         | Change      |
|---|--------------|--------------|-------------|
| Amortisation on intangible fixed assets                           | 44.4         | 39.4         | 5.0         |
| - of which: Infrastructure rights                                 | 23.7         | 22.7         | 1.0         |
| Depreciation of property, plant and equipment                     | 274.4        | 240.0        | 34.4        |
| Impairment of property, plant and equipment and intangible assets | -            | 2.8          | -2.8        |
| Impairment of trade receivables                                   | -            | 14.1         | -14.1       |
| <b>Total</b>  | <b>318.8</b> | <b>296.3</b> | <b>22.5</b> |



The increase of € 22.5 million on 2009 is due to the additional amortisation (totalling € 39.4 million), mainly due to the start-up during the year of new plants (in particular pole 2 of SA.PE.I.) and of intangible assets of the Company. The change is also due to the impairment losses on property, plants and equipment and intangible assets (€ 2.8 million) and accruals to the allowance for impairment (€ 14.1 million) recorded last year.

## 7. Other operating expenses – € 17.8 million

Other operating expenses break down as follows:

| In millions of euros                     | 2010        | 2009        | Change      |
|--|-------------|-------------|-------------|
| Provisions for risks and charges         | 1.8         | 0.8         | 1.0         |
| Power failure charges                    | 2.0         | 2.8         | -0.8        |
| Indirect and local taxes and duties      | 5.6         | 4.6         | 1.0         |
| Prior period expense                     | 2.4         | 2.3         | 0.1         |
| Losses on the disposal/closure of plants | 0.3         | 2.9         | -2.6        |
| Other operating costs                    | 5.7         | 6.5         | -0.8        |
| <b>Total</b>                             | <b>17.8</b> | <b>19.9</b> | <b>-2.1</b> |

The item records a decrease of € 2.1 million on last year, generally due to the increased capital losses for disposals/sales of parts of primary plants (-€ 2.6 million) and the greater operating expenses involved in the construction and development of dispatching infrastructures (pursuant to IFRIC 12 -€ 1.9 million) recorded in 2009. The change is also due to the 2010 allocations made to the Provision for risks, both for charges to be paid to distributing companies for power failures of the transformation plants linked to the NTG (pursuant to Resolution 341/07 – +€ 0.7 million) and for the sharing of indemnities due to final users (+€ 0.2 million) in addition to greater taxes, duties and local charges (+€ 1.0 million), mainly referred to TARSU (€ 0.8 million).

## Financial income and expense

## 8. Net financial expense – -€ 87.7 million

This caption is analysed below:

| In millions of euros   | 2010          | 2009          | Change      |
|--|---------------|---------------|-------------|
| <b>Financial income</b>  |               |               |             |
| Financial income from parents  | -             | 3.1           | -3.1        |
| Interest income from Terna Participações   | -             | 14.3          | -14.3       |
| Financial income from subsidiaries   | 18.0          | 2.2           | 15.8        |
| Interest income and other financial income   | 9.0           | 10.6          | -1.6        |
| Debt adjustment (bonds) and related hedges   | 2.2           | 1.2           | 1.0         |
| <b>Total income</b>  | <b>29.2</b>   | <b>31.4</b>   | <b>-2.2</b> |
| <b>Financial expense</b>   |               |               |             |
| Interest expense on medium/long-term loans and related hedges                        | -121.1        | -147.6        | 26.5        |
| Exchange rate differences and related non-hedge-accounting exchange-rate derivatives | -5.6          | -25.2         | 19.6        |
| Interest expense on short-term loans and other financial expense                     | -0.7          | -11.9         | 11.2        |
| Discounting of post-employment benefits and other personnel-related provisions       | -4.9          | -5.7          | 0.8         |
| Financial charges from Parent  | -1.3          | -1.2          | -0.1        |
| Financial expense to subsidiaries  | -             | -0.1          | 0.1         |
| Capitalised borrowing costs  | 17.4          | 11.2          | 6.2         |
| Impairment of investments in JV  | -0.7          | -             | -0.7        |
| <b>Total expense</b>   | <b>-116.9</b> | <b>-180.5</b> | <b>63.6</b> |
| <b>Total</b>   | <b>-87.7</b>  | <b>-149.1</b> | <b>61.4</b> |

Net financial expense amounted to € 87.7 million for the period, comprising € 116.9 million in financial expense and € 29.2 million in financial income. The decrease of € 61.4 million with respect to last year is the net result of the following main factors:

- financial proceeds which accrued in 2009 with respect to CDP bonds underwritten by Terna and reimbursed in the same year (-€ 3.1 million);
- interest income accrued during 2009 on the financing between Terna and Terna Participações (-€ 14.3 million);
- greater net financial proceeds from subsidiaries (+€ 15.9 million) mainly relating to the loan supplied to the subsidiary TELAT (+€ 15.6 million);
- decreased financial proceeds (-€ 1.6 million) which were primarily attributable to the combined effect of:
  - lesser liquidity invested and lower interest rates (-€ 5.8 million);
  - greater default interest charged in 2009 for the late payment of receivables in respect of dispatching activities (-€ 1.8 million);
  - booking of net uplift proceeds in 2010 (+€ 2.3 million) compared to the negative balance (€ 11.8 million, booked under financial expenses) of the previous year;
  - increased receivable interest accrued on short-term securities issued by UBS and MPS (+€ 4.0 million);
- the net economic benefit deriving from the fair value adjustment of bonds and the related hedges (€ 1.0 million);
- decreased financial expense in respect of medium/long-term debt (€ 26.5 million) due to the reduction in interest rates, partially offset by the increase in borrowing;
- the positive impact (€ 19.6 million) mainly of the 2009 reporting of charges on hedges not qualifying for hedge accounting to mitigate the risk associated with the volatility of exchange rates with respect to dividends and intercompany loan payments from Terna Participações;
- reductions in interest expense on short-term loans and in other financial charges (€ 11.2 million) due almost entirely to the uplift charges recognised in 2009;
- lower financial expense deriving from the discounting of employee benefits (€ 0.8 million);
- increased capitalised financial expense (€ 6.2 million) due to greater capital expenditure during the year;
- impairment of the investment in the company ELMED Études (€ 0.7 million) following the difficult political situation in Tunisia, which is currently making it difficult to recover the investment.

## 9. Income taxes – € 230.5 million

Income taxes for the year amount to € 230.5 million.

The following table reports changes in taxes with respect to 2009:

| In millions of euros                                       | 2010         | 2009         | Change      |
|--|--------------|--------------|-------------|
| <b>Income taxes of the year</b>                            |              |              |             |
| Current taxes:   |              |              |             |
| - IRES   | 217.7        | 163.9        | 53.8        |
| - IRAP   | 55.0         | 50.7         | 4.3         |
| <b>Total current taxes</b>                                 | <b>272.7</b> | <b>214.6</b> | <b>58.1</b> |
| New temporary differences:                                 |              |              |             |
| - deferred tax assets                                      | -12.2        | -13.8        | 1.6         |
| - deferred tax liabilities                                 | 0.0          | 0.0          | 0.0         |
| Reversal of temporary differences:                         |              |              |             |
| - deferred tax assets                                      | 11.1         | 16.7         | -5.6        |
| - deferred tax liabilities                                 | -36.1        | -32.8        | -3.3        |
| <b>Total change in deferred tax assets and liabilities</b> | <b>-37.2</b> | <b>-29.9</b> | <b>-7.3</b> |
| Adjustment of prior-year taxes                             | -5.0         | -5.2         | 0.2         |
| <b>Total</b>   | <b>230.5</b> | <b>179.5</b> | <b>51.0</b> |

## Current taxes

Current taxes increased by € 58.1 million on the previous year, essentially due to higher taxable income.

## Deferred tax assets and liabilities

Deferred tax assets and liabilities (-€ 37.2 million) record a net increase of € 7.3 million on 2009. This difference is due to the decreased set-offs for advance taxes (-€ 4.0 million) which were primarily due to bookings, in 2009, for both the provisions for energy discounts following the previously mentioned agreement with Enel Servizio Elettrico (-€ 7.4 million) and the allowance for impairment losses (+€ 2.2 million), in addition to the lesser net allocations made to the other provisions for employee benefits (+€ 0.9 million).

The greater use of deferred tax liabilities (-€ 3.3 million) mainly refers to previous allocations made for accelerated depreciation (-€ 3.6 million).

## Adjustment of prior-year taxes

Adjustments to taxes for previous years, amounting to -€ 5.0 million, mainly refer to the greater current tax paid in previous years.

The effective rate of income tax (which totalled € 230.5 million) on taxable income came to 34.8% (equal to 35.5%, without taking into account adjustments from previous years), down from 35.5% in 2009 (equal to 36.6%, without taking into account adjustments from previous years).

The effective tax rate is higher than the theoretical rate (32.6%), essentially due to the distorting effect of the inclusion of personnel expense in taxable income for the purposes of IRAP (regional business tax).

For a clearer presentation of the differences between the theoretical and actual tax rates, the table below reconciles the theoretical tax rate with the effective tax rate for the year:

| In millions of euros   | Taxable income | Tax          | % Change     |
|--|----------------|--------------|--------------|
| Profit before taxes  | 662.8          |              |              |
| IRES - theoretical tax charge (27.50%)   |                | 182.3        |              |
| IRAP - theoretical tax charge (4.51% on operating profit of € 750.5 million)   |                | 33.8         |              |
| <b>Total</b>   |                | <b>216,1</b> |              |
| <b>Theoretical tax rate</b>  |                |              | <b>32.6%</b> |
| <b>Permanent IRES differences</b>  |                |              |              |
| Employee benefits  |                | 1.4          | 0.2%         |
| Exchange rate differences  |                | 1.5          | 0.2%         |
| Contingencies and non-deductible taxes   |                | 1.5          | 0.2%         |
| Other increases/decreases  |                | 5.5          | 0.9%         |
| IRAP - art. 6 Law 28 January 2009  |                | -1.3         | -0.2%        |
| Release of goodwill pursuant to Law Decree 185/2008                            |                | -1.4         | -0.2%        |
| <b>Permanent IRAP differences</b>  |                |              |              |
| Personnel expense  |                | 12.2         | 1.8%         |
| Other increases/decreases  |                | 0.2          | 0.0%         |
| Release of goodwill pursuant to Law Decree 185/2008                            |                | -0.2         | 0.0%         |
| <b>Effective tax rate net of adjustments to income taxes of previous years</b> |                |              | <b>35.5%</b> |
| Prior year taxes   |                | -5.0         | -0.7%        |
| <b>Total taxes for the year</b>  |                | <b>230.5</b> |              |
| <b>Effective tax rate</b>  |                |              | <b>34.8%</b> |

## 10. Profit from discontinued operations and assets held for sale – € 1.4 million

In accordance with the provisions of accounting standard IFRS 5 - Non-current assets held for sale and discontinued operations, following the agreement for the transfer of 100% of the share capital of Rete Rinnovabile S.r.l., the item includes, amongst others, the result of financial expense for the period of the company RTR (€ 1.3 million). More specifically, under this scope it includes:

- interest expense accrued on the loan of € 500 million supplied by the parent company in September (€ 4.6 million). It is pointed out that, on 28 January 2011, the company RTR, in view of the sale, signed a refinancing contract for a total of € 593.8 million, with a view to refinancing investments sustained for the development of the photovoltaic plant portfolio, on the basis of a project financing no recourse;
- net interest income on the intercompany current accounts held with Terna, for the purpose of centralised treasury management (€ 3.3 million).

The item also includes the capital gain realized from the sale of the residual shareholding in Terna Participações (10,000 units) in response to the Public Offer made on 6 May 2010 by Alterosa, the company deriving from the partial spin-off from Taesa S.A., which acquired control over it during the course of 2009 (€ 0.1 million).

The 2009 comparative figure, of 464.2 million, in fact, refers to the total result of the sale of the share package in the Brazilian subsidiary Terna Participações (€ 385.0 million and € 79.2 million referring respectively to the net capital gain realised and the net dividends distributed prior to the sale).

## D. Notes to the separate statement of financial position

### Assets

## 11. Property, plant and equipment – € 6,687.7 million

Property, plant and equipment amount to € 6,687.7 million (€ 5,890.9 million at 31 December 2009). The amount and changes for each category are reported in the following table:

|   | Land        | Buildings     | Plant and machinery | Industrial and commercial equipment | Other assets | Assets under construction and payments on account | Total           |
|---|-------------|---------------|---------------------|-------------------------------------|--------------|---|-----------------|
| In millions of euros  |             |               |                     |                                     |              |   |                 |
| <b>Cost at 1 January 2010</b>   | <b>53.1</b> | <b>822.5</b>  | <b>8,633.4</b>      | <b>53.3</b>                         | <b>84.2</b>  | <b>801.9</b>                                      | <b>10,448.4</b> |
| Investment  | 3.6         | 1.8           | 11.1                | 3.9                                 | 4.0          | 1,039.0   | 1,063.4         |
| Entry into use  | 24.2        | 134.2         | 795.9               | 5.6                                 | 5.4          | -965.3  | 0.0             |
| Intra-group purchases   | -           | -             | 33.3                | -                                   | -            | 0.9   | 34.2            |
| Disposals and impairment losses   | -           | -0.4          | -52.7               | -0.1                                | -0.6         | -   | -53.8           |
| Other changes (grants)  | -           | -             | -18.0               | -                                   | -            | 5.9   | -12.1           |
| Reclassifications   | 0.8         | -0.4          | -0.4                | -                                   | 0.1          | -   | 0.1             |
| <b>Cost at 31 December 2010</b>   | <b>81.7</b> | <b>957.7</b>  | <b>9,402.6</b>      | <b>62.7</b>                         | <b>93.1</b>  | <b>882.4</b>                                      | <b>11,480.2</b> |
| <b>Accumulated depreciation and impairment losses at 1 January 2010</b>   | <b>-</b>    | <b>-266.2</b> | <b>-4,209.5</b>     | <b>-38.3</b>                        | <b>-43.5</b> | <b>-</b>  | <b>-4,557.5</b> |
| Depreciation for the year   | -           | -20.4         | -238.6              | -3.2                                | -12.2        | -   | -274.4          |
| Intra-group purchases   | -           | 0.0           | -13.0               | -                                   | -            | -   | -13.0           |
| Disposals   | -           | 0.4           | 51.5                | 0.1                                 | 0.4          | -   | 52.4            |
| Reclassifications   | -           | -             | 0.1                 | 0.0                                 | -0.1         | -   | 0.0             |
| <b>Accumulated depreciation and impairment losses at 31 December 2010</b> | <b>-</b>    | <b>-286.2</b> | <b>-4,409.5</b>     | <b>-41.4</b>                        | <b>-55.4</b> | <b>-</b>  | <b>-4,792.5</b> |
| <b>Carrying amount</b>  |             |               |                     |                                     |              |   |                 |
| At 31 December 2010   | 81.7        | 671.5         | 4,993.1             | 21.3                                | 37.7         | 882.4   | 6,687.7         |
| At 31 December 2009   | 53.1        | 556.3         | 4,423.9             | 15.0                                | 40.7         | 801.9   | 5,890.9         |

The category “Plants and machinery” includes the energy Transportation Network as well as the Transformation Stations.

The item shows an increase on the previous year of € 796.8 million in respect of ordinary changes for capital expenditure (€ 1,063.4 million of which € 17.4 million for capitalised borrowing costs), disposals and other changes (€ 13.4 million) and amortisation and depreciation (€ 274.4 million). It also reflects the acquisition of the transmission plants from the subsidiary TELAT (€ 21.2 million) with a view to carrying out a series of urgent interventions for the development and renewal of the NTG in the Territorial Operative Areas of Milan, Padua, Florence and Naples.

A summary of changes in property, plant and equipment during the year is provided in the table below:

In millions of euros

|                             |                |
|-----------------------------|----------------|
| Investment                  |                |
| - Transmission lines        | 471.0          |
| - Transformation stations   | 468.0          |
| - Other                     | 124.4          |
| <b>Total investments</b>    | <b>1,063.4</b> |
| Depreciation                | -274.4         |
| Disposals and other changes | -13.4          |
| Intra-group purchases       | 21.2           |
| <b>Total</b>                | <b>796.8</b>   |

With reference to period investments (€ 1,063.4 million) we note, in particular, the conclusion of the installation of underwater cables of the second SA.PE.I. connection pole (Sardinia - Italian peninsula) for a total of 425 km (€ 168.6 million); the opening of sites and preparation of materials for the alternating current power line in Sorgente-Rizziconi, and the development of all civil engineering works in relation to the conversion stations of Scilla, Villafranca and Sorgente (€ 61.1 million); works relating to the development of the stations 380/150 kV for connection of new wind power production plants between Foggia and Benevento (€ 47.5 million); progress of works aiming to rationalise the city of Turin (€ 34.0 million); progress of works for rationalising the province of Lodi and opening of sites for the construction of two new 380 kV electrical stations in the municipalities of Chignolo Po and Maleo and for the development of a new dual circuit connection at 380 kV along the “La Casella-Caorso” road (totalling € 31.7 million); the purchase of the Florence site and the construction of the new Milan site (totalling € 28.2 million); the completion of activities relating to the Casellina-Tavarnuzze-S. Barbara connection, the 380 kV overhead line part (€ 22.1 million); progress of the preliminary activities for the development of the Italy Montenegro connection (€ 19.5 million).

Following the application – as of 1 January 2010 - of IFRIC 12 (discussed in more detail in section “A. Accounting policies”), the property, plant and equipment identified within the realm of application of IFRIC 12 as dispatching activities have been reclassified to the “Infrastructure rights” item within intangible assets; accordingly, the corresponding amounts in the balance sheet at 31 December 2009 have also been reclassified in the same way. In particular, the carrying amount at 31 December 2009 of the infrastructure relating to the concession arrangements covered by IFRIC 12 (€ 85.4 million) has been reclassified from “Property, plant and equipment” to “Intangible assets”.

In terms of assets under construction at the end of the year, the main grid development and re-powering projects worth more than € 10 million are listed below.

| <b>Transmission lines</b>                    | <b>Euro</b> |
|--|-------------|
| Sorgente-Rizziconi 380 kV power line         | 51,131,685  |
| La Casella-Caorso                            | 37,805,526  |
| Valcamonica (Phase A1)                       | 28,630,604  |
| C.P. Ionadi                                  | 19,654,889  |
| Italy-Montenegro Interconnections            | 18,085,441  |
| Turin Rationalisation – 220 kV               | 16,928,576  |
| S. Barbara-Tavarnuzze-Casellina              | 15,605,272  |
| Restructuring of metropolitan area of Rome   | 14,493,937  |
| Torino-Lacchiarella 380 kV power line        | 13,515,059  |
| <b>Transformation stations</b>               |             |
| Scilla 380/150 kV station                    | 27,903,075  |
| ATR-TR National Reserve                      | 20,991,370  |
| Deliceto 380/150 kV station                  | 17,138,783  |
| Troia 380 kV station                         | 16,410,241  |
| SA.PE.I. station (Fiumesanto and Latina)     | 16,018,275  |
| Station of Cardano-Nuovi armoured department | 15,312,537  |
| Villafranca 380/150 kV station               | 15,156,195  |
| Sorgente 380/220 kV station                  | 14,119,881  |
| Augusta 150 kV station                       | 11,412,581  |
| Villanova 380 kV station                     | 10,982,357  |
| Casuzze 150 kV station                       | 10,291,129  |

## 12. Goodwill – € 88.6 million

Goodwill amounted to € 88.6 million and it is unchanged as compared to the balance of the previous year.

### Impairment testing

#### Cash Generating Unit – Terna

The recoverable amount of the goodwill (as a result of the merger of RTL into Terna in 2008) booked in the financial statements as € 88.6 million, with respect to the Terna Cash Generating Unit (CGU) was estimated using the unlevered version of the discounted cash flow method; the latter estimates future cash flows and applies an appropriate discount rate.

The discounting of the cash flows was performed with respect to the period 2010-2020 and the final value was assumed to be equal to the RAB (Regulatory Asset Base) in 2020. In particular, cash flows were determined, up to 2015, on the basis of the approved business plan, drawing on the forecasts and assumptions it uses for developments in Terna's performance and financial position, while for subsequent years the cash flow projection was based on the development of investments provided in the most recently approved Grid Development Plan and assuming business development operations in line with the last year of the business plan. The discount rate was set at a WACC of 4.78%.

The value in use thus determined was higher than the carrying amount.





### 13. Intangible assets – € 274.0 million

Changes during the year in intangible assets are detailed below:

| In millions of euros               | Infrastructure rights | Concessions  | Other assets | Assets under development and payments on account | Total        |
|------------------------------------|-----------------------|--------------|--------------|--|--------------|
| <b>Balance at 31 December 2009</b> | <b>98.7</b>           | <b>112.1</b> | <b>29.3</b>  | <b>21.5</b>                                      | <b>261.6</b> |
| Investment                         | -                     | -            | 0.0          | 57.0   | 57.0         |
| Entry into use                     | 32.4                  | -            | 17.0         | -49.4  | -            |
| Depreciation                       | -23.7                 | -5.6         | -15.1        | -  | -44.4        |
| Other changes (grants)             | -0.2                  | 0.0          | 0.0          | -  | -0.2         |
| Reclassifications                  | -0.8                  | 0.0          | 0.8          | -  | -            |
| <b>Balance at 31 December 2010</b> | <b>106.4</b>          | <b>106.5</b> | <b>32.0</b>  | <b>29.1</b>                                      | <b>274.0</b> |
| Cost                               | 239.6                 | 135.4        | 104.8        | 29.1   | 508.9        |
| Accumulated amortisation           | -133.2                | -28.9        | -72.8        | -  | -234.9       |
| <b>Balance at 31 December 2010</b> | <b>106.4</b>          | <b>106.5</b> | <b>32.0</b>  | <b>29.1</b>                                      | <b>274.0</b> |

Intangible assets amount to € 274.0 million (€ 261.6 million at 31 December 2009). This item, in particular, includes:

- the infrastructure used for the dispatching service, recognised as of 1 January 2010 in application of IFRIC 12 (discussed in more detail in section “A. Accounting policies”), with a net carrying amount at 31 December 2010 of € 106.4 million for infrastructure already in use and € 25.1 million for the infrastructure under construction classified under “assets under construction and advances” caption, and a net carrying amount at 31 December 2009, of € 98.7 million for infrastructure already in use and € 18.5 million for the infrastructure under construction classified in the “assets under construction and advances” caption;
- the licensing for the provision of electricity transmission and dispatching services in Italy (with a net carrying amount of € 106.5 million at 31 December 2010), recognised initially during 2005 at fair value and subsequently measured at cost.

The other intangible assets comprise application software developed internally or purchased when implementing systems development projects.

The increase of the item as compared with last year (€ 12.4 million) is due to routine movements during the period, regarding mainly to investments (€ 57.0 million, including € 38.6 million in Infrastructure rights) – mainly in application software – and amortisation (€ 44.4 million, of which € 23.7 million in relation to dispatching infrastructure).

Investments for the year in intangible assets (€ 57.0 million) included expenditure on the development and evolution of a software for the remote management system for dispatching (€ 12.7 million), for the Power Exchange (€ 9.5 million) and for the protection of the electrical system (€ 0.6 million), as well as general applications and software licenses (€ 17.8 million).

### 14. Financial assets

The following table details financial assets recognised by Terna S.p.A.:

| In millions of euros                | Carrying amount |                | Change        |
|-------------------------------------|-----------------|----------------|---------------|
|                                     | 31 Dec. 2010    | 31 Dec. 2009   |               |
| Investments in subsidiaries         | 568.4           | 568.4          | 0.0           |
| Investments in associates           | 14.9            | 6.6            | 8.3           |
| Investments in joint ventures       | 0.0             | 0.7            | -0.7          |
| Other shareholdings:                | 0.5             | 0.0            | 0.5           |
| TELAT loan                          | 500.0           | 500.0          | 0.0           |
| FVH derivatives                     | 200.3           | 123.2          | 77.1          |
| <b>Non-current financial assets</b> | <b>1,284.1</b>  | <b>1,198.9</b> | <b>85.2</b>   |
| Other current financial assets      | 2.9             | 503.3          | -500.4        |
| <b>Current financial assets</b>     | <b>2.9</b>      | <b>503.3</b>   | <b>-500.4</b> |

“Non-current financial assets”, equal to € 1,284.1 million, reported the value at 31 December 2010 of equity investments, the intercompany loan to TELAT S.r.l. and the fair value of financial derivatives.

“Investments in subsidiaries” (€ 568.4 million) refer to investments in subsidiaries held directly by Terna S.p.A. and summarised below.

“Investments in associates” (€ 14.9 million) refers to:

- the holding of 39.91% in CESI S.p.A. (€ 14.6 million), an increase of € 8.0 million on the previous year due to the acquisition of additional stakes in the associate CESI in December 2010 from Ansaldo Trasmissione & Distribuzione S.p.A. for 9% of the share capital;
- the holding of 22.485% of the share capital of CORESO S.A. (€ 0.3 million) acquired in November 2010.

CESI S.p.A. operates in the construction and management of laboratories and plants for tests, inspections, studies and experimental research relating to the electro-technical field in general and technical and scientific developments in that area. The company CORESO S.A. is the first technical centre owned by various electrical energy transmission companies which implements joint TSO technical coordination activities in order to improve and strengthen security and coordination of the electrical system in central/western Europe; it prepares daily forecasts and analyses in real of energy flows in the region, identifying potentially critical areas and promptly notifying the TSOs which are affected. For more information, please see the section “Significant events”.

The value of “Investments in joint ventures” has been zeroed out with respect to the balance of last year, due to the write-down of the investment of Terna in ELMED Études Sarl (-€ 0.7 million), which was booked as a result of the changed political situation in Tunisia which occurred during the year and which currently makes the investment difficult to recover. In April 2009, ELMED Études Sarl was established. This limited-liability company is an equally-held joint venture between Terna and Société Tunisienne de l'Electricité et du Gaz (STEG) whose main purpose is the study and preliminary consulting concerning the preparation of documents for the Tunisian government's call for tenders for the construction and management of the power generation hub in Tunisia for the Italy-Tunisia interconnection project.

“Other investments” (€ 0.5 million) refers to:

- the holding of 5.6% of the share capital of Desertec Industrial Initiative (“DII”) (€ 0.1 million) acquired in September 2010;
- the holding of 8.3% of the share capital of CASC CWE S.A. (€ 0.3 million) acquired in November 2010;
- the advance paid by Terna (€ 0.1 million) on 7 December 2010, in accordance with contractual agreements, for the founding of the company Medgrid SAS which occurred on 7 January 2011 with a shareholding of 5% of the share capital;
- for more information, please see the section “Significant events”.

The following table summarises Terna S.p.A.'s direct investments in subsidiaries and associates at 31 December 2010, with data drawn from the most recent approved financial statements:

| Company                  | Registered office  | Assets  | Currency       | Share/quota capital | % held  | Carrying amount |
|--------------------------|--------------------|---|----------------|---------------------|---------|-----------------|
| <b>SUBSIDIARIES</b>      |                    |   |                |                     |         |                 |
| <b>TELAT S.r.l.</b>      | Rome               | Design, construction, management, development, operation and maintenance of high-voltage power lines  | euro           | 243,577,554         | 100%    | 557,666,437     |
| <b>SunTergrid S.p.A.</b> | Rome               | Construction and maintenance of electricity transmission grids and plants for the generation of electricity, including renewables' generation, for own use and sale in Italy and abroad   | euro           | 120,000             | 100%    | 10,672,709      |
| <b>ASSOCIATES</b>        |                    |   |                |                     |         |                 |
| <b>CESI S.p.A.</b>       | Milan              | Experimental electro-technical research   | euro           | 8,550,000           | 30.91%  | 14,618,241      |
| <b>CORESO S.A.</b>       | Brussels (Belgium) | Technical centre owned by various electrical energy transmission companies which implements joint TSO technical coordination activities in order to improve and strengthen security and coordination of the electrical system in central/western Europe. It prepares daily forecasts and analyses in real of energy flows in the region, identifying potentially critical areas and promptly notifying the TSOs which are affected. | euro           | 1,000,000           | 22.485% | 281,082         |
| <b>JOINT CONTROL</b>     |                    |   |                |                     |         |                 |
| <b>ELMED Etudes SARL</b> | Tunis              | Analysis and preliminary consulting for the preparation of tender documentation of the Tunisian government for construction tenders and the management of the electricity generation site in Tunisia involved in the project for the interconnection of Italy and Tunisia   | Tunisian Dinar | 2,700,000           | 50%     | 0               |

The fair value of the FVH derivatives hedging the Company's bonds, equal to € 200.3 million, is calculated by discounting forecast cash flow with the market interest rate curve at the date of reference. The increase in the fair value of the derivatives (€ 77.1 million) compared with 31 December 2009 is essentially attributable to the decline in market interest rates during the course of 2010 and is offset by the fair value increase of the bonds recorded within financial liabilities.

The item "Current financial assets" records a balance of € 2.9 million (€ 503.3 million as of 31 December 2009). This mainly refers to interest accrued and not yet collected as of the reporting date in relation to the intercompany loan to TELAT (€ 2.4 million). The decrease (€ 500.4 million) with respect to the previous year, equal to € 500.4 million, is primarily due to the redemption – during the course of 2010 – of investments in securities undersigned with UBS and MPS in 2009 (-€ 500.0 million).

## 15. Other assets

“Other assets” are analysed below:

| In millions of euros              | 31 Dec. 2010 | 31 Dec. 2009 | Change       |
|-----------------------------------|--------------|--------------|--------------|
| Receivables due from others:      |              |              |              |
| - loans and advances to employees | 5.9          | 5.1          | 0.8          |
| - deposits with third parties     | 0.3          | 0.4          | -0.1         |
| <b>Other non-current assets</b>   | <b>6.2</b>   | <b>5.5</b>   | <b>0.7</b>   |
| <b>Other tax assets</b>           | <b>3.9</b>   | <b>17.7</b>  | <b>-13.8</b> |
| Receivables due from others:      |              |              |              |
| - advances to employees           | 0.2          | 0.2          | 0.0          |
| - others                          | 14.5         | 8.6          | 5.9          |
| <b>Other current assets</b>       | <b>18.6</b>  | <b>26.5</b>  | <b>-7.9</b>  |

**Other non-current assets** (€ 6.2 million) - which are reported in the table above - are essentially unchanged since the end of last year (€ 5.5 million) and mainly comprise loans and advances paid to employees (€ 5.9 million).

The item “Other current assets”, equal to € 18.6 million and whose composition is reported in the previous statement, decreased by € 7.9 million compared to 31 December 2009 and is essentially due to:

- other minor tax assets (€ 13.8 million), mainly related to:
  - collection of receivables due to the Greek tax authorities for indirect taxes relative to activities implemented by the branch company of Terna in Greece (-€ 8.8 million);
  - decreased withholding taxes on interest income accrued on investments (-€ 1.6 million);
  - lesser VAT receivables (-€ 0.6 million);
- receivables from others (€ 5.9 million), mainly regarding:
  - increased quotas of previously paid costs which accrue in subsequent years (€ 1.4 million) and which are ascribable to insurance premiums;
  - the booking of revenue which accrued during the year and which was not yet collected at the reporting date (€ 2.0 million) and relative to use by Enel Distribuzione of the Company’s infrastructures, aiming to ensure power line communication;
  - increased receivables for insurance reimbursements accrued in the year but still not paid (about € 1.9 million).

## 16. Inventories – € 11.4 million

Current asset inventories (€ 11.4 million) refer to a balance which has not undergone any significant changes with respect to the previous year (€ 11.7 million); it relates to materials and devices allocated for operational, maintenance and construction activities of plants.

## 17. Trade receivables – € 1,495.6 million

Trade receivables are analysed as follows:

| In millions of euros              | 31 Dec. 2010   | 31 Dec. 2009   | Change       |
|-----------------------------------|----------------|----------------|--------------|
| Energy-related receivables        | 1,116.2        | 843.9          | 272.3        |
| Grid transmission fees receivable | 304.8          | 284.6          | 20.2         |
| Other trade receivables           | 64.2           | 38.5           | 25.7         |
| Receivables from subsidiaries     | 10.4           | 10.1           | 0.3          |
| <b>Trade receivables</b>          | <b>1,495.6</b> | <b>1,177.1</b> | <b>318.5</b> |

Trade receivables amount to € 1,495.6 million. The increase (€ 318.5 million) with respect to the previous year mainly comprises pass-through amounts deriving from the electricity dispatching activities.

Receivables are measured net of impairment losses, relating to items considered uncollectible and recognised as an adjustment in the allowance for impairment losses (€ 16.8 million for energy items and € 6.7 million for other items in 2010, compared with € 22.3 million for energy-related items and € 4.7 million for other items in 2009).

#### Energy-related receivables – € 1,116.2 million

They mainly include receivables in relation to pass-through energy items arising in respect of dispatching activities. This item also includes receivables for fees payable by market operators for dispatching activities (DIS fee as per AEEG Resolution no. 237/04 and its subsequent amendments and supplements).

The increase in this caption by € 272.3 million since the end of last year was mainly due to:

- additional receivables for the accrued incentives associated with the reduction in volumes procured from the dispatching service market, made available under AEEG Resolution 213/09 (+€ 77.0 million compared with the incentive reported in the previous year on the basis of Resolution ARG/elt 206/08);
- increased receivables from the sale of electrical energy within the power exchange (€ 105.7 million) which were primarily due to the net effect of increased receivables for the UPLIFT component (€ 136.1 million), as well as the booking of receivables for virtual interconnection activities (€ 35.2 million), the compensation used to cover the costs for modulating wind production (in accordance with article 44-bis of AEEG Resolution 111/06, totalling € 19.5 million), the dispatching of electrical energy produced by non-programmable renewable resources pursuant to Resolution ARG/elt 5/10 (€ 11.6 million) and the increased receivables generated from the increase in volumes of resources attained from the energy market (€ 21.3 million); these were partly compensated by the decreased receivables generated from the reduction of quantities and the reduction in valuation prices of the imbalance as well as the advance invoicing of balances required by Resolution AEEG 34/09 (€ 60.4 million) and decreased receivables (€ 58.3 million) which, in particular, refer to the mechanism for compensating costs correlated to energy transmissions across foreign electrical networks and the balance for delayed adjustments relative to 2008 on the basis of Resolution ARG/elt 111/10;
- increased receivables from the sale of electrical energy outside of the power exchange (€ 81.4 million) which essentially refer to the dispatching service for energy collection; these are due from market operators.

#### Grid transmission fees receivable – € 304.8 million

The receivable relative to grid transmission fees, equal to € 304.8 million, refer to the compensation due to the Company and other owners for utilisation of the National Transmission Grid from distributors of electrical energy; it primarily refers to the fee which accrued in the last two months of the year, with a normal expiration date in the months of the January and February 2011. The above-mentioned receivable reported a positive change equal to 20.2 million compared to the previous year; this was primarily due to the effect of the incentive from CCSE on the remuneration of investments in strategic transmission infrastructures (Resolution ARG/elt 87/10 – +€ 16.8 million) as well as rate adjustments.

#### Other trade receivables – € 64.2 million

Other trade receivables mainly refer to amounts due from diversified business clients and record an increase of € 25.7 million on last year, mainly due to the greater receivables due from Italy clients (€ 15.9 million), mainly for orders underway with third party clients in relation to stations and connections, and receivables due for invoices to be issued for the sale, on the basis of specific contractual agreements, of photovoltaic panels (€ 15.3 million) to contractors appointed to develop the photovoltaic plants owned by the subsidiary RTR. This item also includes receivables for contract work in progress (€ 1.1 million), highlighted in the table below, relative to works of multi-year duration which the Company has been implementing with third party customers and which decreased with respect to the previous year by € 1.5 million:

| In millions of euros | Payments on account | Contract value | Balance at 31 Dec. 2010 | Payments on account | Contract value | Balance at 31 Dec. 2009 |
|----------------------|---------------------|----------------|-------------------------|---------------------|----------------|-------------------------|
| Others               | -11.1               | 12.2           | 1.1                     | -9.8                | 12.4           | 2.6                     |
| <b>Total</b>         | <b>-11.1</b>        | <b>12.2</b>    | <b>1.1</b>              | <b>-9.8</b>         | <b>12.4</b>    | <b>2.6</b>              |

#### Receivables from subsidiaries – € 10.4 million

The item amounts to € 10.4 million and regards receivables in respect of contracts for the coordination and operational management of the subsidiaries, in particular:

- receivables due from TELAT amount to € 3.8 million and relate to maintenance work and technical services of the HV lines owned, in relation to December;
- receivables due from RTR amount to € 6.4 million and mainly relate to the sale of solar panels used on its sites;
- receivables due from RTS amount to € 0.2 million and refer to the sale of equipment needed to develop its photovoltaic plants.

The guarantees given to third parties by Terna at 31 December 2010 totalled € 19.6 million. They comprise payable sureties issued to secure the contractual obligations arising in relation to operating activities.

## **18. Cash and cash equivalents – € 168.7 million**

Cash and cash equivalents at 31 December 2010 amounted to € 168.7 million and refer to the cash invested in short-term deposits for € 150.0 million, to the credit position on the intercompany current account held with TELAT S.r.l. for € 24.3 million, to the debt position on the intercompany current account held with SunTergrid S.p.A. and RTS S.r.l. respectively for € 3.4 million and € 2.3 million and to cash provisions provided to territorial operational areas for € 0.1 million.

The item notes an increase on last year of € 168.6 million, due to the cash invested in short-term deposits and net liquidity on intercompany bank current accounts as described above.

## **20. Tax assets – € 16.8 million**

Tax assets came to € 16.8 million, attributable to deferred tax assets created following the release of the goodwill deriving from the merger by incorporation of the subsidiary RTL (€ 12.6 million) and the recognition, pursuant to art. 6 of the Law of 28 January 2009, of the receivable due from tax authorities for excess income taxes paid in previous years as a result of not deducting IRAP in the amount provided for under the law (€ 4.2 million).

The decrease of € 1.6 million in this item with respect to the previous year is exclusively due to the release of the quota of the year of the substitute tax paid under art. 15 of Legislative Decree no. 185/2008 to release the goodwill that arose on the merger by incorporation of RTL.

## **21. Discontinued operations and assets held for sale – € 259.2 million**

The items “Assets held for sale” and “Discontinued operations” include the balances of financial expense of the company RTR, reclassified following the stated sales agreement for the subsidiary.

“Assets held for sale”, for € 504.6 million, includes the balance of the intercompany loan granted to the subsidiary RTR in September (€ 500 million) and the balance of interest accrued on the loan but not collected as of the reference date of these statements (€ 4.6 million).

“Discontinued operations” amounting to € 245.4 million includes the balance of the liability position of the treasury current account with regards to RTR.

## **Liabilities**

## **22. Equity – € 2,534.3 million**

### **Share capital – € 441.0 million**

The share capital of Terna is represented by 2,004,395,700 ordinary shares, par value € 0.22 each. The increase of € 0.8 million with respect to the previous year reflects the issue of 3,486,900 shares, during 2010, to service the Stock Option Plan described later in this report.

### **Legal reserve – € 88.0 million**

Terna S.p.A.'s Shareholders' Meeting that met on 13 May 2011 and approved Terna's financial statement, resolved to allocate the 2010 net profits to legal reserve up to its reaching 20% of the share capital.

### **Other reserves – € 703.0 million**

Other reserves have increased by € 32.3 million due to:

- other comprehensive income (€ 25.9 million): adjustment to fair value of derivatives hedging floating-rate loans of the Company (cash flow hedges), which produced a decrease of € 35.7 million, net of the related tax effect (–€ 9.8 million);
- transactions with shareholders (€ 6.4 million): increase in the share price premium reserve (€ 6.8 million) and decrease in the stock option reserve (–€ 0.4 million) to reflect the stock options exercised during the period.

### Retained earnings – € 1,029.0 million

The increase of € 409.5 million regarded the residual profit for 2009, equal to profit remaining after the distribution of the 2009 dividend (€ 380.5 million).

### Interim dividend

After receiving the report of the independent auditors required by art. 2433-bis of the Italian Civil Code, on 18 October 2010 the Company's Board of Directors approved the distribution of an interim dividend of € 160.4 million, equal to € 0.08 per share, which is payable on the upcoming 25 November, with an ex dividend date (coupon 13) of 22 November 2010.

The following table reports the origin, availability and possibility of distribution of the components of equity:

| In millions of euros | 31 Dec. 2010   | Possibility of use | Available portion |
|----------------------|----------------|--------------------|-------------------|
| Share capital        | 441.0          | B                  | -                 |
| Legal reserve        | 88.0           | B                  | 88.0              |
| Other reserves       |                |                    |                   |
| - equity-related     | 404.8          | A,B,C              | 404.8             |
| - income-related (*) | 298.2          | A,B,C              | 298.2             |
| Retained earnings    | 1,029.0        | A,B,C              | 1,029.0           |
| Interim dividend     | -160.4         | A,B,C              | -                 |
| Profit for the year  | 433.7          | -                  | -                 |
| <b>Total</b>         | <b>2,534.3</b> |                    | <b>1,820.0</b>    |

Key:

A - for share capital increase

B - for coverage of losses

C - for distribution to shareholders

(\*) Includes the negative reserve for the effective portion of changes in the fair value of cash flow hedges, which is equal, net of tax effects, to € 35.3 million.

Of the total available portion, € 642.5 million refers to untaxed income-related reserves.

### Stock Option Plans

On 21 December 2005, based on proposals presented by the Remuneration Committee, the Company's Board of Directors approved a Stock Option Plan for 2006 applicable to those senior managers of Terna who hold key roles in terms of achieving the Company's strategic objectives.

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 that imbues key employees with a sense of belonging to the corporate team, while ensuring they are constantly focused on creating value, with a view to melding the interests of shareholders and management.

The features of the 2006 Stock Option Plan are outlined below:

#### Rules governing the 2006 Stock Option Plan (approved on 21 December 2005)

The plan provides for the distribution of a maximum of 10,000,000 options to about 20 Terna managers holding the most important positions in terms of achieving the Company's strategic targets, including the CEO, as a senior manager of the Company.

Under the approved rules governing the Stock Option Plan:

- the strike price of each share shall be the arithmetic mean of the reference price of Terna ordinary share observed on the electronic Stock Exchange operated by Borsa Italiana S.p.A. in the period between the date of the offer and the same day of the previous calendar month;
- the exercise of the options and, consequently, the right to subscribe newly-issued Terna ordinary shares depends on achieving two performance parameters. In particular:
  - Terna EBITDA for the grant year (2006) must be greater than that established in the budget approved by the Board of Directors;
  - the 2006 performance of each beneficiary must be positively assessed by the CEO, with a provision for a 50% reduction in the options that the individual beneficiary can exercise, should this second condition not be met;
  - if the exercise conditions are met, individual beneficiaries can exercise their options by 31 March 2010 up to the following maximum quantities:
  - up to 30% of vested options, beginning from the date specified in the notice announcing that the exercise conditions have been met;



- up to 60% of vested options, beginning from the first day of the first calendar year subsequent to that in which the notice announcing that the exercise conditions have been met is issued;
- up to 100% of vested options, beginning from the first day of the second calendar year subsequent to the year in which the notice announcing that the exercise conditions have been met is issued.

On 22 April 2009, the Extraordinary Shareholders' Meeting voted to extend the time limit for exercising the options under the above-mentioned option plan by three years until 31 March 2013, and to amend art. 5 of the Bylaws.

Options can be exercised only on a Stock Exchange trading day during the last 10 days of each month. However, options cannot in any case be exercised in the following days:

- in the period between the third-to-last trading day and the last trading day before the *ex dividend* date;
- in the period between the date scheduled for the approval of the financial statements of the year by the Board of Directors and the same day of the previous month;
- in the period between the date scheduled for the approval of the half-year report by the Board of Directors and the same day of the previous month.

The 2006 Stock Option Plan entailed the granting, on 21 December 2005, of 9,992,000 options with a strike price of € 2.072 to 17 managers of the Company. The Board of Directors verified that the conditions for exercise were met when it approved the financial statements of 31 December 2006.

At 31 December 2010, the changes in the options granted under this plan are summarised as follows:

|                                      |           |
|--------------------------------------|-----------|
| Outstanding at the start of the year | 9,083,200 |
| Unopted during the year              | 5,596,300 |
| Exercised during the year            | 3,486,900 |
| Outstanding at the end of the year   | 5,596,300 |
| Exercisable at the end of the year   | 5,596,300 |

The weighted average prices of the shares at their exercise dates were:

- € 3.226 (\*) on 22 March 2010;
- € 3.226 (\*) on 23 March 2010;
- € 3.218 (\*) on 24 March 2010;
- € 3.224 (\*) on 29 March 2010;
- € 3.216 (\*) on 31 March 2010;
- € 3.048 (\*) on 30 April 2010;
- € 3.062 (\*) on 31 May 2010;
- € 3.061 (\*) on 21 June 2010;
- € 3.292 (\*) on 29 October 2010.

(\*) Source: Bloomberg

Fair value at the grant date was determined using the Cox-Rubinstein pricing method, which takes account of Terna's stock price at the grant date, the volatility of the security, and the rate curve at the grant date considering the term of the plan. The following pricing parameters were used:

- Closing price (underlying or spot price) for the stock on the grant date (source Bloomberg) of € 2.058;
- Strike price of € 2.072;
- Rate curve for calculating the discount factors at the grant date (source Reuters);
- Historical volatility of the stock identified 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 and General Managers:

| Name and Surname | Position | Number of options |
|------------------|----------|-------------------|
| Flavio Cattaneo  | CEO      | 2,115,000         |

Other information on the Stock Option Plan:

|  |           |
|--|-----------|
| Other beneficiaries of the Stock Option Plan | 3,481,300 |
|--|-----------|

## 22. Loans and financial liabilities

The following table details loans and financial liabilities recognised in the separate financial statements of Terna at 31 December 2010:

| In millions of euros   | Carrying amount |                | Change       |
|--|-----------------|----------------|--------------|
|  | 31 Dec. 2010    | 31 Dec. 2009   |              |
| Bonds  | 2,728.2         | 2,643.5        | 84.7         |
| Bank loans   | 2,419.3         | 1,555.7        | 863.6        |
| <b>Long-term loans</b>   | <b>5,147.5</b>  | <b>4,199.2</b> | <b>948.3</b> |
| CFH derivatives  | 47.1            | 82.6           | -35.5        |
| <b>Non-current financial liabilities</b>                       | <b>47.1</b>     | <b>82.6</b>    | <b>-35.5</b> |
| Short-term loans   | 73.1            | 42.7           | 30.4         |
| Current portion of long-term loans                             | 59.7            | 59.7           | 0.0          |
| <b>Short-term loans and current portion of long-term loans</b> | <b>132.8</b>    | <b>102.4</b>   | <b>30.4</b>  |
| <b>Total</b>   | <b>5,327.4</b>  | <b>4,384.2</b> | <b>943.2</b> |

Gross debt for the year increased with respect to the previous year by € 943.2 million to € 5,327.4 million.

The increase in the carrying amounts of bonds (€ 84.7 million) comprises the change in the fair value of the hedged risk, € 75.9 million, and capitalisation of the inflation for the period net of the amortised-cost effect, € 8.8 million. The change linked to the hedging of interest-rate risk comprises € 17.4 million in relation to the inflation-linked bonds, € 39.3 million to the 2014-2024 bonds and € 19.2 million to the private placement, and offsets the increase in the fair value of the derivatives recognised as financial assets, € 77.1 million.

The fair value of the bonds is measured by discounting the projected cash flows along a yield curve of interest rate at the reporting date. The latest official prices for the bonds listed on the Luxembourg Stock Exchange are detailed below:

- bond maturing 2024, 2010 price: 104.23; 2009 price: 102.29;
- bond maturing 2014, 2010 price: 105.70; 2009 price: 104.34;
- bond maturing 2023, 2010 price: 96.57; 2009 price: 102.60;
- bond maturing 2019, 2010 price: 105.00; 2009 price: 103.56.

Source: Reuters

Consequently, compared with the total carrying amount of € 2,782.2 (€ 2,643.5 million at 31 December 2009), the market value is € 2,609.7 (€ 2,600.3 at 31 December 2009).

As regards debt originally bearing floating rates, the increase of € 894.0 million is due to:

- a € 59.7 million reduction in European Investment Bank loans and other financing following repayments made on outstanding loans;
- the collection in March of an EIB loan totalling € 73 million;
- the collection in November of an EIB loan totalling € 300 million;
- an increase in other loans of € 550 million as a result of drawing on the 2006 revolving credit facility;
- the establishment of a short-term loan totalling € 50 million;
- decrease in the use of overdraft facilities in the amount of € 16.9 million.

Movements include the issue, on 25 March 2010, of the previously cited EIB financing of € 73 million which has a term of 20 years and will be repaid in semi-annual instalments as of the fifth year at 6-month Euribor uplifted by 40 basis points. These include the issue, on 24 November 2010, of the previously cited EIB financing of € 300 million which has a term of 20 years and will be repaid in semi-annual instalments as of the fifth year at 6-month Euribor uplifted by 39 basis points.

## Long-term loans

The following table reports the carrying amounts of long-term debt and the repayment plan as of 31 December 10, broken down by loan type, including amounts falling due within one year and average interest rate at year-end:

|                            |           | Maturity 31 Dec. 2009 | 31 Dec. 2010   | Due within one year | Due beyond one year | 2012        | 2013         | 2014         | 2015         | After          | Average interest rate as of 31 Dec. 2009 |
|----------------------------|-----------|-----------------------|----------------|---------------------|---------------------|-------------|--------------|--------------|--------------|----------------|--|
| In millions of euros       |           |                       |                |                     |                     |             |              |              |              |                |  |
| Bonds 10y and 20y          | 2014-2024 | 1,479.5               | 1,518.8        | 0.0                 | 1,518.8             | 0.0         | 0.0          | 636.5        | 0.0          | 882.3          | 4.62%                                    |
| Bond Inflation Linked      | 2023      | 563.5                 | 589.7          | 0.0                 | 589.7               | 0.0         | 0.0          | 0.0          | 0.0          | 589.7          | 4.42%                                    |
| Bond Private Placement     | 2019      | 600.5                 | 619.7          | 0.0                 | 619.7               | 0.0         | 0.0          | 0.0          | 0.0          | 619.7          | 4.88%                                    |
| <b>Total fixed rate</b>    |           | <b>2,643.5</b>        | <b>2,728.2</b> | <b>0.0</b>          | <b>2,728.2</b>      | <b>0.0</b>  | <b>0.0</b>   | <b>636.5</b> | <b>0.0</b>   | <b>2,091.7</b> |  |
| EIB                        | 2014-2030 | 766.9                 | 1,080.1        | 59.7                | 1,020.4             | 59.7        | 69.4         | 79.2         | 76.9         | 735.2          | 1.03%                                    |
| Club Deal                  | 2015      | 648.5                 | 648.9          | 0.0                 | 648.9               | 0.0         | 0.0          | 0.0          | 648.9        | 0.0            | 1.31%                                    |
| RCF 2006                   | 2013      | 200.0                 | 750.0          | 0.0                 | 750.0               | 0.0         | 750.0        | 0.0          | 0.0          | 0.0            | 1.04%                                    |
| <b>Total floating rate</b> |           | <b>1,615.4</b>        | <b>2,479.0</b> | <b>59.7</b>         | <b>2,419.3</b>      | <b>59.7</b> | <b>819.4</b> | <b>79.2</b>  | <b>725.8</b> | <b>735.2</b>   |  |
| <b>Total</b>               |           | <b>4,258.9</b>        | <b>5,207.2</b> | <b>59.7</b>         | <b>5,147.5</b>      | <b>59.7</b> | <b>819.4</b> | <b>715.7</b> | <b>725.8</b> | <b>2,826.9</b> |  |

The repayment of the nominal amount of the 2014, 2024, and 2019 bonds, equal to € 2,000.0 million, will entail payment of € 600.0 million on 28 October 2014, € 800.0 million on 28 October 2024 and € 600 million on 3 October 2019; the inflation-linked bonds will be repaid at maturity, on 15 September 2023, with the nominal value adjusted to reflect inflation. All other financial debt items are stated at their nominal value along with the related repayment plan.

The total loans at 31 December 2010 of Terna amount to € 5,207.2 million, including loans of € 5,147.5 million due after one year and € 2,826.9 million due after the fifth year.

The table shows the average interest rate for each type of financial liability. Below we also comment on the Group's hedging operations against interest rate fluctuations.

As regards the 2014-2024 bonds, with an average coupon of 4.62%, if FVH hedging operations are taken into account, the average interest rate is equal to 1.42%.

For the inflation-linked bonds – and taking hedges into account – and assuming a 1.68% inflation rate, the average interest rate paid in the year was 1.03%.

In line with financial risk management policies, the fixed-rate private placement was synthetically transformed to a floating rate security by means of derivative contracts with the same maturity. Consequently, the average interest rate paid in the year was 2.31%.

With regard to floating rate loans covered by fluctuations in interest rates – and taking into account the effect of derivative financial instruments booked as cash flow hedges – an average rate of 4.46% is reported for EIB financing while for the Club Deal financing totalling € 650 million the average rate was 4.70% and for the RCF financing the average rate was 2.17%.



The following table reports changes in long-term debt for the year:

| Type of loan                | Nominal debt at 31 Dec. 2009 | Carrying amount at 31 Dec. 2009 | Repayment and capitalisation | New issues   | Delta Fair Value 31 Dec. 2009 31 Dec. 2010 | Change in carrying amount | Nominal debt at 31 Dec. 2010 | Carrying amount at 31 Dec. 2010 |
|-----------------------------|------------------------------|---------------------------------|------------------------------|--------------|--|---------------------------|------------------------------|---------------------------------|
| In millions of euros        |                              |                                 |                              |              |  |                           |                              |                                 |
| Listed fixed-rate bonds     | 1,400.0                      | 1,479.5                         | 0.0                          | 0.0          | 39.3                                       | 39.3                      | 1,400.0                      | 1,518.8                         |
| Listed IL bond              | 521.0                        | 563.5                           | 8.8                          | 0.0          | 17.4                                       | 26.2                      | 529.8                        | 589.7                           |
| Private Placement           | 600.0                        | 600.5                           | 0.0                          | 0.0          | 19.2                                       | 19.2                      | 600.0                        | 619.7                           |
| <b>Total bonds</b>          | <b>2,521.0</b>               | <b>2,643.5</b>                  | <b>8.8</b>                   | <b>0.0</b>   | <b>75.9</b>                                | <b>84.7</b>               | <b>2,529.8</b>               | <b>2,728.2</b>                  |
| Bank loans                  | 1,616.8                      | 1,615.4                         | (59.7)                       | 923.0        | 0.3  | 863.6                     | 2,480.1                      | 2,479.0                         |
| <b>Total bank loans</b>     | <b>1,616.8</b>               | <b>1,615.4</b>                  | <b>(59.7)</b>                | <b>923.0</b> | <b>0.3</b>                                 | <b>863.6</b>              | <b>2,480.1</b>               | <b>2,479.0</b>                  |
| <b>Total financial debt</b> | <b>4,137.8</b>               | <b>4,258.9</b>                  | <b>(50.9)</b>                | <b>923.0</b> | <b>76.2</b>                                | <b>948.3</b>              | <b>5,009.9</b>               | <b>5,207.2</b>                  |

As compared with 31 December 2009, long-term debt shows an overall increase of € 948.3 million, for € 550 million drawn from the Revolving Credit Facility, for € 373 million in the form of two new loans from the EIB, € 8.8 million on the capitalisation of inflation for the period in relation to the IL bond, and € 75.9 million on the increase in the fair value of the bonds due to the decline in interest rates, net of € 59.7 million in instalment payments on the EIB loans and for € 0.3 million to the measurement of the Club Deal loan at amortised cost.

As of 31 December 2010, Terna has unused lines of credit exceeding € 1,697.6 million, of which more than € 697.6 million in short-term credit lines and € 1,000.0 million in medium-term credit lines.

#### Non-current financial liabilities

The table below reports the amount and changes in non-current financial liabilities with respect to value at the end of 2009:

| In millions of euros | 31 Dec. 2010 | 31 Dec. 2009 | Change       |
|----------------------|--------------|--------------|--------------|
| CFH derivatives      | 47.1         | 82.6         | -35.5        |
| <b>Total</b>         | <b>47.1</b>  | <b>82.6</b>  | <b>-35.5</b> |

“Non-current financial liabilities” include the fair value of cash flow hedges.

Fair value was measured by discounting the expected cash flows using the market yield curve at the reporting date. The change with respect to 31 December 2009 was equal to -€ 35.5 million.

#### Short-term loans

Short-term loans, equal to € 73.1 million, consist of drawings on overdraft facilities for € 23.1 million and short-term loans for € 50.0 million.

#### Current financial liabilities

Current financial liabilities, which are generated by the net financial expense accrued on financial instruments but not yet settled, decreased on the previous year by € 1.3 million; this was primarily due to current financial liabilities for private placement (-€ 7.4 million) and the relative derivatives (€ 2.9 million) which were partially compensated by the greater amount of loans in force in 2010 (€ 3.2 million).

The following table details deferred liabilities on the basis of the financial liabilities to which they relate:

| In millions of euros            | 31 Dec. 2010 | 31 Dec. 2009 | Change      |
|---------------------------------|--------------|--------------|-------------|
| <b>Deferred liabilities on:</b> |              |              |             |
| Derivatives:                    |              |              |             |
| - <i>hedging</i>                | -6.5         | -9.4         | 2.9         |
| Bond                            |              |              |             |
| - <i>IL</i>                     | 4.3          | 4.3          | 0.0         |
| - <i>private placement</i>      | 7.2          | 14.6         | -7.4        |
| - <i>10 years</i>               | 4.5          | 4.5          | 0.0         |
| - <i>20 years</i>               | 7.0          | 7.0          | 0.0         |
| <b>Total</b>                    | <b>23.0</b>  | <b>30.4</b>  | <b>-7.4</b> |
| Loans                           | 7.7          | 4.5          | 3.2         |
| <b>Total</b>                    | <b>24.2</b>  | <b>25.5</b>  | <b>-1.3</b> |

### Net financial position

Pursuant to the CONSOB Communication of 28 July 2006, and in conformity with the CESR Recommendation of 10 February 2005 for the “*Consistent implementation of the European Commission regulation on prospectuses*”, the net financial position of the Company is as follows:

| In millions of euros                                      | Carrying amount<br>31 Dec. 2010 |
|---|---------------------------------|
| A. Cash   | 0.1                             |
| B. Other liquidity  | 150.0                           |
| C. TELAT loan   | 500.0                           |
| D. Net current a/c position of intercompany treasury      | 18.6                            |
| <b>E. Cash and cash equivalents (A) + (B) + (C) + (D)</b> | <b>668.7</b>                    |
| F. Current portion of long-term debt                      | 59.7                            |
| G. -Short-term loans                                      | 73.1                            |
| <b>H. Current financial debt (F)+ (G)</b>                 | <b>132.8</b>                    |
| <b>I. Net current financial debt (H) - (E)</b>            | <b>-535.9</b>                   |
| J. Non-current bank debt                                  | 2,419.3                         |
| K. Bonds  | 2,728.2                         |
| L. Derivative financial instruments in portfolio          | -153.2                          |
| <b>M. Net non-current financial debt (J)+ (K)+ (L)</b>    | <b>4,994.3</b>                  |
| <b>N. Net financial debt (I) + (M)</b>                    | <b>4,458.4</b>                  |

For more detail on the composition of the items in this table, please see notes 14 and 18, as well as the information presented here in note 22.

Certain long-term loans obtained by Terna S.p.A. are subject to covenants normally applying in international practice. The principal covenants relate to:

- the Company's bonds, comprising two issues of € 600 million and € 800 million in 2004, and two issues under the € 4,000,000,000 Euro Medium-Term Notes Programme, one of € 500 million in 2007 and one, in the form of a private placement, of € 600 million in 2009;
- bank debt, consisting of two revolving lines of credit of € 500 and € 750 million, a “Club Deal” syndicated loan of € 650 million, and a loan from Cassa Depositi e Prestiti (CDP) of € 500 million that draws on EIB funds;
- loans from the European Investment Bank (EIB) totalling € 1,298 million.



None of the covenants have been triggered to date.

The principal covenants relating to the issue of bonds and the € 4 billion EMTN programme are summarised below:

- “negative pledge” clauses, under which the Issuer or “significant subsidiaries” (consolidated companies whose total assets represent at least 10% of total consolidated assets and, solely for the EMTN programme, whose registered offices are in an OECD country) may not establish or maintain mortgages, liens or other encumbrances on all or part of its assets in order to secure listed bonds, unless these guarantees are extended on the same basis to the bonds concerned. A number of exceptions apply (guarantees required by law, guarantees in place prior to the date of the loan, guarantees on new assets that only secure the debt arranged to acquire them etc.), in relation to which the Company is not bound by the above pledges;
- “pari passu” clauses under which the securities constitute a direct, unconditional and unsecured obligation of the issuer and are issued without preferential rights among them and have at least the same seniority as other present and future unsecured and unsubordinated borrowing of the issuer;
- “default event” clauses, under which certain events (e.g. failure to pay, initiation of liquidation proceedings, breach of contractual obligations etc.) are considered to represent potential default; in addition, under the “cross default” clauses, the occurrence of a default event in respect of any financial liability (above a threshold level) issued by the Issuer also constitutes a default in respect of the loan concerned, which becomes immediately repayable;
- periodic or occasional reporting requirements on the occurrence of specified events;
- voluntary early redemption clauses, under which the Issuer may redeem at any time all outstanding bonds at par, in the event of new tax requirements.

The principal covenants for the revolving lines of credit, the “Club Deal” syndicated loan and the € 500 million loan from CDP are summarised below:

- “negative pledge” clauses, under which the Company and each significant subsidiary (consolidated companies whose total assets represent at least 10% of total consolidated assets) agree not to establish new guarantees securing any type of financial liability, with the exception of permitted guarantees (guarantees required by law, guarantees in place prior to the date of the loan, guarantees on new assets that only secure the debt arranged to acquire them, guarantees given to governmental or international entities, including the EIB, guarantees on borrowing whose amount does not exceed 10% of total assets etc.);
- “pari passu” clauses under which the payment undertakings of the borrower in respect of loans are not subordinate to any obligation in respect of other unsecured and unsubordinated creditors, except in the case of statutory preferential rights;
- “event of default” clauses linked to the occurrence of specified events (such as, for example: failure to pay; false declarations, insolvency, termination of activities, seriously prejudicial events, breach of contractual obligations, including the equality of the conditions applied by lenders etc.) are considered to represent potential default; in addition, under the “cross default” clauses, the occurrence of a default event in respect of any financial liability (above a threshold level) also constitutes a default in respect of the loan concerned, which becomes immediately repayable;
- periodic or occasional reporting requirements on the occurrence of specified events;
- compulsory early redemption clauses under which the Company is required to repay the loan early if its long-term credit rating is reduced below investment grade (BBB-) by a majority of the rating agencies that monitor the Company, if the Company ceases to be monitored by one or more rating agencies.

The main covenants governing the EIB loans can be summarised as follows:

- “negative pledge” clauses, under which if the Company establishes, agrees, provides or decides to maintain restrictions in favour, whether directly or indirectly, of third parties (such as unsecured or secured guarantees, liens, encumbrances, charges or other rights), it must also extend equivalent guarantees to the Bank, upon simple request from the latter, except in the case of restrictions granted in relation to borrowing below a threshold level;
- clauses requiring the delivery of additional guarantees to the Bank in the event of a reduction in the Company's rating: clauses requiring the pledging of additional guarantees to the EIB in the event of a reduction in the Company's rating: A- by Standard & Poor's; or A3 by Moody's; or A- by Fitch), the Bank is entitled to require the Company to provide it with additional guarantees that are considered satisfactory at the sole discretion of the Bank, exercised on a reasonable basis.
- “pari passu” clauses, under which, for the entire period of the loans, the Company will ensure that the payment obligations have the same seniority as those relating to all other unsecured and unsubordinated creditors.
- periodic or occasional reporting requirements on the occurrence of specified events concerning both the projects being financed and the Company itself;
- clauses regarding “termination”/“early repayment”/“withdrawal” of the contract: on which basis, where certain events occur (such as, for example: failure to pay, serious inaccuracies in documentation presented, insolvency, events resulting in negative consequences on the financial commitments made by the company, special administration, liquidation, etc.) constitutes default, triggering immediate repayment; in addition, where the Company is required upon default to discharge in advance any other financial obligation in respect of loans, credit facilities, bank advances, discounting, the issue or subscription of any form of bond or security, such default shall also constitute default on the loan in question, triggering immediate repayment.



## 23. Employee benefits – € 122.3 million

Terna provides benefits to its employees during their period of employment (loyalty bonus), at the termination of their employment (termination benefits, additional month's pay and indemnity for lack of notice), and in the period after the termination of employment (electricity discount and the ASEM health plan).

The loyalty bonus is awarded to employees and managers of the Company when they reach certain seniority levels (25 and 35 years of service).

The benefits granted at the termination of employment are recognised for all employees (termination benefits), managers hired or appointed before 28 February 1999 (indemnity for lack of notice), and employees (production workers, office staff and junior managers) hired before 24 July 2001 (additional month's pay indemnity).

Post-employment benefits consist of the following:

- discount on electrical energy consumed for domestic use. This benefit is offered to all employees hired before 30 June 1996 (electricity discount);
- a healthcare plan complementing the national health service, as agreed under the terms of the national contract for industrial managers (the ASEM health plan).

The composition of termination benefits and other employee-related provisions at 31 December 2010 is detailed below along with changes in the period:

| In millions of euros                                   | 31 Dec. 2009 | Provision   | Interest cost | Utilisations and other changes | 31 Dec. 2010 |
|--|--------------|-------------|---------------|--------------------------------|--------------|
| <b>Benefits payable to employees</b>                   |              |             |               |                                |              |
| Loyalty bonus  | 4.9          | 0.0         | 0.2           | -0.9                           | 4.2          |
| <b>Total</b>   | <b>4.9</b>   | <b>0.0</b>  | <b>0.2</b>    | <b>-0.9</b>                    | <b>4.2</b>   |
| <b>Benefits payable upon termination of employment</b> |              |             |               |                                |              |
| Termination benefits                                   | 71.5         | 11.0        | 2.6           | -17.2                          | 67.9         |
| Additional months' pay                                 | 7.3          | 0.4         | 0.2           | -1.2                           | 6.7          |
| Indemnities for lack of notice and similar             | 3.3          | 0.0         | 0.1           | -0.4                           | 3.0          |
| <b>Total</b>   | <b>82.1</b>  | <b>11.4</b> | <b>2.9</b>    | <b>-18.8</b>                   | <b>77.6</b>  |
| <b>Post-employment benefits</b>                        |              |             |               |                                |              |
| Energy discount  | 26.7         | 1.4         | 1.5           | -0.3                           | 29.3         |
| ASEM   | 11.4         | 0.0         | 0.3           | -0.5                           | 11.2         |
| <b>Total</b>   | <b>38.1</b>  | <b>1.4</b>  | <b>1.8</b>    | <b>-0.8</b>                    | <b>40.5</b>  |
| <b>Total</b>   | <b>125.1</b> | <b>12.8</b> | <b>4.9</b>    | <b>-20.5</b>                   | <b>122.3</b> |

The item, equal to € 122.3 million at 31 December 2010 (€ 125.1 million at 31 December 2009), decreased by € 2.8 million on the previous year, due to the utilisations of the year (€ 20.5 million), partially offset by the allocations and the recognition of the discounting charge for the period (€ 17.7 million in total).

Costs for liabilities in respect of employee benefits recognised in the income statement break down as follows:

| In millions of euros    | Termination benefits | Indemnities for lack of notice and similar | Additional months' pay | Loyalty bonus | ASEM        | Energy discount | Total        |
|-------------------------|----------------------|--|------------------------|---------------|-------------|-----------------|--------------|
| <b>31 December 2009</b> | <b>71.5</b>          | <b>3.3</b>                                 | <b>7.3</b>             | <b>4.9</b>    | <b>11.4</b> | <b>26.7</b>     | <b>125.1</b> |
| Provision               | 11.0                 | 0.0  | 0.4                    | 0.0           | 0.0         | 1.4             | 12.8         |
| Financial expense       | 2.6                  | 0.1  | 0.2                    | 0.2           | 0.3         | 1.5             | 4.9          |
| Payments and transfers  | -17.2                | -0.4                                       | -1.2                   | -0.9          | -0.5        | -0.3            | -20.5        |
| <b>31 December 2010</b> | <b>67.9</b>          | <b>3.0</b>                                 | <b>6.7</b>             | <b>4.2</b>    | <b>11.2</b> | <b>29.3</b>     | <b>122.3</b> |

The main assumptions made in the actuarial estimate of employee benefit obligations are as follows:

| Percentage figures                    | 2010        | 2009        |
|---------------------------------------|-------------|-------------|
| Discount rate                         | 4.1%        | 4.1%        |
| Rate of increase in personnel expense | 2.0% - 4.0% | 2.0% - 4.0% |
| Rate of increase in healthcare costs  | 3.0%        | 3.0%        |

## 24. Provisions for risks and charges – € 165.0 million

The items and changes of the provisions for risks and charges at 31 December 2010 are set out below:

| In millions of euros           | Provision for disputes and litigation | Provisions for other risks and charges | Provision for early retirement incentives | Total        |
|--------------------------------|---------------------------------------|--|---|--------------|
| <b>31 December 2009</b>        | <b>14.6</b>                           | <b>121.1</b>                           | <b>12.2</b>                               | <b>147.9</b> |
| Provision                      | 0.9                                   | 42.1                                   | 2.2                                       | 45.2         |
| Utilisations and other changes | -0.2                                  | -26.5                                  | -1.4                                      | -28.1        |
| <b>31 December 2010</b>        | <b>15.3</b>                           | <b>136.7</b>                           | <b>13.0</b>                               | <b>165.0</b> |

### Provision for disputes and litigation – € 15.3 million

The provision is accrued to cover the liabilities at year end that may arise from lawsuits and out-of-court disputes relating to Company activities. The amount accrued takes into account the opinions both of internal and external legal counsel. Compared with the previous year, the caption shows a slight increase of € 0.7 million. Litigation for which no potential charge can reasonably be calculated are described under “Commitments and risks”.

### Provision for other risks and charges – € 136.7 million

The provision shows a net increase of € 15.6 million compared with last year, ascribable to accruals of € 42.1 million and utilisations of -€ 26.5 million in the course of the year. More specifically:

- a net accrual of € 10.2 million relating to “Projects for urban and environmental renewal”, the aim of which is to offset the environmental impact of the construction of power lines;
- a net accrual of € 1.5 million for incentive plans for management personnel and social security disputes with INPS;
- net utilisations (€ 1.9 million) for charges which are payable to distributing companies for power failures of the transformation plants linked to the NTG (in accordance with Resolution 341/07 – € 0.6 million) as well as for the sharing of indemnities due to final users (€ 0.3 million) in addition to the issue of allocations implemented in the previous year for the contribution that is payable to the Exceptional Events Fund. The latter is part of the Compensation Fund of the Electrical Sector established by Resolution 333/07 for power failure events (€ 2.8 million);
- an exchange rate adjustment (€ 5.6 million) of the provisions allocated in 2009 for probable charges in respect of contractual and tax obligations related to the disposal of the controlling stake in Terna Participações.

### Provision for early retirement incentives – € 13.0 million

This provision reflects the estimated non-recurring charges related to the voluntary early termination of the working relationship of employees who are eligible for retirement. The caption shows substantially no change on the previous year.

## 25. Deferred tax liabilities – € 248.9 million

The changes in this provision are analysed below:

|  | 31 Dec. 2009 | Impact recognised<br>in profit or loss |              | Impact recognised<br>in equity | 31 Dec. 2010 |
|--|--------------|--|--------------|--------------------------------|--------------|
| In millions of euros                           |              | Provisions                             | Utilisations |                                |              |
| <b>Deferred tax liabilities</b>                |              |  |              |                                |              |
| Property, plant and equipment                  | 334.6        | 0.0                                    | -36.1        | 0.0                            | 298.5        |
| Employee benefits<br>and financial instruments | 3.5          | 0.0                                    | 0.0          | 0.0                            | 3.5          |
| <b>Total deferred tax liabilities</b>          | <b>338.1</b> | <b>0.0</b>                             | <b>-36.1</b> | <b>0.0</b>                     | <b>302.0</b> |
| <b>Deferred tax assets</b>                     |              |  |              |                                |              |
| Provisions for risks and charges               | 14.5         | 3.8                                    | -4.1         | 0.0                            | 14.2         |
| Allowance for impairment                       | 3.1          | 0.0                                    | 0.0          | 0.0                            | 3.1          |
| Employee benefits                              | 21.5         | 8.4                                    | -7.0         | 0.0                            | 22.9         |
| FVH - CHF derivatives                          | 22.7         | 0.0                                    | 0.0          | -9.8                           | 12.9         |
| <b>Total deferred tax assets</b>               | <b>61.8</b>  | <b>12.2</b>                            | <b>-11.1</b> | <b>-9.8</b>                    | <b>53.1</b>  |
| <b>Net deferred tax liabilities</b>            | <b>276.3</b> | <b>-12.2</b>                           | <b>-25.0</b> | <b>9.8</b>                     | <b>248.9</b> |

This balance, € 248.9 million, reflects the net movements in the Company's deferred tax assets and liabilities.

Deferred tax liabilities totalled € 302.0 million, down € 36.1 million, essentially due to:

- the use of previous provisions to cover the difference between accelerated amortisation/depreciation and the depreciation calculated using ordinary technical rates (€ 27.4 million), including the reversal in respect of the amortisation/depreciation charge for the period attributable to the difference from merger eliminations allocated to property, plant and equipment following mergers carried out in previous years (€ 1.7 million);
- release of the period element (€ 8.7 million) of the provision for deferred IRAP liabilities governed by Law no. 244 dated 24 December 2007 (the 2008 Finance Law), recorded in prior years in relation to accelerated depreciation.

Deferred tax assets came to € 53.1 million, a decrease of € 8.7 million, mainly attributable to the following changes:

- provisions of € 9.8 million, attributable to the tax effect, which has no impact on the income statement, in respect of changes in cash flow hedge instruments;
- net allocation of € 1.4 million relative to movements in provisions for employee benefits;
- a decrease of € 0.3 million in net utilisations of the year to the provisions for risks and charges.

## 26. Other non-current liabilities – € 136.6 million

This item (€ 136.6 million at 31 December 2010) reports the deferred portion of grants related to assets (€ 134.3 million) as well as the deferred portion of grid transmission fees of the Company remunerating future costs in respect of the safety plan for the NTG (€ 2.3 million).

The decrease of € 15.0 million in the item with respect to the previous year regards:

- the release, in the amount of € 6.2 million, of the portions of grants related to assets in connection with depreciation for the year applicable to the plants involved;
- the recognition, in the amount of € 8.8 million, of the accrued portion of the grid transmission fees to cover the costs of the year of the National Transmission Grid safety plan, essentially due to the adjustment of the useful life of the intangible assets at the rates specified by the AEEG for rate purposes.

## 27. Current liabilities

Current liabilities are analysed as follows at 31 December 2010:

| In millions of euros                   | 31 Dec. 2010   | 31 Dec. 2009   | Change       |
|--|----------------|----------------|--------------|
| Short-term loans (*)                   | 73.1           | 42.7           | 30.4         |
| Current portion of long-term loans (*) | 59.7           | 59.7           | 0.0          |
| Trade payables                         | 1,552.8        | 1,487.6        | 65.2         |
| Tax liabilities                        | 69.1           | 20.8           | 48.3         |
| Current financial liabilities (*)      | 24.2           | 25.5           | -1.3         |
| Other current liabilities              | 133.2          | 95.4           | 37.8         |
| <b>Total</b>                           | <b>1,912.1</b> | <b>1,731.7</b> | <b>180.4</b> |

(\*) See the comments in note 22. "Loans and financial liabilities".

### Trade payables – € 1,552.8 million

Trade payables are analysed as follows at 31 December 2010:

| In millions of euros                   | 31 Dec. 2010   | 31 Dec. 2009   | Change      |
|--|----------------|----------------|-------------|
| Suppliers:                             |                |                |             |
| - Energy-related payables              | 1,068.5        | 1,100.7        | -32.2       |
| - Non energy-related payables          | 455.1          | 363.5          | 91.6        |
| Associates:                            | 5.0            | 8.0            | -3.0        |
| - Subsidiaries                         | 22.2           | 15.0           | 7.2         |
| Payables for contract work in progress | 2.0            | 0.4            | 1.6         |
| <b>Total trade payables</b>            | <b>1,552.8</b> | <b>1,487.6</b> | <b>65.2</b> |

### Suppliers

#### Energy-related payables

This item reports the effects on the balance sheet of payables for "pass-through" costs not ascribable to the Company, and refers mostly to purchase of energy relative to dispatching activities and the transport fee due to the owners of other sections of the National Transmission Grid.

The decrease of € 32.2 million compared with the previous year is essentially attributed to the net effect of:

- decreased payables (€ 39.0 million) relative to "pass-through items" which are primarily ascribable to the joint effect of:
  - the decrease of payables for the acquisition of electrical energy outside of the power exchange (€ 122.7 million) which is essentially due to the lower balance of net payables for capacity payment (€ 54 million), the decrease in debt items awaiting definition on the part of the AEEG – in particular the availability of productive capacity (PC), totalling € 27.5 million – as well as the reduction in payables for the essential units for safety of the electrical system (EUSES), totalling € 32.7 million;
  - the increase of payables for the acquisition of electrical energy within the power exchange (€ 83.7 million) which is essentially due to virtual interconnection activities (€ 121.1 million) and the dispatching of electrical energy produced by non-programmable renewable resources pursuant to Resolution ARG/elt 5/10 (Euro 17.9 million) as well as the increase in volumes of resources attained from the energy market (€ 14.9 million); these were partly compensated by the decreased payables generated from the reduction of quantities and the reduction in valuation prices of the imbalance as well as the advance invoicing of balances required by Resolution AEEG 34/09 (€ 66.6 million);
- booking of payables not ascribable to the parent company (€ 6.8 million) due to the Compensation Fund for the Electrical Sector and relative to charges payable to the Exceptional Events Fund for power failures which occurred during the year (€ 2.0 million), in accordance with Resolution 333/07 and its subsequent amendments as well as the reimbursement of the grid transmission fees balance for 2008 (€ 4.8 million) which was partially compensated by the receivable booked by the Company for the same amount, as described in the paragraph relative to "Receivables for grid transmission fees" under trade receivables.

### Non energy-related payables

Amounts due to suppliers refer to invoices both already received and yet to be received for tenders, services and the purchase of materials and equipment.

The increase on last year (€ 91.6 million) is basically due to purchases and services for the greater investments made during the last quarter of the period, mainly linked to Pole 2 of SA.PE.I., as compared with the last quarter of 2009.

### Payables to subsidiaries

The increase in the item, equal to € 7.2 million, is mainly due to the greater amount owing to the subsidiary TELAT (€ 6.7 million) for the portion of NTG relating to December, by virtue of the tariff adjustments and the extension of the scope of grid coverage (€ 1.4 million) in addition to the recording of the payable on the portion of NTG owned by the subsidiary linked to the mitigation mechanism (€ 5.3 million) established by ARG/elt Resolution 188/08.

### Payables to associates

This item amounts to € 5.0 million and relates to payables to CESI for services provided to the Company in the construction and management of laboratories and plants for tests, inspections, studies and experimental research in the general field of electricity technology and scientific progress. The decrease (€ 3.0 million) compared with 31 December 2009 is the result of an increase in services delivered in the final part of the year.

Company commitments with suppliers totalled about € 2,138.7 million and refer to purchase commitments relating to normal operating activities for the period 2011-2016.

### Payables for contract work in progress

This caption amounted to € 2.0 million at 31 December 2010 and was substantially in line with the balance at 31 December 2009 with an increase of € 1.6 million. It is composed as follows:

| In millions of euros | Payments on account | Contract value | Balance at 31 Dec. 2010 | Payments on account | Contract value | Balance at 31 Dec. 2009 |
|----------------------|---------------------|----------------|-------------------------|---------------------|----------------|-------------------------|
| Other                | -23.2               | 21.2           | -2.0                    | -3.0                | 2.6            | -0.4                    |
| <b>Total</b>         | <b>-23.2</b>        | <b>21.2</b>    | <b>-2.0</b>             | <b>-3.0</b>         | <b>2.6</b>     | <b>-0.4</b>             |

### Tax liabilities – € 69.1 million

The caption refers to the Company's tax liabilities for IRES and IRAP taxes for the financial year. It records an increase of € 48.3 million for the lesser payable recorded during last year.

### Other current liabilities – € 133.2 million

Other current liabilities are analysed as follows:

| In millions of euros                     | 31 Dec. 2010 | Due within one year | Due beyond one year | 31 Dec. 2009 | Change      |
|--|--------------|---------------------|---------------------|--------------|-------------|
| Payments on account                      | 29.3         | 1.9                 | 27.4                | 9.1          | 20.2        |
| Other tax liabilities                    | 6.0          | 6.0                 | -                   | 7.1          | -1.1        |
| Payables to social security institutions | 22.4         | 22.4                | -                   | 23.6         | -1.2        |
| Payables to employees                    | 38.9         | 38.9                | -                   | 36.3         | 2.6         |
| Other payables:                          |              |                     |                     |              |             |
| - Third parties                          | 36.2         | 3.7                 | 32.5                | 18.4         | 17.8        |
| - Subsidiaries                           | 0.4          | 0.4                 | -                   | 0.9          | -0.5        |
| <b>Total</b>                             | <b>133.2</b> | <b>73.3</b>         | <b>59.9</b>         | <b>95.4</b>  | <b>37.8</b> |

### Payments on account

This caption (€ 29.3 million) reflects the grant related to assets collected by the Company in relation to assets under construction at 31 December 2010.

Compared to the 2009 carrying amount (€ 9.1 million), there is a net increase of € 20.2 million, mainly due to the net effect of new payments on account for € 32.5 million and a decrease of € 12.3 million in the grants reducing the carrying amount of assets entered in service during the period; in particular there are advances received in accordance with the mandate contract for the design of interconnection networks with abroad (€ 15.6 million, in accordance with ARG/elt 179/09 Resolution and its subsequent amendments).

### Other tax liabilities

Other tax liabilities, amounting to € 6.0 million record a € 1.1 million drop on last year, mainly due to the reduction of payables for withholdings recorded by the Company as tax substitute.

### Payables to social security institutions

This caption amounts to € 22.4 million (€ 23.6 million at 31 December 2009); the item also reports the payable in respect of the Fondo Previdenza Elettrici (F.P.E., a complementary pension fund for the electricity industry), equal to € 4.9 million.

### Payables to employees

Payables to employees came to € 38.9 million (€ 36.3 million at 31 December 2009) and essentially refer to:

- accruals made for staff incentives to be paid the following year (€ 25.8 million);
- payments due to employees for unused holiday time and abolished public holidays (€ 8.7 million);
- termination indemnities due to employees whose employment was terminated before 31 December 2009 (€ 2.6 million).

### Other payables to third parties

Other payables, equal to € 36.6 million (€ 19.3 million at 31 December 2009), mainly regard security deposits (€ 32.5 million) received from electricity market operators securing their obligations in respect of dispatching contracts. This item reports an increase of € 17.3 million which is essentially attributable to caution money provided as a guarantee of contractual obligations (+€ 17.4 million) in connection with dispatching and virtual interconnection contracts.

## E. Commitments and risks

### Risk management

#### Risk management - Terna S.p.A.

In the conduct of its operations, Terna is exposed to various financial risks: market risk (namely exchange rate risk, interest rate risk and inflation risk), liquidity risk and credit risk.

This section provides comprehensive information regarding Terna's exposure to all the above risks, along with a presentation of the objectives, policies and processes for managing those risks and the methods used to measure them, with further quantitative disclosures concerning the 2010 financial statements.

The risk management policies adopted by Terna seek to identify, analyse and monitor the risks to which the Company is exposed, establishing appropriate limits and controls, and checking compliance with such limits. These policies and related systems are revised on a regular basis in order to reflect any changes in market conditions and the Company's activities. As a part of the financial risk management policies approved by the Board of Directors, Terna has established the responsibilities and operating procedures for financial risk management, specifically as concerns the instruments to be used and the precise operating limits in managing them.

#### Market risks

Market risk is the risk that the fair value or future cash flows of a financial instrument may fluctuate as a result of changes in financial market conditions. Market risks comprise three forms of risk: exchange rate risk, interest rate risk and inflation risk.

Risk management must be performed with the objective of maximising financial income and minimising the related risks by selecting counterparties and instruments compatible with the corporate risk management policy. Speculative activity is not envisaged in the corporate mission.

Terna S.p.A. seeks to adopt a dynamic approach to financial risk management. This approach is characterised by risk aversion, aiming at minimising risk through continuous monitoring of financial markets in order to plan hedging transactions in favourable market conditions. The dynamic approach makes it possible to take action to improve existing hedges where changes in market conditions or in the hedged item make the latter unsuitable or excessively expensive. The concept of hedging transaction is not restricted to those hedges that qualify for hedge accounting, but rather encompasses the objective of total or partial hedging of the income statement or statement of financial position item from interest rate risk. 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 fair value of financial derivatives reflects the estimated amount that Terna would pay or receive in order to extinguish contracts at the closing date.

The fair value of instruments is determined in accordance with the fair value hierarchy envisaged under IFRS 7 (Level 2)

by means of appropriate valuation techniques for each category of financial instrument, using market data as at the closing date (such as interest rates, exchange rates, volatility) and discounting projected cash flows on the basis of the market yield curve and inflation at the reporting date.

The financial assets and liabilities in respect of derivative instruments in place during the year can be classified as:

- cash flow hedge derivatives, essentially related to hedging the risk of changes in the cash flows associated with long-term floating-rate loans;
- fair value hedge derivatives, essentially related to hedging the exposure to changes in the fair value of a financial asset or liability associated with fluctuations in interest rates (fixed-rate bonds).

### Interest rate risk

Interest rate risk is represented by the uncertainty associated with interest rate fluctuations. This is the risk that a change in market rates may produce effects on the fair value or future cash flows of financial instruments. It is the risk that movements in interest rates that could have an impact on the fair value or future cash flows of financial instruments.

In conducting its operations, Terna is exposed to the risk of fluctuations in interest rates. Its main source of interest rate risk is associated with items of net financial debt and the related hedging positions in derivative instruments that generate financial expense. Terna's borrowing strategy focuses on long-term loans whose term reflects the useful life of company assets. It pursues an interest rate risk hedging policy that aims to reconcile this approach with the regulatory framework, which every four years establishes the cost of debt as part of the formula to set the return on the Regulatory Asset Base (RAB).

Accordingly, the hedging instruments used, at various maturity dates, include both derivatives that transform fixed rates into floating rates and derivatives that transform floating rates into fixed rates.

In order to reduce the amount of financial debt exposed to the risk of fluctuations in interest rates and to optimise the temporal correlation between average cost of debt and regulatory rate used in the WACC formula, various types of plain vanilla derivatives are used, such as interest rate swaps and interest rate collars.

Interest rate swaps are used in order to reduce the volume of debt exposed to fluctuations in interest rates and to reduce the volatility of borrowing costs. With an interest rate swap, Terna agrees with a counterparty to exchange, at specific intervals, the floating-rate cash flows on a specified notional amount against the fixed-rate (agreed between the parties) cash flows, or vice versa.

Interest rate collars are used to lower the impact of the volatility of interest rates on the cost of the debt. They are considered appropriate in times of uncertainty about future developments in interest rates.

The following table shows the financial instruments entered into by Terna, classified according to the type of interest rate (fixed or floating):

| In millions of euros                | Carrying amount |                | Change         |
|-------------------------------------|-----------------|----------------|----------------|
|                                     | 31 Dec. 2010    | 31 Dec. 2009   |                |
| Fixed-rate financial instruments    |                 |                |                |
| - assets                            | 0.0             | 0.0            | 0.0            |
| - liabilities                       | 2,775.3         | 2,726.1        | 49.2           |
| Floating-rate financial instruments |                 |                |                |
| - assets                            | 869.0           | 1,130.9        | -261.9         |
| - liabilities                       | 2,552.1         | 1,665.7        | 886.4          |
| <b>Total</b>                        | <b>4,458.4</b>  | <b>3,260.9</b> | <b>1,197.5</b> |



### Sensitivity to interest rate risk

As regards the management of interest rate risk, Terna has, on the one hand, entered into fixed-to-floating interest rate swaps (FVH) to hedge the fair value of the fixed-rate risk bonds and, on the other, floating-to-fixed interest rate swaps (CFH) to hedge the expected cash flows in respect of all other floating-rate debt.

Since the hedging relationship between the derivative and the hedged item is formally documented and the effectiveness of the hedge, as verified initially and periodically over its life, is high (between 80% and 125%), the Company has elected to use hedge accounting to ensure the perfect temporal matching of the hedge and the hedged item. The aim of hedge accounting is to recognise the effects of the hedges and the hedged items in the income statement at the same time. Accordingly, for FVH derivatives, any changes in the fair value of the hedged item attributable to the risk being hedged must be booked in the income statement, thereby offsetting the changes in the fair value of the derivative booked in the income statement. For CFH derivatives, the changes in the fair value of the derivative must be booked under equity (recognising any ineffective portion of the hedge directly in the income statement) and then reversed through the income statement in the same period in which the cash flows of the hedged instrument materialise. The characteristics of the CFH derivatives mirror those of the hedged underlying, so the related cash flows will materialise at the same maturities as the interest on the debt, with no impact of the changes in fair value on profit or loss.

The following table reports the amounts booked in the income statement and equity for positions that are sensitive to changes in interest rates, the theoretical value of the positions following a positive or negative shift in the yield curve and the differential impact booked in the income statement and equity of such changes. A hypothetical 10% variation in interest rates with respect to market interest rates at the reporting date has been assumed:

| In millions of euros   | Profit or loss        |               |                       | Equity                |               |                       |
|--|-----------------------|---------------|-----------------------|-----------------------|---------------|-----------------------|
|  | Current rates<br>+10% | Current rates | Current rates<br>-10% | Current rates<br>+10% | Current rates | Current rates<br>-10% |
| <b>31 December 2010</b>  |                       |               |                       |                       |               |                       |
| Positions sensitive to interest rate variations<br>(FVH, Bonds, CFH) | 2.9                   | 2.2           | 1.7                   | -44.5                 | -47.1         | -49.9                 |
| <i>Hypothetical change</i>   | 0.7                   | -             | -0.5                  | 2.6                   | -             | -2.8                  |
| <b>31 December 2009</b>  |                       |               |                       |                       |               |                       |
| Positions sensitive to interest rate variations<br>(FVH, Bonds, CFH) | 1.6                   | 1.2           | 0.8                   | -76.8                 | -82.6         | -88.3                 |
| <i>Hypothetical change</i>   | 0.4                   | -             | -0.4                  | 5.7                   | -             | -5.8                  |

### Inflation risk

As regards inflation rate risk, the rates established by regulators to remunerate Terna S.p.A.'s activities are determined so as to allow coverage of the sector's recognised costs. Such cost components are updated on an annual basis to consider the accrued impact of inflation. In 2007, the Company used an inflation-linked bond issue to obtain an effective hedge of profit for the year; any decrease in expected revenue due to a decrease in the inflation rate would be offset by lower financial expense.

### Exchange rate risk

Generally Terna hedges exchange rate risk through the forward sale or purchase of currencies (forward contracts) or the use of options. Currency options give Terna the right or the obligation to buy or sell predetermined amounts of a currency at a specific exchange rate at the end of a specific period of time. Normally, both forward contracts and options have maturities of no more than 12 months.

Such contracts have a notional amount and maturity date less than or equal to that of the underlying financial liability, or the expected cash flows, so that any change in the fair value and/or estimated cash flows deriving from an appreciation or depreciation of the euro against other currencies is fully offset by a corresponding change in the fair value and/or estimated cash flows of the underlying position.

At 31 December 2010 (as at 31 December 2009), no financial instruments exposed to exchange rate risk were present.

### Liquidity risk

The liquidity risk is the risk Terna might encounter difficulty in discharging its obligations in respect of its financial liabilities and operational cycle. Liquidity risk management seeks to ensure adequate coverage of financial needs by obtaining adequate lines of credit and appropriate management of any surplus liquidity. As of 31 December 2010 Terna had € 1,000 million in medium-term credit lines and € 697.6 million in short-term credit lines. Such amount is sufficient to refinance the debt falling due discussed in the section on long-term loans (€ 59.7 million).

### Credit risk

Credit risk is the risk a customer or one of the counterparties to a transaction in financial instruments could cause a financial loss by failing to discharge an obligation. It is mainly generated by trade receivables and the financial investments of the Company.

The credit risk originated by open positions on transactions in financial derivatives is considered to be marginal since the counterparties, in compliance with financial risk management policies, are leading international credit institutions with high ratings and such transactions are diversified in compliance with specific concentration limits.

Terna provides its services to counterparties considered solvent by the market, who therefore have a high credit standing, and does not have highly concentrated credit risk.

Credit risk management is guided by the provisions of AEEG Resolution no. 111/06, which, in art. 49, introduced instruments for the limitation of risks related to the insolvency of dispatching customers, both on a preventive basis and in the event of actual insolvency. In particular, the Resolution establishes three instruments to safeguard the electricity market: a guarantee system (bank guarantees provided by individual dispatching customers, based on their revenue), the option of terminating dispatching contracts (in the event of insolvency or failure to replace enforced guarantees) and, finally, the possibility of recovering uncollected debts, after having taken all other possible collection actions, through a specific fee defined by the Authority.

The following table summarises the exposure to such risk as at the reporting date:

| In millions of euros                              | Carrying amount |                | Change       |
|---|-----------------|----------------|--------------|
|   | 31 Dec. 2010    | 31 Dec. 2009   |              |
| FVH derivatives                                   | 200.3           | 123.2          | 77.1         |
| TELAT loan  | 500.0           | 500.0          | 0.0          |
| Net current a/c position of intercompany treasury | 18.6            | 0.0            | 18.6         |
| Cash and cash equivalents                         | 150.1           | 0.1            | 150.0        |
| Trade receivables                                 | 1,495.6         | 1,177.1        | 318.5        |
| <b>Total</b>                                      | <b>2,364.6</b>  | <b>1,800.4</b> | <b>564.2</b> |

The total value of the exposure to credit rate risk at 31 December 2010 is represented by the carrying amount of financial assets (current and non current), trade receivables and cash and cash equivalents.

The following tables provide qualitative information on customer receivables that are not past due and have no impairment:

#### GEOGRAPHICAL DISTRIBUTION

| In millions of euros | Carrying amount |                |
|----------------------|-----------------|----------------|
|                      | 2010            | 2009           |
| Italy                | 1,482.6         | 1,165.9        |
| Euro-area countries  | 8.9             | 10.1           |
| Other countries      | 4.1             | 1.1            |
| <b>Total</b>         | <b>1,495.6</b>  | <b>1,177.1</b> |

#### CUSTOMER TYPOLOGY

| In millions of euros   | Carrying amount |                |
|--|-----------------|----------------|
|  | 2010            | 2009           |
| Distributors <sup>(*)</sup>  | 243.9           | 209.4          |
| Electricity Equalisation Fund <sup>(**)</sup>  | 71.7            | 88.9           |
| Input dispatching contractors  | 310.2           | 380.5          |
| Withdrawal dispatching contractors (non distributors)  | 765.3           | 455.1          |
| Parties which have undersigned virtual import contracts and virtual import services (interconnectors and shippers) | 35.2            | -              |
| Receivables from unregulated activities  | 69.3            | 43.2           |
| <b>Total</b>   | <b>1,495.6</b>  | <b>1,177.1</b> |

(\*) Includes receivable accrued in respect of TELAT grid transmission fees;  
 (\*\*) of which € 45.1 million from volume effect on grid transmission fees.

The following table breaks down customer receivables by age, reporting any potential impairment losses:

| In millions of euros        | 2010                     |                | 2009                     |                |
|-----------------------------|--------------------------|----------------|--------------------------|----------------|
|                             | Allowance for impairment | Gross          | Allowance for impairment | Gross          |
| Not yet past due            | -                        | 1,430.9        | -2.0                     | 1,134.3        |
| 0-30 days past due          | -                        | 38.5           | -                        | 18.6           |
| 31-120 days past due        | -                        | 3.5            | -0.6                     | 15.6           |
| More than 120 days past due | -23.5                    | 46.2           | -24.4                    | 35.6           |
| <b>Total</b>                | <b>-23.5</b>             | <b>1,519.1</b> | <b>-27.0</b>             | <b>1,204.1</b> |

Changes in the allowance for impairment in the course of the year were as follows:

| In millions of euros          | 2010         | 2009       |
|-------------------------------|--------------|------------|
| Balance at 1 January          | -27.0        | -11.7      |
| Reversal of provision         | 3.5          | -          |
| Impairment for the year       | -            | -15.3      |
| <b>Balance at 31 December</b> | <b>-23.5</b> | <b>-27</b> |

The value of guarantees received from eligible electricity market customers is illustrated below:

| In millions of euros                  | 2010           | 2009           |
|---------------------------------------|----------------|----------------|
| Input dispatching activity            | 220.5          | 251.3          |
| Withdrawal dispatching activity       | 831.3          | 851.3          |
| Grid transmission fees - distributors | 173.7          | 172.3          |
| Virtual importing                     | 338.0          | -              |
| <b>Balance at 31 December</b>         | <b>1,563.5</b> | <b>1,274.9</b> |

### Default risk and debt covenants

This risk is associated with the possibility that the loan contracts or bond rules to which the Company is party may contain provisions authorising counterparties to call in such loans immediately upon the occurrence of certain events, thereby generating liquidity risk. For more information on the contractual provisions of outstanding loans at 31 December 10, please see the section “Loans and financial liabilities” in the notes to the separate financial statements of Terna S.p.A.

## Legal disputes

The main off-balance sheet commitments and contingencies of Terna S.p.A. at 31 December 2010 are as follows.

### Environmental and urban planning litigation

Environmental litigation originates from the installation and operation of electrical plants and primarily involves damages which could be derived from exposure to electrical and magnetic fields that are generated by power lines. The Company is involved in various civil and administrative suits requesting the transfer or change in operations of allegedly-harmful power lines, even though they were installed in full compliance with applicable legislation (Law no. 36 of 22 February 2001 and D.P.C.M. of 8 July 2003). Only a very small number of cases include claims for damages for harm to health caused by electromagnetic fields.

Only in a few cases have adverse judgements been issued against the companies. These have been appealed and the appeals are still pending, although adverse rulings are considered unlikely.

In addition, a number of cases relating to urban planning and environmental issues are pending in respect of the construction and operation of certain transmission lines. The possible effects of any unfavourable outcome to these cases are unpredictable and, accordingly, have not been considered when determining the “Provision for disputes and other contingencies”.

In a limited number of cases, the possibility of an adverse outcome cannot be entirely ruled out. The possible consequences could, in addition to the award of damages, include, inter alia, the costs of modifying lines and the temporary suspension of their use. In any case, any unfavourable outcome would not jeopardise line operations.

Examination of the above litigation, having regard for the information provided by the external legal consultants, suggests that the likelihood of adverse outcomes is remote.

### Litigation concerning concession activities

Given that it has been the licensee for transmission and dispatching activities since 1 November 2005, the Company has been involved in a number of cases appealing AEEG, MED and/or Terna measures relating to activities operated under the license. Only in those cases in which the plaintiffs not only claim defects in the measures, but also allege that Terna violated the rules established by such Authorities has the Company appeared in court. Within the scope of this litigation, although a number of cases have seen the Resolutions of AEEG struck down in the first and/or second-level court, together with the consequent measures adopted by Terna, it is felt that there is little risk of adverse outcomes for Terna, since the matters generally regard pass-through items. This position is supported by the information provided by the external legal counsel representing the Company in the cases involved. As the licensee for transmission and dispatching activities, the measures taken by the Company when applying the Resolutions adopted by the Authority are sometimes the subject of challenges. In appropriate circumstances, the economic costs of such challenges may be borne by the Authority.

## F. Business combinations

No business combinations were carried out in 2010.

## G. Related party transactions

Terna's transactions with related parties, taking account of the de facto control exercised over the Company by Cassa Depositi e Prestiti S.p.A. first ascertained in 2007, regarded – in addition to the subsidiaries (TELAT, SunTergrid, RTS and the companies held for sale, RTR and Valmontone) – the associate company CESI, the employee pension funds (FondeneI and Fopen), Cassa Depositi e Prestiti as well as companies belonging to:

- the GSE Group;
  - the Enel Group;
  - the Eni Group;
  - the Ferrovie dello Stato Group;
- and those with ANAS S.p.A.

Related party transactions in 2010 are mainly services that are part of core business and regulated by market conditions. More specifically, Terna supplies the operative management of all subsidiaries through specific Management fee contracts, which not only ensure administrative and financial coordination, but also coordination of institutional relations, giving it the option of acting, for and on behalf of the subsidiaries. With the subsidiary TELAT, there is also an “Electrical service agreement in relation to power lines” in place for the management and maintenance of HV lines.

Terna is also involved in the management of cash demands of subsidiaries through specific Treasury contracts that ensure the guidance and coordination of all transactions in relation to financial resource and needs management and treasury service, as well as the implementation of all related transactions. Under the scope of the centralised management of financial resources, we note two loans, each for € 500.0 million, supplied by Terna to the subsidiaries TELAT (in November 2009) and RTR <sup>(1)</sup> (on 8 September 2010).

The following are the contractual terms and conditions of the financial transactions in place with subsidiaries:

|   |                         | Contractual conditions - interest rates    |   |
|---|-------------------------|--|---|
|   |                         | intercompany current a/c                   |   |
|   | Loan                    | Inventories                                | Utilisations                              |
| <b>TELAT S.r.l.</b>   | Euribor 6 months +2.50% | Euribor monthly average<br>1 month -0.50%  | Euribor monthly average<br>1 month +1.00% |
| <b>SunTergrid S.p.A.</b>                                      | -                       | Euribor monthly average<br>1 month -0.50%  | Euribor monthly average<br>1 month +1.00% |
| <b>RTS S.r.l.</b>   | -                       | Euribor monthly average<br>1 month -0.50%  | Euribor monthly average<br>1 month +1.00% |
| <b>Assets held for sale<br/>(RTR S.r.l, Valmontone S.r.l)</b> | Euribor 6 months +1.70% | Euribor monthly average<br>6 months +1.70% | Euribor monthly average<br>1 month +1.00% |

The tables below specify the nature of the transactions implemented by the Company with related parties and, following on from this, the respective income and expense totalled during the period, in addition to the respective receivables and payables in place as of 31 December 2010:

(1) On 28 January 2011, the company RTR, in view of the sale, signed a refinancing contract for a total maximum amount of € 593.8 million. This aimed to refinance the investments sustained to develop the photovoltaic plant portfolio, on the basis of a project financing non recourse.

| Related party                                    | Revenue transactions  | Cost transactions  |
|--|---|--|
| <b>TELAT</b>                                     | <b>NTG transmission fees</b><br>NTG transmission fees.<br><br><b>Non energy-related items</b><br>Technical services and line maintenance, supply of management fee, treasury services, loan.  | <b>NTG transmission fees</b><br>Network remuneration.<br><br><b>Non energy-related items</b><br>Purchase of transmission plants.   |
| <b>Suntergrid and RTS</b>                        | <b>Non energy-related items</b><br>Treasury services for the development of photovoltaic plants, management fees, land leasing.   | <b>Non energy-related items</b><br>Treasury services.  |
| <b>Assets held for sale (RTR and Valmontone)</b> | <b>Non energy-related items</b><br>Treasury services for the development of photovoltaic plants, management fees, sale of photovoltaic panels, loans.   | <b>Non energy-related items</b><br>Treasury services   |
| <b>Cassa Depositi e Prestiti S.p.A.</b>          | <b>Non energy-related items</b><br>Subscription of bonds.   | <b>Non energy-related items</b><br>Commission for loans to be granted.   |
| <b>CESI S.p.A.</b>                               | <b>Non energy-related items</b><br>Lease of laboratories and similar structures for specific purposes.  | <b>Non energy-related items</b><br>Technical consultancy, studies and research, projects and experimentation.  |
| <b>GSE Group</b>                                 | <b>Energy-related items</b><br>Remuneration of the grid and MIS component, energy sale, rights of withdrawal, rights to use transport capacity for interconnections.<br><br><b>Non energy-related items</b><br>Specialist services (remote console), leases, IT services.               | <b>Energy-related items</b><br>Purchase of energy, rights to use transport capacity for interconnections.  |
| <b>Enel Group</b>                                | <b>Energy-related items</b><br>Remuneration of NTG and metering aggregation, energy sales, rights of withdrawal, coverage of transmission costs, rights to use transport capacity for interconnections.<br><br><b>Non energy-related items</b><br>Leases and rentals, line maintenance. | <b>Energy-related items</b><br>Metering aggregation, energy purchases, rights to use transport capacity for interconnections, coverage of joint management costs, joint management fees.<br><br><b>Non energy-related items</b><br>Return of electricity discount, staff administration, building services, supply of MV power to new stations, specialised services for connection to Terna control and protection systems. |
| <b>Eni Group</b>                                 | <b>Energy-related items</b><br>Rights of withdrawal, energy sales, rights to use transport capacity for interconnections, coverage of transmission costs, remuneration of grid.<br><br><b>Non energy-related items</b><br>Line maintenance.   | <b>Energy-related items</b><br>Energy purchase, coverage of joint management costs, NTG remuneration.  |
| <b>Ferrovie Group</b>                            | <b>Non energy-related items</b><br>Line moving.   | <b>Energy-related items</b><br>Remuneration of the NTG.<br><br><b>Non energy-related items</b><br>Right-of-way fees.   |
| <b>Anas S.p.A.</b>                               | <b>Non energy-related items</b><br>Line moving.   | <b>Non energy-related items</b><br>Right-of-way fees.  |
| <b>Fondenel and Fopen</b>                        |   | <b>Non energy-related items</b><br>Pension contributions borne by the Terna Group.   |

| Company<br>In millions of euros                         | Income statement                                      |  |                          |   |   |                          |
|---|---|--|--------------------------|---|---|--------------------------|
|   | Revenue   |  |                          | Expenses  |   |                          |
|   | Grid transmission fees and other energy-related items | Grid transmission fees and pass-through energy related items | Non energy-related items | Grid transmission fees and other energy-related items | Grid transmission fees (other owners) and pass-through energy related items | Non energy-related items |
| Subsidiaries:   |   |  |                          |   |   |                          |
| TELAT S.r.l.  | -   | 138.5  | 76.5                     | -   | 138.5   | -                        |
| SunTergrid S.p.A.                                       | -   | -  | 1.5                      | -   | -   | -                        |
| RTS S.r.l.  | -   | -  | 0.1                      | -   | -   | -                        |
| Assets held for sale<br>(RTR S.r.l., Valmontone S.r.l.) | -   | -  | 7.6                      | -   | -   | 3.8                      |
| <b>Total subsidiaries</b>                               | -   | <b>138.5</b>   | <b>85.7</b>              | -   | <b>138.5</b>  | <b>3.8</b>               |
| De facto parent:  |   |  |                          |   |   |                          |
| Cassa Depositi e Prestiti S.p.A.                        | -   | -  | -                        | -   | -   | 1.3                      |
| <b>Total de facto parent</b>                            | -   | -  | -                        | -   | -   | <b>1.3</b>               |
| Associated companies:                                   |   |  |                          |   |   |                          |
| CESI S.p.A.   | -   | -  | 0.3                      | -   | -   | 2.6                      |
| <b>Total associated companies</b>                       | -   | -  | <b>0.3</b>               | -   | -   | <b>2.6</b>               |
| Other realted companies:                                |   |  |                          |   |   |                          |
| Gruppo GSE  | 14.6  | 1,078.8  | 0.4                      | -   | 475.1   | -                        |
| Gruppo Enel   | 1,148.6   | 751.6  | 4.5                      | 5.9   | 1,235.9   | 6.5                      |
| Gruppo Eni  | 2.1   | 197.2  | 0.5                      | -   | 145.0   | 0.1                      |
| Gruppo Ferrovie   | 0.8   | 34.3   | 0.1                      | 7.0   | 3.4   | 0.1                      |
| ANAS S.p.A.   | -   | -  | -                        | -   | -   | -                        |
| <b>Total other realted companies</b>                    | <b>1,166.1</b>  | <b>2,061.9</b>   | <b>5.5</b>               | <b>12.9</b>   | <b>1,859.4</b>  | <b>6.7</b>               |
| Pension funds:  |   |  |                          |   |   |                          |
| Fondenel  | -   | -  | -                        | -   | -   | 0.4                      |
| Fopen   | -   | -  | -                        | -   | -   | 1.7                      |
| <b>Total pension funds</b>                              | -   | -  | -                        | -   | -   | <b>2.1</b>               |
| <b>Total</b>  | <b>1,166.1</b>  | <b>2,200.4</b>   | <b>91.5</b>              | <b>12.9</b>   | <b>1,997.9</b>  | <b>16.5</b>              |



| Company<br>In millions of euros                         | Statement of financial position  |                                 |                |                                   |              |                           |
|---|----------------------------------|---------------------------------|----------------|-----------------------------------|--------------|---------------------------|
|   | Property, plant<br>and equipment | Receivables and<br>other assets |                | Payables and<br>other liabilities |              | Guarantees <sup>(*)</sup> |
|   | Capitalised costs                | Other                           | Financial      | Other                             | Financial    |                           |
| Subsidiaries:   |                                  |                                 |                |                                   |              |                           |
| TELAT S.r.l.  | 21.6                             | 3.8                             | 526.7          | 21.8                              | -            | -                         |
| SunTergrid S.p.A.                                       | -                                | -                               | -              | -                                 | 3.4          | -                         |
| RTS S.r.l.  | -                                | 0.2                             | -              | 0.1                               | 2.3          | -                         |
| Assets held for sale<br>(RTR S.r.l., Valmontone S.r.l.) | -                                | 6.4                             | 504.6          | 0.7                               | 245.4        | -                         |
| <b>Total subsidiaries</b>                               | <b>21.6</b>                      | <b>10.4</b>                     | <b>1,031.3</b> | <b>22.6</b>                       | <b>251.1</b> | <b>-</b>                  |
| De facto parent:  |                                  |                                 |                |                                   |              |                           |
| Cassa Depositi e Prestiti S.p.A.                        | -                                | -                               | 0.4            | -                                 | 2.4          | -                         |
| <b>Total de facto parent</b>                            | <b>-</b>                         | <b>-</b>                        | <b>0.4</b>     | <b>-</b>                          | <b>2.4</b>   | <b>-</b>                  |
| Associated companies:                                   |                                  |                                 |                |                                   |              |                           |
| CESI S.p.A.   | 19.4                             | -                               | -              | 5.0                               | -            | 3.5                       |
| <b>Total associated companies</b>                       | <b>19.4</b>                      | <b>-</b>                        | <b>-</b>       | <b>5.0</b>                        | <b>-</b>     | <b>3.5</b>                |
| Other related companies:                                |                                  |                                 |                |                                   |              |                           |
| Gruppo GSE  | -                                | 15.7                            | -              | 1.7                               | -            | -                         |
| Gruppo Enel   | 7.7                              | 128.7                           | -              | 28.2                              | -            | 435.4                     |
| Gruppo Eni  | -                                | 2.1                             | -              | 10.9                              | -            | 30.3                      |
| Gruppo Ferrovie   | -                                | 1.3                             | -              | 0.8                               | -            | 22.0                      |
| ANAS S.p.A.   | -                                | 0.2                             | -              | 0.2                               | -            | -                         |
| <b>Total other related companies</b>                    | <b>7.7</b>                       | <b>148.0</b>                    | <b>-</b>       | <b>41.8</b>                       | <b>-</b>     | <b>487.7</b>              |
| Pension funds:  |                                  |                                 |                |                                   |              |                           |
| Fondenel  | -                                | -                               | -              | -                                 | -            | -                         |
| Fopen   | -                                | -                               | -              | 1.4                               | -            | -                         |
| <b>Total pension funds</b>                              | <b>-</b>                         | <b>-</b>                        | <b>-</b>       | <b>1.4</b>                        | <b>-</b>     | <b>-</b>                  |
| <b>Total</b>  | <b>48.7</b>                      | <b>158.4</b>                    | <b>1,031.7</b> | <b>70.8</b>                       | <b>253.5</b> | <b>491.2</b>              |

(\*) The guarantees refer to the bank guarantees received on contracts.

## H. Significant non-recurring events and operations, atypical or unusual transactions

No significant, non-recurring, atypical or unusual transactions were carried out during 2010, either with third parties or with related parties.

## I. Notes to the statement of cash flows

The cash flow generated from **continuing operations** in the year amounted to around € 471 million, which reflects around € 1,115.7 million in cash from operating activities (self-financing) and the use of around € 644.7 million in financial resources generated by the management of net working capital.

**Investing activities** absorbed net financial resources of around € 1,137.5 million, including € 1,051.3 million invested in property, plant and equipment (€ 1,063.4 million net of grants related to assets totalling € 12.1 million received in the period), and € 56.8 million invested in intangible assets (€ 57.0 million net of grants related to assets totalling € 0.2 million received in the period).

Cash flow for investments also reflects the acquisition from the subsidiary TELAT of some transmission plants concerned by development and renewal interventions (€ 21.2 million) and the recording of additional stakes (€ 8 million) in the associate CESI, acquired in December 2010 from Ansaldo Trasmissione & Distribuzione S.p.A. for 9% of the share capital. The net change in **cash flows** records an increase of € 830.5 million, basically due to the combined effect of the increased medium/long-term financial payables (€ 948.3 million, including the short-term share and net of FVH derivatives), the short-term loans (€ 30.4 million) and repayment during 2010 of investments in securities subscribed (€ 500.0 million) with UBS and MPS in 2009, offset by the supply of the 2009 dividend balance (€ 240.4 million) and the advance on the 2010 dividend (€ 160.4 million) in addition to the net positive balance of assets held for sale (€ 254.6 million) in relation to the loan and debt position on the intercompany current account with regards to the subsidiary RTR (€ 500.0 million and € 245.4 million respectively).

The changes in equity (€ 7.2 million in total) also include the effects deriving from the exercise of stock options during the year. Consequently, the financial resources used in for investing activities and the remuneration of equity amounted to € 1,526.5 million in the year, part of which (€ 471 million) was covered by the cash flows generated by operating activities, while the balance came from new debt.

## L. Events after the reporting date

### Acquisition of the shareholding in CGES and agreement for the construction of the electrical connection between Italy-Montenegro

On **23 November 2010**, Terna signed the definitive agreement for the strategic partnership with the transmission operator of Montenegro, Crnogorski Elektroprenosni Sistem AD ("CGES"), and the government of Montenegro, acting in the capacity of majority shareholder of CGES; this agreement refers to the construction of the new electrical connection between Italy-Montenegro and the strategic Terna-CGES partnership. The transaction was completed in January following the occurrence of the conditions precedent. The stipulation was completed following the approval, on the part of the shareholders of CGES, of the share capital increase for Terna and the adoption of new Bylaws. Terna therefore became the shareholder of CGES with 22.09% of the share capital and, in its capacity as the new shareholder, signed the shareholders' agreement relative to the new governance system and the industrial contract for investments.

The agreement represents the end point of a process of industrial and country cooperation and is part of the intergovernmental agreements between Italy and Montenegro which were initiated on 19 December 2007 with the start-up of activities of the Italy-Montenegro Work Group and consolidated on 6 February 2010 by means of the contract which ratified the commitment at an institutional level for the construction of a new submarine electrical connection and the implementation of partnerships with national transmission operators.

It is expected that the overall investment of Terna for the first "electrical bridge" to the Balkans will total circa € 760 million. The investment of CGES for the connection of the existing network and the reinforcement of the local network will total approx. € 100 million.

## 2011-2015 Business Plan

On **14 February 11**, Terna presented to financial analysts the Company's 2011-2015 business plan, after approval of the plan by the Board of Directors on that same date.

The 2011-2015 plan of the Terna Group follows five main guidelines:

- traditional regulated activities: increase of investments from € 4.3 to approx. 5 billion (+15%) in order to modernise the grid; development investments for which incentive-based remuneration is planned represents circa 82% of the total and increased from € 3.3 billion to 4 billion;
- non-traditional activities. investment activities were tripled for these activities, with planned allocations of up to 1 billion euro. In particular, the development of an additional set of photovoltaic projects of circa 50 MWp is planned for the course of 2011. In addition, other investment opportunities will also be assessed, including those within the sector of energy efficiency and for the construction and management of grid infrastructures for connecting renewable energy source plants in the Balkan area to the local grid, as well as storage systems and batteries in the Italian's grid;
- improved margins (EBITDA margin): increasing revenue and containing costs will improve Group profitability from the current 74% to 78% at the end of the period covered by the plan;
- a sound capital structure: during the period of the plan, pledge to maintain the ratio between debt and regulated invested capital (RAB) always remains significantly under 60%;
- confirmation of dividend policy: the 2011-2015 Strategic Plan confirms the dividend policy. As had previously occurred with the sale of Terna Participações, part of the capital gains attained with the sale of non-traditional assets may integrate the above-mentioned policy which provides for an annual growth of 4%, assuming the year 2008 as the year of reference.

## 10-year bond issue for € 1.25 billion

On **8 March 2011** Terna launched a bond issue on the market in euros, at a fixed rate, with expiry in 10 years, for a total of € 1.25 billion under the scope of its Euro Medium Term Notes (EMTN) programme. This has been assigned an A+ rating for Standard and Poor's, A2 for Moody's and A+ for Fitch.

The bond expires on 15 March 2021, has an annual coupon of 4.750% and issue price of 99.245. The security has thus been priced with a spread of 130 basis points as compared with the mid swap.

Securities are listed on the Luxembourg Stock Exchange.

The transaction, destined for Institutional Investors, has been placed by a syndicate of banks comprising Banca Akros S.p.A., MPS Capital Services S.p.A., Natixis, UniCredit Bank AG and WestLB AG as joint-lead managers and joint-bookrunners.

The bond is intended to finance the grid development investments envisaged in the Company's business plan.

## The new "SA.PE.I." power line uniting Sardinia and mainland Italy is opened

On **17 March 2011** Terna was proud to open the new SA.PE.I. power line. SA.PE.I. is an acronym for SARdegna-PENisola-Italiana (Sardinia-Italian-Peninsula) and this is the first ever direct electrical connection to be created between Sardinia and mainland Italy, and the most important and technologically advanced high voltage power line ever to be developed in Italy. The infrastructure has achieved a great many records, in fact, which include: the world's longest "electrical bridge", with a power of 1,000 megawatts; the world's deepest, as it extends for 435 km from Fiumesanto (Sardinia) to Latina (Lazio), reaching depths of 1,640 m; and the greatest investment: worth a grand total of € 750 million, it is the most important investment ever to be made in Italy in a single electrical infrastructure. More than 50% of the work was funded by Terna's own means with the remainder financed by grant of € 373 million awarded by the European Investment Bank (EIB) due to the high strategic value at hand. The result boasts a great many economic, electrical and environmental benefits. The work allows for annual savings of € 70 million for the electrical system, thanks to the elimination of "bottlenecks" between Sardinia and the rest of the electricity market, in addition to increased safety of the Sardinian electrical system and a more secure coverage of the demands of Lazio and central Italy, thanks to use of more efficient energy, partly originating from Sardinia.

## Sale of Rete Rinnovabile S.r.l. completed

In implementation of the agreement signed on 18 October 2010 by Terna S.p.A., SunTergrid S.p.A. and Terra Firma Investments (GP) 3 Limited (wholly owned by Terra Firma Capital Partners III, L.P.), on **31 March 2011**, the transfer to RTR Acquisition S.r.l. (an indirect subsidiary of Terra Firma Investment (GP) 3 Limited) of 100% of the share capital of Rete Rinnovabile S.r.l. ("RTR S.r.l.") was completed.

RTR S.r.l. owns 62 photovoltaic plants, located in 11 different regions of Italy, for a total capacity of 143.7 MWp, of which 101.6 MWp will benefit from the 2010 Energy Account tariffs for the 1<sup>st</sup> quarter 2011. The sale of the investment in RTR S.r.l. has resulted in total net income of around € 204 million and a reduction in the effective net financial debt of continuing operations of the Terna Group for more than € 200 million.

The completion of the sale confirmed the effect on the 2010 consolidated income statement, booked as the contract margin in terms as compared with total costs sustained during the year, on the basis of works progress, as described in full previously, amounts to € 147 million. The difference will instead be recognised on an accruals basis in 2011.

It is also specified that in addition to renting the land, Terna will also provide RTR S.r.l. with plant maintenance, surveillance and monitoring services, according to multiyear contracts defined in the context of the sale. At the end of the individual rental contracts, Terna will regain possession of the leased areas.

## Information pursuant to art. 149-*duodecies* of the CONSOB Issuers Regulation

The following table, prepared pursuant to art. 149-*duodecies* of the CONSOB Issuers Regulation, reports the fees for 2010 for the audit and the non-audit services provided to Terna S.p.A. by the same independent auditors.

| Euros                | Entity providing service | Amounts due for the year |
|----------------------|--------------------------|--------------------------|
| Auditing services    | KPMG S.p.A.              | 525,359.40               |
| Attestation services | KPMG S.p.A.              | 169,370.30               |
| <b>Total</b>         |                          | <b>694,729.70</b>        |

**Certification of the financial statement pursuant to art. 81-ter of Consob Regulation n. 11971 dated May 14, 1999 and subsequent amendments and additions**

1. The undersigned Flavio Cattaneo as CEO and Luciano di Bacco as Executive in Charge of preparing the accounting documents of Terna S.p.A., also taking into account the provisions of art. 154-bis paragraphs 3 and 4 of Legislative Decree n. 58 dated February 24, 1998 hereby certify:
  - the adequacy with regard to the characteristics of the company and
  - the actual implementation of the administrative and accounting procedures for preparing the financial statement for 2010.
2. With regard to the above, nothing significant emerged.
3. It is also certified that
  - 3.1. the financial statement as of December 31, 2010:
    - a) was prepared in compliance with the applicable international accounting standards recognized by the European Community pursuant to regulation (EC) n. 1606/2002 of the European Parliament and of the Council, dated July 19, 2002 as well as with the provisions implementing art. 9 of Legislative Decree n. 38/2005.
    - b) corresponds to the results of the books and of the accounting records.
    - c) provides a truthful and correct representation of the statement of assets and liabilities and of the economic and financial situation of the issuer.
  - 3.2. The Report on the management includes an accurate and faithful analysis of the management trend and results and of the issuer's situation, together with the description of the principal risks and uncertainties faced.

Rome, March 31, 2011

Delegated Administrative Bodies

The Executive in Charge  
of preparing the Company's accounting documents

Flavio Cattaneo

Luciano Di Bacco

*(Signed on the original)*

*This report has been translated into the English language solely for the convenience of international readers.*





## Reports



**REPORT BY THE BOARD OF STATUTORY AUDITORS TO TERNA S.p.A.'S  
SHAREHOLDERS MEETING**

(pursuant to art. 153 of Legislative Decree no. 58/98)

Shareholders,

During the year that ended on December 31, 2010, we performed the supervisory activity required by the Law (Legislative Decree no. 58 dated February 24, 1998– “Consolidated text for the provisions regarding financial brokerage activity ” and Legislative Decree dated January 27, 2010 no. 39 “Implementation of Directive 2006/43/CE related to the legal auditing of annual accounts and consolidated accounts, modifying Directives 78/660/CEE and 83/349/CEE and abrogating Directive 84/253/CEE ), adapting our activity to the code of practice of the Boards of Statutory Auditors of capital-based companies with shares listed in regulated markets as recommended by National Board of Chartered Accountants and by CONSOB provisions regarding company auditing and activities conducted by the Boards of Statutory Auditors.

The auditing activity, pursuant to Legislative Decree 39/2010, was assigned and carried out by the KPMG S.p.A. Auditing firm whose reports are referred to.

The Board of Statutory Auditors presently in office was appointed by the Shareholders Meeting on April 28, 2008 based on the provisions of the By-laws. We remind you that, with the approval of this Annual financial statement, our term of office will expire.

Also in compliance with the provisions issued by CONSOB with Notice DEM/125564 dated April 6, 2001 and subsequent updates, the following was carried out:

-We monitored that the Law and the By-laws were complied with.

-We attended the meetings of the Board of Directors and specific preparatory meetings regarding the items on its agenda, including the meetings of the Internal Control Committee and of the Remuneration Committee and were regularly informed by the Directors about the activities carried out, expected outlook and the most significant economic, financial and equity transactions of the Company, and we were satisfied that the resolutions adopted and implemented were in compliance with Law provisions and the By-laws and were not manifestly imprudent, risky, representing a potential conflict of interests, in contrast with the resolutions passed by the shareholders meeting or capable of compromising the Company's assets. During the assessments, no atypical and/or unusual operation emerged.

- The Board of Directors on its meeting on October 18, 2010 has proceeded to adopt by-laws mandatory modifications as provided for by Legislative Decree 27/210, deliberating to modify

articles 10.1, 11.1, 14.3, and 26.2 of the By-laws in compliance to legal provisions, pursuant to art. 21.2, letter e) of Company By-laws and art. 2365 of the Civil Code.

- In the chapter "Related-party transactions" included into the Notes to the Consolidated and separate financial statement, the directors highlighted the principal transactions that were conducted with related parties, identified on the basis of the international accounting standards and on the provisions issued on the matter by CONSOB. This chapter can be referred to, to identify the type of transactions and relative economic, financial and equity effects. We also inform that the Board of Directors, on October 18, 2010 has adopted, once the positive opinion of a specific Committee has been obtained, the "Related party transactions procedure", pursuant to art. 4 of the Regulation adopted by CONSOB with resolution no. 17221 of March 12, 2010 as subsequently amended and integrated. The procedure, pursuant to CONSOB Regulation no. 17221 of March 12, 2010 and to CONSOB Communication of September 24, 2010, is effective from January 1, 2011 and was published on the Company's web site.

- The Company drew up the 2010 Separate financial statement according to the International Accounting Standards (IAS/IFRS), as was also done for the previous one in 2009. The Notes include the accounting standards and the evaluation criteria adopted. Terna S.p.A.'s 2010 Separate financial statement was submitted to the evaluation of the KPMG S.P.A. Accounting firm which issued its auditing report on April 18, 2011 without anything significant to report. Significant events that occurred during 2010 are included in the Directors' Report and can be examined more in detail:

- with reference to the development of the photovoltaic project, Terna S.p.A., its subsidiary SunTergrid and Terra Firma Investments (GP) 3 Limited have signed a preliminary agreement aiming at the conveyance of 100% of the capital of Rete Rinnovabile s.r.l., completely controlled by SunTergrid S.p.A., for a total amount agreed in a modular fashion (in terms of enterprise value) on the basis of the plants which, on the closing date (31 March 2011), alternatively benefited from the incentives of the 2010 Energy Account or the Energy Account of the first months of 2011;
- the Company, on August 5, 2010, through its subsidiary Telat S.p.A, has completed the acquisition of 100% of capital of Reti Trasmissioni Energia Elettrica ASM S.r.l. ("Retrasm") from A2A S.p.A. for a total amount of Euros 28 million; Retrasm used to own and manage a part of National Transmission Grid amounting to approximately 288 Km lines and related bays and a 220/130Kv power station;

- the Company, on November 24, 2010, has signed an agreement with BEI – European Investment Bank for Euros 300 million financing designed for a quadrennial investment programme (2010-2013) aiming at reinforcing the national energy transport system and assuring safety and efficiency standards requested by the transmission system.
  
- The Company drew up the 2010 Consolidated financial statement applying the International Accounting Standards (IFRS/IAS) as it did for the previous year; the Terna Group's Consolidated Financial Statement was submitted to the evaluation of the KPMG S.p.A. Auditing firm that issued its auditing report on April 18, 2011 without anything significant to report.
  
- We collected information and monitored, as far as our authority allowed, the adequacy of the Company's organizational structure, compliance with the principles of proper management and the adequacy of the provisions issued by the Company to the subsidiaries pursuant to art. 114, paragraph 2, of Legislative Decree 58/59 by acquiring information from the Heads of the designated company departments, through meetings held with the Auditing firm and through meetings held with the control bodies of subsidiaries in order to mutually exchange data and significant information.
  
- We monitored the administrative and accounting system, assessing the reliability of the latter in providing a true and fair view of operations; this activity was carried out by obtaining information from the heads of the various departments, by examining company documents and analyzing results of the work carried out by the KPMG S.p.A. Auditing firm. The Board of Directors appointed the Executive in charge of "preparing the Company's accounting documents" also verifying for him the existence of the necessary professional requirements. The CEO and the Executive in charge of preparing the Company's accounting documents certified with a specific report (attached to the Company's 2010 Financial Statement) a) compliance and effective application of administrative and accounting procedures; b) compliance of the contents of the accounting documents with the international accounting standards IFRS /IAS approved by the European Community, as well as with the provisions issued by CONSOB implementing Legislative Decree no. 38/2005; c) compliance of the documents with the data included in the books and the accounting records and their reliability in correctly representing the Company's economic, financial and equity situation. The same type of Certification Report is attached to the Terna Group's Consolidated financial statement.



- We monitored the adequacy of the internal control system also through a) the examination of the report by the Executive in charge of Terna's internal control system; b) the examination of the *Internal Audit* reports, as well as the informative report on the outcomes of the monitoring activity; c) the relationships with the Supervisory Bodies of the subsidiaries pursuant to of par. 1 and 2 of art. 151 of Legislative Decree 58/98; d) the participation in all the Internal Control Committee meetings and acquisition of related documentation. The participation to the Internal Control Committee has also allowed the Board to coordinate with the activities of the same Committee, the exercise of its functions of "Committee for internal control and auditing of accounts" pursuant to art. 19 of Legislative Decree 39/2010 and to proceed, in particular, to supervise i) the process of financial information reporting ii) the effectiveness of the internal control, auditing and risk management systems iii) on the legal auditing of the annual and consolidated accounts iv) on the aspects related to the independence of the Auditing firm. By the activity carried out, the Board expresses an evaluation of adequacy of Terna's Internal Control System in its complex and acknowledges, in quality of Committee for internal control and auditing of accounts, that there are no observations to report to the Shareholders Meeting. With reference to the provisions of par. 1 of art. 19 of Legislative Decree 39/2010, the Auditing firm has notified used hours and invoiced fees for the Auditing of the Separate and Consolidate financial statement as at 31 December 2010, besides the limited auditing of the Interim financial statement, for the activities of assessment of regular accounting activities, and for the other assignments; the fees for those assignments are shown in the table below:

| Client Company | Service description   | Amount         |
|----------------|---|----------------|
| Terna S.p.A.   | Audit of Unbundling for AEEG (including expenses)                     | 53.680         |
|                | Audit of reporting packages as at 30 June 10 (including expenses)     | 16.830         |
|                | Audit of reporting packages as at 31 December 10 (including expenses) | 30.140         |
|                | Opinion for interim dividend (including expenses)                     | 50.000         |
|                | Review of Modelli Unico and 770                                       | 4.950          |
|                | Certification of the Sustainability Annual Report                     | 72.400         |
|                | EMTN and related comfort letter                                       | 135.300        |
|                | <b>Total</b>  | <b>363.300</b> |

Moreover, KPMG has notified that, based on the best information available, taken into account prescribed and professional requirements that discipline the auditing activity, has maintained in the reference period its position of independence and objectivity towards Terna S.p.A. and that there

have been no variations in the inexistence of incompatibility causes with reference to the situations and the subjects provided for by art. 17 of the Legislative Decree 39/2010 and of the articles of which to par. I-bis (Incompatibility) of Title IV of Issuers Regulation.

- We held periodic meetings with the representatives of the KPMG S.p.A. Auditing firm, pursuant to art. 150, paragraph 3 of Legislative Decree 58/59 and no facts worthy to be mentioned in this Report emerged. We also give notice that on April 18, 2011 the Auditing firm has submitted its report, pursuant to the third paragraph of art. 19 of Legislative Decree 39/2010, reporting that on the occasion of the auditing activities, neither fundamental issues or meaningful deficiencies in the internal control system, with reference to the process of financial information reporting, have emerged.

- With the end of 2010 accounting period, the term of office for the Separate and Consolidate financial statement of Terna S.p.A auditing by KPMG S.p.A will expire and since such assignment has lasted for nine years, it is no longer renewable and it becomes therefore necessary to entrust the assignment to a new subject, different from KPMG S.p.A. Pursuant to art. 13 of Legislative Decree 39/2010 *"The general shareholders meeting, on motivated proposal by the Supervising Body, confers the assignment of legal audit of accounts and determines the fee due to the legal auditor or Auditing firm for the entire duration of the assignment and any criteria for the adjustment of such fee during the assignment"*; the Board of Statutory Auditors, therefore, has proceeded to select the subject to propose to the Shareholders Meeting for the attribution of the legal assignment of audit of accounts for accounting periods 2011 - 2019. Carried out activity, criteria and decisions adopted are illustrated in the report containing the motivated proposal submitted to the exam of the Shareholders Meeting.

- We have monitored the actual implementation of Terna S.p.A.'s Code of Conduct adopted by the Board of Directors without noticing anything significant to be mentioned in this report. Moreover, with reference to the provisions established by the Code of Conduct which refer to the tasks of the Board of Statutory Auditors, the following should be pointed out:

- we verified the correct application of the criteria and procedures for assessing independence, adopted by the Board of Directors, with nothing significant to report;
- with regard to the "self-evaluation" of the independence requirement of its members, the Board of Statutory Auditors verified its existence during the meeting held on February 14, 2011;

- we complied with the provisions of the regulation for managing and handling confidential and privileged company information;

Furthermore, it should be pointed out that the Auditing firm expressed its opinion regarding coherence of information pursuant to paragraph 1) letters c), d), f), l), m) and to paragraph 2, letter b), of art. 123-*bis* of Legislative Decree 58/98 as indicated by the amendments introduced by article 5, paragraph 4, of Legislative Decree 173/2008.

- With reference to Legislative Decree n. 231/2001, the Company adopted an organizational and management model whose contents were in compliance with the best international practices. Furthermore, we met the Supervisory Board for the mutual exchange of information.

- During the year, no legal actions pursuant to Art. 2408 of the Civil Code were filed and received.

- We do not have the knowledge of any other facts or reports to be mentioned to the Meeting.

- We have verified compliance with the laws regarding the drawing up of the draft Separate financial statement and of the draft Consolidated financial statement, of the respective Illustrative Notes and the Directors' Report, directly and with the collaboration of the Heads of departments and through information obtained by the Auditing firm, and we have nothing significant to report.

- We have issued our opinions pursuant to art. 2389, paragraph 3 of the Civil Code and to art. 2412 of the Civil Code; the Auditing firm issued its opinion pursuant the provisions of paragraph 5 of art. 2433-*bis* of the Civil Code (interim dividends).

- The members of the Board of Statutory Auditors have complied with the obligation to notify administration and control assignments in Italian companies within deadlines and by means provided for by art. 148-*bis* of Legislative Decree of February 24, 1998 no.58 and by art. 144 - *duodecies* and following of the so-called Issuers Regulation adopted by CONSOB with Resolution no. 11971 of May 14, 1999.

- In carrying out the above-mentioned monitoring activity, during 2010, the Board of Statutory Auditors met 9 times, attended the 8 meetings of the Board of Directors and participated in the 4 meetings of the Internal Control Committee and in the 4 meetings of the Remuneration Committee.

During the above-mentioned activity, as well as on the basis of the information periodically exchanged with the KPMG S.p.A. Auditing firm, no omissions and/or reproachable facts and/or irregularities were found that required reporting to the control bodies or that were worthy to be mentioned in this Report.

The Board of Statutory Auditors, following the monitoring activity carried out, requests your approval of the financial statement as of December 31, 2010 in compliance with the proposal of the Board of Directors.

Rome, April 18, 2011

The Board of Statutory Auditors

Luca A. Guarna  
Lorenzo Pozza  
Marcello Cosconati







KPMG S.p.A.  
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(Translation from the Italian original which remains the definitive version)

## Report of the auditors in accordance with articles 14 and 16 of Legislative decree no. 39 of 27 January 2010

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 2010, comprising the income statement, statement of comprehensive income, statement of financial position, statement of changes in equity, statement of cash flows and notes thereto. The company's directors are responsible for the preparation of these financial statements in accordance with the International Financial Reporting Standards endorsed by the European Union and the Italian regulations implementing article 9 of Legislative decree no. 38/05. 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 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 and the statement of financial position as at 1 January 2009 for comparative purposes. As disclosed in the notes, following the application of IFRIC 12 *Service Concession Arrangements* to electricity dispatching activities carried out under concession, the directors restated some of the corresponding figures included in the prior year separate financial statements and statement of financial position as at 1 January 2009, which derives from the separate financial statements at 31 December 2008. We audited the 2009 and 2008 separate financial statements and issued our reports thereon on 9 April 2010 and 31 March 2009, respectively. We have examined the methods used to restate the prior year corresponding figures and related disclosures for the purposes of expressing an opinion on the separate financial statements at 31 December 2010.

KPMG S.p.A. è una società per azioni di diritto italiano e fa parte del network KPMG di entità indipendenti affiliate a KPMG International Cooperative ("KPMG International"), entità di diritto svizzero.

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Bologna Bolzano Brescia Cagliari  
Catania Como Firenze Genova  
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Padova Palermo Parma Perugia  
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Sede legale: Via Vittor Pisani, 20  
20124 Milano MI (ITALIA)



**TERNA S.p.A.**  
*Report of the auditors*  
31 December 2010

- 3 In our opinion, the separate financial statements of TERNA S.p.A. as at and for the year ended 31 December 2010 comply with the International Financial Reporting Standards endorsed by the European Union and the Italian regulations implementing article 9 of Legislative decree no. 38/05. 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 2010, the results of its operations and its cash flows for the year then ended.
- 4 The directors of TERNA S.p.A. are responsible for the preparation of a directors' report on the financial statements and a report on the corporate governance and ownership structure in accordance with the applicable laws and regulations. Our responsibility is to express an opinion on the consistency of the directors' report and the information required by article 123-bis.1.c/d/f/l/m and article 123-bis.2.b of Legislative decree no. 58/98 disclosed in the report on the corporate governance and ownership structure with the financial statements to which they refer, as required by the law. For this purpose, we have performed the procedures required by the Italian Standard on Auditing 001 issued by the Italian Accounting Profession and recommended by Consob. In our opinion, the directors' report and the information required by article 123-bis.1.c/d/f/l/m and article 123-bis.2.b of Legislative decree no. 58/98 disclosed in the report on the corporate governance and ownership structure are consistent with the separate financial statements of TERNA S.p.A. as at and for the year ended 31 December 2010.

Rome, 18 April 2011

KPMG S.p.A.

(signed on the original)

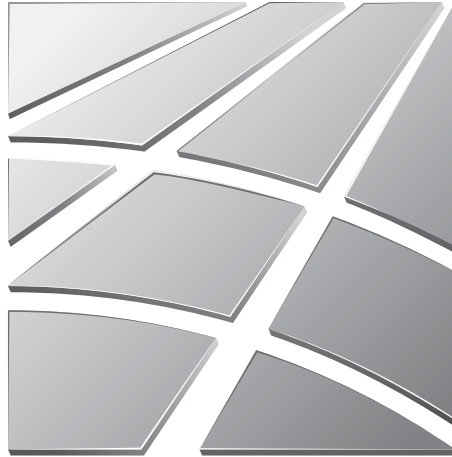
Marco Maffei  
Director of Audit







2010



## Corporate Governance

(traditional management control model)

Issuer: "Terna – Rete Elettrica Nazionale Società per Azioni" (Terna S.p.A.)  
Website: [www.terna.it](http://www.terna.it)  
Reporting period: 2010  
Date of approval: 31 March 2011



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## Report on Corporate Governance and ownership structures

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# 2010 Report on Corporate Governance and ownership structures

## Foreword

Since 2006, Terna has adopted the new Code of Conduct for listed companies published by Borsa Italiana in March 2006 (Code of Conduct) and as of 2007 has approved the updates to the Corporate Governance system in place within the Company to meet its commitments arising there from, that were implemented during 2009 and up to the approval date of the 2009 draft financial statements, as illustrated here below.

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

Since 2004, the year the Company's shares were listed on Borsa Italiana, Terna provides, with an appropriate annual report, information regarding the development of its Corporate Governance system with respect to the provisions of the Governance Code of Borsa Italiana, which the Company has adopted.

Furthermore, already as part of the annual report for 2008, Terna provides with its report on Corporate Governance – the information required by art. 123-bis of Legislative Decree no. 58/98 (Consolidated Law on Finance) as included in a specific section.

This report on the Corporate Governance was drafted taking into account the indications by Borsa Italiana with the support of Assonime – also with the specific references in the provisions of the Consolidated Law on Finance and supplemented with an appropriate attachment that illustrates the main characteristics of the existing risk management and internal controls over the financial reporting process.

Failure to comply with certain provisions of the Governance Code is explained in the section of the report that concerns the relative practice of governance otherwise applied by the Company.

All the information included in the report, unless otherwise specified, were updated on the basis of information available as of the date of the report's approval.

## Section I Issuer's profile - Corporate structure

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### Issuer's profile - Governance Code for listed companies, with CONSOB recommendations

#### Mission

"Terna is a leading grid operator for energy transmission. The Company manages electricity transmission in Italy and guarantees its safety, quality and affordability over time. It ensures equal access conditions for all grid users. It develops market activities and new business opportunities with the experience and technical expertise acquired in managing complex systems. It creates values for shareholders with a strong commitment towards professional excellence and with a responsible approach towards the community, fully respecting the environment it operates in".

#### Social Responsibility

Terna manages all its activities focusing on their possible economic, social and environmental consequences and has identified a sustainability approach for creating, maintaining and consolidating a relationship of mutual trust with its stakeholders.

Terna's main Corporate Social Responsibility (CSR) aspects are provided by the Code of Ethics and by the Company mission. Taking on sustainability as a guiding feature, Terna has defined its responsibilities and established its objectives in the economic, environmental and social areas. Considering its role in the electricity system, Terna has added the specific responsibility for the electricity service to the other ones.

From the point of view of sustainability, respect for the environment is particularly important. The physical presence of pylons, lines and power stations and their interaction with the landscape and biodiversity are indeed crucial for Terna's activities. That is why Terna has chosen the approach of negotiation and coordination with local authorities, also involving significant stakeholders such as the main environmentalist associations to take environmental needs into consideration from the early stages of planning new lines. The Company has also developed a management system to control and limit

the environmental impact of its activities. Thus, consideration of environmental issues matches Terna's interests in implementing grid development investments and in the more general interest of community for a reliable, inexpensive and environmentally safe electricity system.

The management approach adopted and the results and new economic responsibility objectives reached in the field of social and environmental responsibility are presented in the Sustainability Report, published yearly.

Since the 2006 edition, the report has been drawn up in compliance with the G3 Sustainability Reporting Guidelines of the Global Reporting Initiative and verified by an auditing company. The level of application of the G3 Guidelines was marked as A+ for the 2009 Sustainability report, thus demonstrating the Company's commitment to information transparency and correctness.

Among the main 2010 results for CSR it is worth mentioning:

- collaboration continued with the WWF aiming at integrating biodiversity preservation criteria in planning new lines and in managing the existing ones, for planning measures to be carried out in natural oases;
- the completion of scientific research, together with LIPU (Italian League for Bird Protection), on the interaction between high-voltage power lines and the birdlife for establishing mitigation measures;
- support given to the final phase of an International solidarity project stemming from volunteer activity carried out by some of Terna's staff; they coordinated and shared their technical experience and knowledge to build an electricity line, 37 km long, to the benefit of a Salesian mission in Kami in the Bolivian Andes;
- an awareness-raising campaign on sustainability issues, with presentations made by the Corporate Social Responsibility Department, that involved over 500 employees from the 8 Operating Transmission Areas and all central Departments;
- the initiative "Vote your value" that completed the campaign for disseminating the Code of Ethics, allowing all employees to turn some of Terna's charitable initiatives to associations supporting the most voted values among those that are at the basis of the Code of Ethics.

Terna's constant commitment to continually improving its economic, environmental and social performance made it possible for the company to be included in an increasing number of Stock Exchange sustainability indexes. In 2010, in particular, in addition to being included in the Dow Jones Sustainability World Index, that contains the best 300 companies in the world, with respect to sustainability performance, Terna was also present in the Dow Jones Sustainability Index Europe and in the FTSE-ECPI indexes, the only ones that select the sustainability best practices in companies that are listed in the Italian Stock Exchange.

## Company organization

In compliance with the provisions of the Italian legislation concerning listed companies, the Company's organization, based on the traditional administration and management model, includes the following:

- a Board of Directors responsible for the Company management. To such aim, the Board is entrusted with the widest powers so as to complete all the actions that deems appropriate for the performance and the attainment of the Corporate purpose, excluding only the action that the law and the Bylaws reserve for the shareholders';
- 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 as well as those of the foreign subsidiaries outside of the EU. It is also responsible for carrying out all duties assigned to the Board of Statutory Auditors by Law and by the Code of Conduct; according to art. 19 of Legislative Decree 39/2010, it is the responsibility of the Board of Statutory Auditors to supervise the financial information process, the efficiency of the internal control systems, of internal reviews and risk management, the auditing of annual and consolidated results pursuant to law provisions and the independent of the auditors .
- the Shareholders' Meeting – ordinary and extraordinary – during which the shareholders resolves upon, *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 Bylaws, and (V) the issuance of convertible bonds;
- an Executive in Charge of the preparation of the Company's accounting documents, who is given all assignments and responsibilities provided by the law and regulations as well as those provided for by the Code of Conduct (art. 8.C.3).

Auditing is entrusted to specialized independent auditors registered in the appropriate records, which is specifically appointed by the Shareholders' Meeting upon proposal of the Board of Statutory Auditors.

Terna's independent Auditors also have similar engagements with the Company's main subsidiaries.

It has been some time since the Organizational Model adopted by the Company pursuant to Legislative Decree no. 231/01, which was recently updated based on the provisions of Legislative Decree 39/2010, established that the auditing of the Company's financial statements, those of any group company and the consolidated financial statements is not compatible with consultancy activities for Terna or any group company. This incompatibility extends to the audit company's entire network as well as to shareholders, Directors, members of control bodies and employees of the audit company and of the other companies belonging to the same network. The assignments to the audit company are submitted to Terna's Internal Control Committee for any assignment other than the one given under law provisions, in any event related to auditing

activities. In order to ensure independence of the company and of the officer in charge of auditing, the assignment for the auditing of the Company's financial statements and that of any company of the Group and of the consolidated financial statements is not in any case given to audit companies that fall within one of the incompatibility situations pursuant to Part III, Title VI, paragraph I-bis of the "Regulations implementing Legislative Decree no. 58 dated 24 February 1998, regarding the law on issuers" adopted by CONSOB (Issuer Regulations).

Terna's Board of Directors' Meeting of 18 October 2010 approved the amendments to the Bylaws necessary for the adjustment of the Company articulated of association to the provisions regarding shareholders' rights of listed companies to favour the participation of shareholders in the activity of the Company (Directive 2007/36/EC and relative implementing Legislative Decree no. 27 dated 27 January 2010).

Amendments involved articles 10.1, 11.1, 14.3 and 26.2 of the Bylaws regarding the right to participate and vote in Shareholders' Meetings, based on the introduction of the mechanism of the so-called record date (art. 10.1); the terms for issuing proxies, based on the need to include in the Bylaws at least one term for notifying proxies by electronic means (art. 11.1), the appointment procedure for the Board of Directors and the Board of Statutory Auditors, with reference to the terms and conditions for filing lists based on the amendments pursuant to Legislative Decree 27/2010 to art. 4 of Law Decree no. 332 of 31 May 1994, as converted with amendments by Law no. 474 dated 30 July 1994, so-called "Privatization Law" (articles 14.3 e 26.2).

Such amendments will be applied for the first time on occasion of the next annual Meeting which will also have to resolve about the renewal of the expiring company bodies with the approval of the 2010 financial statement.

On that occasion, art. 26.2 of the Bylaws will be modified for being adapted to the law provisions regarding legal auditing that were introduced by Legislative Decree no. 39 dated 27 January 2010.

## **Section II Information on ownership structure (pursuant to art. 123-bis, paragraph 1 of the Consolidated Law on Finance)**

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### **Share capital structure (pursuant to art. 123-bis, paragraph 1, letter a) of the Consolidated Law on Finance)**

The Company's share capital as of 31 March 2011 amounts to € 442,088,020 and comprises exclusively nominal ordinary shares, for a total of 2,009,491,000 ordinary Terna's shares with a nominal value of € 0.22 each. They are fully paid-up and bear voting rights at both the ordinary and extraordinary Shareholders' Meetings. Ordinary shares grant further administrative and financial rights as provided for by the law regulating the shares with right to vote.

Since 23 June 2004, Terna's shares have been listed in the Electronic Stock Exchange organized and managed by Borsa Italiana S.p.A. (Telematic Share Market - Blue Chip segment).

Pursuant to art. 5.2 of the Company Bylaws, the Shareholders' Meeting can approve capital increases through share issuance, also belonging to special categories, to be assigned free of charge pursuant to art. 2349 of the Italian Civil Code for employees, or rather as payment, and with the exclusion of the option right under art. 2441 of the Civil Code, in favor of subjects identified with resolution by the Shareholders' Meeting.

In compliance with this provision of the Company Bylaws, the Shareholders' Meeting held on 1 April 2005 resolved one share-based incentive plan that includes increasing the share capital according to the provisions in the subsequent paragraph "Powers to increase the share capital and authorizations for the purchase of treasury shares".

The Company did not issue other financial tools granting the right to subscribe newly issued shares.

Terna did not issue shares that were not negotiated on regulated markets of the EU.

### **Significant interests in share capital and shareholders agreements (pursuant to art. 123-bis, paragraph 1, letters c) and g) of the Consolidated Law on Finance)**

On the basis of the shareholders' book, communications received pursuant to CONSOB Resolution no. 11971/99 and available information, and with reference to the Company's share capital as of 31 March 2011, equal to € 442,088,020 for a total of 2,009,491,000 ordinary Terna's shares with a nominal value of € 0.22 each, the following investors hold more than 2% of the share capital: Cassa Depositi e Prestiti S.p.A. (public limited company in which the Italian Ministry of Economy and Finance of the Italian Republic owns 70%), with 29.858% of share capital; Enel S.p.A. with 5.095% of share capital; Romano Minozzi (directly and indirectly) with 4.424% of share capital; Pictet Funds (Europe) S.A. (directly and indirectly) with 2.826% of share capital; BlackRock Inc. (through BlackRock Investment Management (UK) Ltd) with 2.185% of share capital; Assicurazioni Generali (directly and indirectly) with 2.000% of share capital.

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

### **Powers to increase share capital and authorization for the purchase of treasury shares (pursuant to art. 123-bis, paragraph 1, letter m) of the Consolidated Law on Finance)**

During the extraordinary Shareholders' Meeting of 1 April 2005 the shareholders approved the assignment of a five-year proxy to the Board of Directors for a share capital increase for maximum € 2,200,000 through the issuance of maximum 10,000,000 ordinary shares with a nominal value of € 0.22 each, on a dividend-right basis, to be offered for subscription to Terna Group managers as payment with exclusion of the option right under the combined provisions of art. 2441, last paragraph, of the Civil Code and art. 134, paragraph 2 of the Consolidated Law on Finance, as provided for by art. 5.3 of the Company Bylaws.

Pursuant to the Shareholders' Resolution of 1 April, 2005, on 21 December 2005, Terna's Board of Directors adopted a share-based incentive plan. With reference to the adopted plan, the Board of Directors of 21 March 2007 partially exercised the above-mentioned proxy, approving a share capital increase regarding the 2006 Stock Option Plan up to maximum € 2,198,240.00 through the issuance of maximum 9,992,000 new ordinary Terna's shares with a nominal value of € 0.22 each, at € 2.072 each, to be implemented in compliance with art. 5.4 of the Bylaws. Based on the Resolution dated 22 April 2009, the latest date for the total subscription of the increase is 31 March 2013.

The 2006 Stock Option Plan is currently the only existing plan at Terna S.p.A.

The share-based incentive plan adopted by the Board of Directors following the Resolution dated 1 April 2005, is outlined in Terna S.p.A.'s 2010 annual report (paragraph "stock options" in the section "Equity" in the notes to the financial statements) in its 2009 annual report (pages 83, 148 and 243), 2008 annual report (pages 93, 248 and 249), 2007 annual report (pages 129 and 130), 2006 annual report (pages 54 and 121) 2005 annual report (pages 104 and following) - in the Company website [www.terna.it](http://www.terna.it) under the "Investor Relations/Annual Reports" section - and in the informative note of 14 September 2007 pursuant to art. 84-bis of Issuer Regulations - available at [www.terna.it](http://www.terna.it) under "The Company/Press Room - Price Sensitive Releases - 2007": all documents to which reference should be made.

No other power to increase capital has been assigned, pursuant to art. 2443 of the Civil Code.

No resolution authorizing the purchase of treasury shares under art. 2357 and following of the Civil Code has been submitted to Terna's Shareholders' Meeting.

Terna does not own, nor has purchased or sold during the year, not even indirectly, treasury shares or shares of its parent.

### **Employees' shareholding: system to express the right to vote (pursuant to art. 123-bis, paragraph 1, letter e) of the Consolidated Law on Finance)**

The system for exercising votes during the Shareholders' Meeting through shareholding associations, including employee's shareholding groups, is regulated based on the existing specific legal provisions on the subject.

Based on the provisions regarding the special legislation on listed companies, Terna's Bylaws introduced a special provision aimed at facilitating collecting voting proxies with its employees' shareholding groups as well as of its subsidiaries, encouraging in this way the relative involvement in the Meeting decision-making processes (art. 11.1 of the Bylaws).

As of 31 March 2011 the Company did not receive any notification of the establishment of employees' shareholding groups.

### **Change of control clauses (pursuant to art. 123-bis, paragraph 1, letter h) of the Consolidated Law on Finance)**

As regards significant agreements Terna or any of its subsidiaries are parties of and that come into effect, are amended or expire in the event of shareholding change within Terna, the following should be noted.

The agreement for a syndicated loan relative to the € 750 million revolving credit line granted to Terna S.p.A. by a bank pool, undersigned in 2006, provides that, as usual for this type of transactions, changes in Company's shareholding, pursuant to art. 2359, nos. 1 and 2, paragraph 1 of the Civil Code, could trigger early repayment of the credit line utilized along with the closure of the line itself, in the event of Company's credit rating decreasing below BBB- and the 2/3 of the financing banks deeming the loan refund necessary.

Furthermore, the loan contracts stipulated with the European Investment Bank (EIB), include mandatory advance repayment clauses, in the event the Company proceeds to or is involved in a merger, a split or transfer of a Company branch.

In such cases, the EIB will have the power of requesting, and the Company will have the obligation to inform the Bank, any information that the latter may reasonably require regarding the Company situation, in order to understand any changes and relative consequences in the Company's commitments towards the Bank. In such cases, should the EIB deem, according to its indisputable judgment, that these transactions may have negative consequences on the commitments undertaken by the Company, the bank itself will have the power to request the necessary changes in the loan contracts or alternative solutions that satisfy the Bank itself.



## Restrictions on share transfer and shares bearing special rights (pursuant to art. 123-bis, paragraph 1, letters b) and d) of the Consolidated Law on Finance)

No limitations under the Bylaws exist to the availability of shares except for the provisions stated by the Bylaws regarding rules for privatization based on the Law Decree no. 332 dated 31 May 1994 converted with amendments by Law no. 474 dated 30 July 1994 and subsequent changes – the so called “Privatization Law”.

In particular, pursuant to Italian regulations concerning privatizations, Terna’s Bylaws provides for the possibility for the Government to exercise certain “special powers” and establishes a “maximum limit of share ownership” – equal to a direct and/or indirect ownership of Terna shares for more than 5% of the share capital – for subjects other than the Italian Government, state-controlled companies and entities subject to either control: the implementation of those provisions, in some circumstances indicated by the Bylaws, has effects also on the voting right.

“Special powers” (indicated by art. 6.3 of the Bylaws, pursuant to art. 2, paragraph 1, of Legislative Decree no. 332 of 31 May 1994, converted with modifications by Law no. 474 of 30 July 1994 and following integrations and amendments – “Privatisation Law” – as provided for by art. 4, paragraph 227, of Law no. 350 of 24 December 2003) can be exercised by the Italian Government, represented in this case by the Ministry of Finance and Economy, notwithstanding the number of Terna’s shares potentially owned by the Ministry itself.

In particular, the Ministry of Finance and Economy, as agreed with the Ministry of Productive Activities (now called Ministry for Economic Development), is assigned the following “special powers”:

- a) opposition to significant interest (that are equal or higher than 1/20<sup>th</sup> of Terna’s share capital formed by shares granting right to vote in Shareholders’ Meetings) by entities subject to the ownership restriction presented above. The opposition must be expressed within 10 days from the date of the communication, which must be made by Directors at the request of subscription in the shareholders’ book, only when this may jeopardize the vital public interest. In the meantime, the right to vote and non-financial rights related to shares representing the significant interests, are suspended;
- b) opposition to shareholder agreements under the Consolidated Law on Finance, in case at least 1/20<sup>th</sup> of Terna’s share capital, including shares granting right to vote at Shareholders’ Meetings, is thereby represented. Opposition must be expressed within 10 days from the date of communication that must be made by CONSOB. In the meantime, the right to vote and non-financial rights related to shares of shareholders that are parties of the agreements, are suspended;
- c) veto, dutifully motivated, in relation to concrete jeopardy of the vital public interest, to the adoption of provisions for the winding-up of the Company, of transfer, merger, division, moving abroad of the registered offices, of Company Corporate purpose change, of Bylaws amendments suppressing or modifying powers indicated by the same art. 6.3 of the Bylaws;
- d) appointment of one Director with no right to vote. In case of termination of the assignment of the appointed Director, the Ministry of Economy and Finance, in agreement with the Ministry for Productive Activities (now called Ministry for Economic Development), will appoint the substitute.

The power of opposition under letters a) and b) can be exercised with reference to each aspect. It can also be exercised when ownership, also through single purchase acts, records an increase which is equal or higher than expectations. Such power can also be exercised every time the need to protect mandatory public interest arises, within ten days from their actual occurrence. In this case, the act of exercising the State power must include explicit and motivated reference to the date such causes arose.

The special powers under letters a), b), c) and d) are exercised with respect of the criteria provided for by the Prime Minister Decree of 10 June 2004.

The “maximum limit of share ownership” (provided for by art. 6.4 of the Bylaws and pursuant to art. 3 of Legislative Decree no. 332 of 31 May 1994, converted with modifications by Law no. 474 of 30 July 1994 and following amendments and additions (“Privatization Law”) is calculated also considering total share ownership related to the parent company, natural person or legal entity or company; to all direct and indirect subsidiaries as well as the subsidiaries under the same controlling subject; to all associated subjects as well as to natural persons bound by parental or affinity relationships up to second grade and by marriage, in the event that husband/wife are not legally separated. Control occurs, also with reference to subjects other than companies, in cases provided for by art. 2359, paragraphs 1 and 2, of the Civil Code. Association occurs in cases under art. 2359, paragraph 3, of the Civil Code, as well as between subjects who, directly and indirectly, through subsidiaries other than those managing common investment funds, join, also with third parties, agreements related to the exercise of the right to vote or to the transfer of shares or portions of third companies or, anyway, to agreements or pacts as per art. 122 of the Consolidated Law on Finance, with reference to other companies, if these agreements or pacts refer to at least 10% of the share capital with right to vote, in case of listed companies, or 20% in case of non-listed companies. With reference to the calculation of the above-mentioned limit of share ownership (5%), shares owned through trustees and/or through a third person and, generally, through an intermediary person are also considered.

Such limit of share ownership terminates, if exceeded due to a take-over bid carried out under articles 106 or 107 of the Consolidated Law on Finance.

The right to vote related to share ownership exceeding the above-mentioned maximum limit cannot be exercised and proportionally reduces the right to vote of each subject to whom the limit in share ownership refers to, except in the event



of joint communications by the involved shareholders. In case of non-compliance, decision can be appealed under art. 2377 of the Civil Code if the requested majority would not be achieved without the votes exceeding the above-mentioned limit. Shares for which the right to vote cannot be exercised are calculated anyhow for the regular formation of the Shareholders' Meeting.

#### **Voting restrictions (pursuant to art. 123-bis, paragraph 1, letter f) of the Consolidated Law on Finance)**

Pursuant to privatization regulations, restrictions exist (under articles 6.3 and 6.4 of the Bylaws) on votes related to the exercise of "special rights" of the Italian State and to the limits of share ownership as mentioned earlier.

Further restrictions are applied to operators of the electricity sector (as provided for by art. 3 of the Prime Minister's Decree dated 11 May 2004 as regards "criteria, modalities and conditions for the unification of ownership and management of the National Transmission Grid") for which a limit equal to 5% of the share capital was established for exercising the right to vote in case of Directors' appointment (art. 14.3, letter e) of Company Bylaws).

#### **Appointment and substitution of Directors and amendments to the Bylaws (pursuant to art. 123-bis, paragraph 1, letter l) of the Consolidated Law on Finance)**

##### **Appointment, requirements and term of office of Directors**

Terms for appointing members of the Board of Directors are ruled by art. 14 of the Bylaws.

The Board of Directors is made up of seven to thirteen members (art. 14.1 of the Bylaws) who are appointed for a period not longer than three years and 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.

Up to now the Italian Government never exercised the power to appoint.

The Chairman is appointed by the Shareholders' Meeting among the members of the Board (art. 16.1 of Bylaws and art. 2380-bis, paragraph 5 of the Civil Code). In case of impossibility, by the Board itself. The Board can appoint a Deputy Chairman. In no case such positions can be held by the Director appointed by the Italian Government under the Privatization Law (art. 16.1 of the Company Bylaws).

The appointment of the entire Board of Directors takes place – in compliance with the privatization regulation, under Prime Minister's Decree of 11 May 2004 and in compliance with the provisions of the Italian Law for listed companies – according to the mechanism of the "list voting", aiming at guaranteeing the presence in the management body of members designated by minority shareholders equal to 3/10<sup>th</sup> of the Directors to be appointed with rounding, in case of lower fractional number to the unit, to the following unit (art. 14.3 of the Bylaws).

On 18 October 2010, Terna's Board of Directors approved the amendments to the Bylaws necessary for adjusting the Company Bylaws to the novelties introduced by law provisions regarding shareholders' rights of listed companies aiming at favouring the participation of shareholders in the life of the Company (Directive 2007/36/EC and relative implementing Legislative Decree no. 27 dated 27 January 2010). Among other things, amendments involved art. 14.3 of the Bylaws regarding the appointment procedure for the Board of Directors and the terms and modalities for depositing the lists.

Such amendments will be applied for the first time on occasion of the next annual Meeting which will also have to resolve about the renewal of the expiring company bodies with the approval of the 2010 financial statements.

On the basis of the novelties and according to the Bylaws, the deposit and publication of lists are ruled by existing applicable laws.

Such appointment system – which does not apply to the appointment of a Director possibly indicated by the Italian Government – states – in line with the provisions of art. 4, paragraph 1-bis of Legislative Decree no. 332 dated 31 May 1994 converted into Law no. 474/94 (so called "Privatization Law"), modified by Legislative Decree no. 27, dated 27 January 2010, by art. 147-ter of the Consolidate Law on Finance and by the implementing rules of the above-mentioned law provisions, included in articles 144-ter and following of Issuer Regulations, – that the lists of candidates can be submitted by the outgoing Board of Directors or by shareholders who, alone or with other shareholders, represent at least 1% of the share capital, according to the law, or a lower amount, as established by the law, of shares with voting right in the meeting. On this matter CONSOB, implementing the provisions of art. 147-ter of the Consolidated Law on Finance and of articles 144-ter and following of the Issuer Regulations, with Resolution no. 17633 dated 26 January 2011 and for the year ended on 31 December 2010, established the participation stake necessary for submitting candidate lists for the appointment of Terna's administration and control bodies at 1% of the share capital, taking into account the Company's capitalization, floating capital and owned assets and without prejudice to the lower share contemplated by the Bylaws.

The lists shall be submitted and filed at least 25 days prior to the day set for the Shareholders' Meeting on first call.

Ownership of the minimum share required to submit lists shall be determined by taking into account the shares that are registered in the name of the shareholder(s) on the day in which the lists are filed with the Company.

In order to prove the legitimacy of presentation of the lists, entitled Shareholders must present and/or deliver the documentation proving the ownership of the number of shares required, even after the lists have been filed but within the time period set for

the publication of the lists (i.e., at least 21 days prior to the day set for the Shareholders' Meeting on first call).

Each shareholder may present or assist in the presentation of one single list and each candidate may be on one list only or he will be considered ineligible.

The lists must indicate candidates according to a progressive number and which of them are in possession of the independence requirements as provided for by the law and the Bylaws, and any other information or statement required by the applicable rules and regulations and the Bylaws pertaining to their respective offices. Together with each list, a statement shall be filed, whereby individual candidates accept their candidature and represent, under their responsibility, the inexistence of any of the causes for ineligibility and incompatibility, as well as any other information required by the applicable rules and regulations and the Bylaws.

On the basis of a specific clause in the notice of call for the Meeting and pursuant to art. 6 of the Governance Code, together with the lists, a detailed description of the candidates' personal and professional characteristics must be provided, accompanied by a statement indicating as to whether or not the candidates qualify as independent according to art. 3 of the Code of Conduct.

It is also provided that the lists, together with the information on the characteristics of candidates, are made available to the public at the registered office, on the Company's website and based on other modalities as provided for by CONSOB, at least 21 days before the Shareholders' Meeting, guaranteeing a transparent procedure for the appointment of the Board of Directors as recommended by art. 6.C.1 of the Code of Conduct of listed companies published by Borsa Italiana in March 2006 (Code of Conduct).

According to the provisions of art. 147-ter, paragraph 3 of the Consolidated Law on Finance, at least one of the members of the Board of Directors should be appointed by the minority list that has obtained the highest number of votes and is not connected in any way, not even indirectly, with the members who have submitted or voted the list that won for a number of votes. Shareholders that submit a "minority list" are the recipients of CONSOB Communication no. DEM/9017893 dated 26 February 2009 having as its subject "Appointment of the members of administration and control bodies".

In compliance with the provisions of Prime Minister's Decree dated 11 May 2004, the Bylaws envisage for operators of the electricity sector a limit equal to 5% of the share capital as regards the exercise of the voting right during the appointment of the Directors according to the above-mentioned rules.

Any replacement of Directors will be carried out pursuant to art. 2386 of the Civil Code.

In any case, the replacement of Directors whose office has ended will be carried out by the Board of Directors guaranteeing the presence of the necessary number of Directors in possession of the requirements of independence established by the law and by art. 15.4 of the Bylaws.

If the majority of the Directors appointed by the Shareholders' Meeting is not reached, the entire Board of Directors is considered as having resigned and the Shareholders' Meeting must be called without delay by the Directors still in office for appointing a new Board.

The Director must meet the requirements of honor, professionalism and independence.

The Company's Directors must meet certain honor and professionalism requirements, similar to those required by the Statutory Auditors of listed companies (art. 15.2 of the Bylaws).

The appointed Directors must immediately report the loss of requirement as per current regulations and according to the Bylaws to the Board of Directors, as well as any possible cause of ineligibility or incompatibility (art. 14.3 of the Bylaws).

As regards the requirements of professionalism, the Bylaws (art. 15.3) provides that those who have not accrued experience of at least three years in the following cannot be appointed as Director and, if so, they must resign:

- activities of administration, control or management in companies having a share capital not lower than € 2 million; or
- professional activities or university teaching in legal, economic, financial and technical-scientific subjects and closely related to the activities of the Company as defined in art. 26.1 of the Bylaws; or
- managing roles in public bodies or public authorities in the finance and insurance fields or, however, in fields closely related to that of the Company, as defined by the art. 26.1 of the Bylaws (subjects such as trade right, tax right, business economy and finance, as well as subjects linked to energy in general, communications and grid structures, are to be considered as closely related to the Company's scope of activities).

With stricter application compared to the provisions of art. 147-ter paragraph 4 of the Consolidated Law on Finance at least 1/3<sup>rd</sup> of the Directors in force must also be in possession of specific requirements of independence under art. 15.4 of the Bylaws that recalls the requirements of the Statutory Auditors indicated by art. 148, paragraph 3 of the Consolidated Law on Finance; furthermore, in line with the provisions of art. 3 of Prime Minister's Decree dated 11 May 2004, Executive Directors, taking into account the specific activity carried out by the Company, can be applied the independence requirements established by art. 10 of Directive 2003/54/EC as stemming from art. 15.5 of the Bylaws.

The presence of "independent" Directors as provided for by the 2006 Code of Conduct for listed companies of Borsa Italiana, becomes important in the composition of the Board Committees, as provided for by the Code itself and by the Committee for Related Party Transactions established within Terna for implementing the provisions of CONSOB Regulations that include provisions regarding related party transactions issued with Resolution no. 17221 dated 12 March 2010 and subsequently amended with Resolution 17389 dated 23 June 2010.

The Board of Directors assesses the presence of honor, professionalism and independence requirements, for every one



of its members and periodically assesses the presence of requirements of independence for every one of its non-executive members, on the basis of the information supplied by each member.

The Company is equipped with a specific internal procedure that defines the criteria for the assessment of independence of the non-executive members and for the assessment of the requirements necessary according to the Bylaws and the Code of Conduct ("Criteria of application and procedure for the assessment of independence of the Directors pursuant to art. 3 of the Code of Conduct"). Such procedure demands the assessment of requirements following the appointment, that is every time events take place that can interfere with the independence of a Director and however at least once a year (in the 30 days before the approval of the financial statements).

According to CONSOB recommendation with Communication no. 11012984 dated 24 February 2011, it should be noted that, taking into account Terna's owned assets and the concentration of ownership, no succession plan is envisaged for Executive Directors.

#### Bylaws - Amendments to the Bylaws

With regard to regulations applicable to the amendments to the Bylaws, the extraordinary Shareholders' Meeting resolves on the matter with the majority envisaged by the law.

The Bylaws (art. 21.2), according to law provisions, attributes the Board of Directors the power to adopt any resolutions pertaining to the Shareholders' Meeting that can determine Bylaws amendments such as:

- a) the merger and the split, in cases envisaged by the law;
- b) the establishment or elimination of other offices;
- c) stating which of the Directors represents the Company;
- d) the reduction of the share capital in case one or more members withdraws;
- e) the amendment of the Bylaws according to regulations;
- f) the transfer of the Company headquarters in the national territory.

art. 6.3 of the Bylaws, in compliance with the regulations on privatization, attributes to the Italian Government, represented for this purpose by the Ministry of Economy and Finance, the "special power" to veto, duly motivated with reference to effective detriment of the Government's vital interests, on the adoption of a series of resolutions adopted by the Shareholders' Meeting of significant impact on the Company, capable of amending the Bylaws, as previously described in "Restrictions in share transfer and shares granting special powers".

Furthermore, as provided for by art. 3, paragraph 3 of Legislative Decree no. 332 of 31 May 1994, converted with modifications by Law no. 474 of 30 July 1994 and art. 3, paragraph 2, letter c) of the Prime Minister's Decree dated 11 May 2004, Terna's Bylaws provide that the measures as per art. 6.4 of the Company Bylaws relative to the above-mentioned "maximum limit of share ownership" as described under "restrictions in share transfer and special powers" and those included in the Bylaws that have the purpose to ensure protection of the share minorities, cannot be modified for a period of three years from the date of effectiveness of the transfer to Terna of the activities, functions, assets and obligations relative to the management of the National Transmission Grid as per art. 1, paragraph 1 of the Prime Minister's Decree dated 11 May 2004 (1 November 2005).

#### **Indemnities for Directors in case of resignation, discharge or cessation of relation following a public take-over bid (pursuant to art. 123-bis, paragraph 1, letter i) of the Consolidated Law on Finance and to CONSOB Communication no. 11012984 dated 24 February 2011 comma 2.3)**

With reference to the agreements entered into between Terna and the Directors that provide indemnities in case of resignation or dismissal/revocation of assignment with no just cause, following the renewal of the Board of Directors resolved by the Shareholders' Meeting held on 28 April 2008, it is pointed out that:

- a) agreements exist regarding the financial compensation recognized to Terna's CEO, who is also an employee of Terna S.p.A. as a manager, on the basis of which indemnities are envisaged in case of early resignation from the appointment. No other indemnities are envisaged in case of termination of the work relation for the other members of the Board of Directors;
- b) on the basis of criteria established as part of these agreements, it should be noted that the Company will pay:
  - for the administration relation pursuant to art. 2389 of the Civil Code, an amount equal to the total emoluments expected up to the expiration of the mandate (as agreed upon, 31 May 2011) as fixed compensation, variable compensation (equal to 50% of the fixed compensation) and severance pay (TFM) (equal to 1/12 for each year of the total emoluments received during the mandate as Director);
  - for the employment relation, an amount as incentive to leave, equal to 3 year compensation defined as the fixed compensation plus variable compensation (40-60% of fixed compensation) and long term incentive "cash" (equal to 50-75% of the fixed compensation);
- c) in case of termination of the work relation, keeping subscription rights for the Company's shares assigned by virtue of the employment relation will be guaranteed in retirement situations or if the work relation is terminated due to permanent disability. Such rights will contrarily be lost in case of termination of the work relation due to voluntary resignation or

- revocation for a just cause or justified subjective reason;
- d) the right to the indemnity accrued in case of early termination of the assignment and with the exception for situations of voluntary resignation (not requested by the majority shareholder) or of revocation for a just cause;
- e) within the above-mentioned agreements, assigning non monetary benefits is not envisaged. Furthermore, entering consulting agreements is also not envisaged;
- f) compensation for non-competition agreements are not included in such agreements.

## Management and coordination

Terna is subject to the de-facto control of Cassa Depositi e Prestiti S.p.A. with 29.858% of the share capital. The assessment, from which the existence of such control emerged, has been carried out by Cassa Depositi e Prestiti S.p.A. and made public on 19 April 2007. As of today, no managing and coordination activity has been officialised nor exercised; Terna carries out its activity either directly or through its subsidiaries under management and negotiation independence. The additional information on the Company's Corporate Governance envisaged in art. 123-bis, paragraph 2 of the Consolidated Law on Finance regarding:

- compliance, (pursuant to art. 123-bis, paragraph 2, letter a) of the Consolidated Law on Finance) are illustrated in the section of the report devoted to compliance (section III);
- the principal characteristics of existing risk management and internal controls over financial reporting, also consolidated (pursuant to art. 123-bis, paragraph 2, letter b) of the Consolidated Law on Finance), and further Corporate Governance practices (pursuant to art. 123-bis, paragraph 2, letter a) of the Consolidated Law on Finance) are illustrated in the section of the report devoted to internal control system (section XI) and in Attachment 1 therein;
- the Shareholders' Meeting activity (pursuant to art. 123-bis, paragraph 2, letter c) of the Consolidated Law on Finance) in the section of the report devoted to the Shareholders' Meeting (section XVI);
- the composition and the role of the Board Members as well as those relative to the appointment and composition of the control body (pursuant to art. 123-bis, paragraph 2, letter d) of the Consolidated Law on Finance), are illustrated in the report respectively in the section devoted to the Board of Directors (section IV) and in subsequent sections devoted to the Board's Internal Committees (sections VI, VII, VIII and X) and in the sections devoted to the appointment and composition of the Board of Statutory Auditors (sections XIII and XIV).

## Section III Compliance

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The Corporate Governance system of the Company is substantially in line with the principles included in the Code of Conduct of listed companies published by Borsa Italiana in March 2006 (which can be consulted in Borsa Italiana S.p.A.'s website: <http://www.borsaitaliana.it>) that Terna has adopted, as illustrated before, with Resolution by the Board of Directors of 21 December 2006.

Further action aimed at improving the Group's system of governance are being carried out and others will be taken into consideration for the constant update and adjustment of the issuer's governance system to the best practices.



## Section IV Board of Directors

### Composition

In compliance with the Shareholders' Resolution passed during the ordinary Meeting held on 28 April 2008, the Board of Directors currently in office is comprised of nine members, whose term will expire with the approval of the financial statements as of 2010.

In compliance with the Shareholders' Resolution passed during the ordinary Meeting held on 28 April 2008, the Board of Directors currently in office is composed of Luigi Roth, Flavio Cattaneo, Cristiano Cannarsa, Paolo Dal Pino, Matteo Del Fante, Michele Polo (Directors appointed within the majority list submitted by Cassa Depositi e Prestiti S.p.A.), Claudio Machetti (Director appointed within the minority list submitted by Enel S.p.A.), Salvatore Machì and Vittorio Rispoli (Directors appointed within the minority list submitted by the Assicurazioni Generali Group). The appointed Board Members represent three of the four lists presented for this Shareholders' Meeting.

On the basis of the statements made for the appointment, of the vote count and of the end of voting, the appointed Board of Directors meets the requirements envisaged by art. 147-ter, paragraph 3 of the Consolidated Law on Finance and two members of the Board of Directors were appointed by the minority list that has obtained the highest number of votes and is not connected in any way, not even indirectly, with the members who have submitted or voted the list that won for a number of votes.

Since its appointment, the Board's composition has remained unvaried. A brief description of the Board members' professional background is provided:

- **Luigi Piergiuseppe Ferdinando Roth, 70 years old – Chairman**

[born in Milan on 1 November 1940]

With a degree in Business Administration from the Luigi Bocconi University, Milan, he is a registered auditor. Since November 2005, he has been Chairman of Terna S.p.A. and since November 2009, he has been Chairman of TELAT S.r.l. a subsidiary of Terna S.p.A.. Since April 2007, Mr. Roth has been Independent Director at Pirelli & C. S.p.A. and since April 2009 he has been President of Banca Popolare di Roma (CARIFE Group).

Mr. Roth began his career as a business manager with the Pirelli Group, handling activities in Italy and abroad. He then joined Metropolitana Milanese as Director of Planning. Since 1980, he has managed mid-sized companies both in the manufacturing and real estate sectors, in the positions of General Manager and CEO. From 1986 to 1993, he served as CEO at Ernesto Breda S.p.A.; from 1993 to 2001 he was Chairman and CEO of Breda Costruzioni Ferroviarie S.p.A. From April 1996 to January 1998, he was Chairman of Società Ferrovie Nord Milano S.p.A. of which he was CEO from December 1996 to January 1998. From December 1996 to January 1998 he was Chairman and CEO of Società Ferrovie Nord Milano Esercizio S.p.A. From May 1998 to December 2000 he was CEO of Ansaldo Trasporti S.p.A. and transmission agent for Finmeccanica S.p.A. From 2002 to 2006, he was Board Member at the Luigi Bocconi University. From January 2004 to April 2007 he was Deputy Chairman at Cassa Depositi e Prestiti S.p.A. From May 2004 to April 2007 he was Board Member at Telecom Italia S.p.A. and from 2001 to 2009 he was President of the Fondazione Fiera Milano. From May 2006 to November 2009 he was Deputy Chairman of Terna Participações SA, a subsidiary of Terna S.p.A.

- **Flavio Cattaneo, 47 years old – CEO**

[nato a RHO (MI) il 27 giugno 1963]

With a degree in Architecture from the Milan Politecnico, Mr. Cattaneo has also received specialized training in business management. Since November 2005, Flavio Cattaneo has been CEO of Terna S.p.A. Since January 2008 he has been Independent Director in Cementir Holding S.p.A. Since October 2008, he has been Deputy Chairman in Charge of Energy and Environmental Policies at UIR, Union of Industrialists and Companies in Rome.

He has held 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 S.p.A., serving as Chairman and CEO until 2003. Flavio Cattaneo has been Director of many energy companies (from 1999 to 2001), including AEM S.p.A. of Milan (as Deputy Chairman), Serenissima Gas S.p.A., Triveneta Gas S.p.A., Seneca S.r.l. and Malpensa Energia S.r.l.. He was appointed head of Italy's public television network RAI S.p.A. 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. From May 2006 to November 2009 he was Chairman of Terna Participações SA, a subsidiary of Terna S.p.A.

- **Cristiano Cannarsa, 48 years old – Director**

[born in Rome on 16 February 1963]

With a degree in Mechanical Engineering from "La Sapienza" University in Rome and specialized in his profession, he is the Director of the Loan Department at Cassa Depositi e Prestiti S.p.A. Since 2005 he has been a member of the Economic and Financial Group of the Intergovernmental Commission for the Turin-Lyon railway line.

He has held positions of increasing responsibility and coordination in companies specialized in Corporate Finance, Project Finance and Advisory. After several years of experience in the renewable energy sector with Aeritalia, in 1991 he joined the Istituto Mobiliare Italiano acquiring experience in industrial Corporate investment projects, public bodies and project companies; subsequently, within the Sanpaolo IMI Group, he became Head of the Large Infrastructure Department of Banca OPI and Head of the Public Financial and Corporate Department. As a member of the TAV S.p.A. financial-technical Committee, between 1992 and 1996, he participated in the High-Capacity/High-Speed Project.

• **Paolo Dal Pino, 48 years old – Director**

[born in Milan on 26 June 1962]

He has a degree in Economics from the University of Pavia. He is presently Senior Advisor of the Private Equity Cyrt Investments fund and Board member at Banijay Holding S.a.S.. From January 2006 to June 2007 he has been CEO of Wind Telecomunicazioni after having been CEO at SEAT Pagine Gialle from July 2001 to 2004, and Chairman of Telecom Italia in Latin America and Chairman of Tim Brazil from February 2004 to 2005.

From 1990 to 2001 he has held various positions within the Espresso Group, among which – from 1991 to March 1995 – that of Financial Director of Editoriale la Repubblica S.p.A. and from 1995 to July 2001, of General Director of the Gruppo Editoriale L'Espresso, CEO of Kataweb S.p.A. and Director and member of the Executive Committee at ANSA. In 1986, he began his career in the Fininvest Group and from 1987, until 1990, he joined the Mondadori Group where he was CFO of the Verkerke Group in The Netherlands.

• **Matteo Del Fante, 43 years old – Director**

[born in Florence on 27 May 1967]

He has a degree in Economic Policy from the Bocconi University in Milan. He began his career at J.P. Morgan in 1991 holding positions of increasing responsibility for Italy and for foreign countries in the sector of fixed income markets. From 1999 to 2003, as Managing Director in London, he managed significant financial and strategic operations in Europe. Since June 2010 he has been General Director of Cassa Depositi e Prestiti S.p.A., where he previously was Head of the Financial Department and of the Real Estate Department.

Since July 2010, leaving the position of CEO, he took on the position of president of CDP Investimenti SGR, which is involved in the real estate sector. Since June 2008 he has been Chairman of the Supervisory Board of STMicroelectronics Holding N.V. and since May 2007 he is Board member of the consulting firm SINLOC, a subsidiary of bank-based foundations.

• **Claudio Machetti, 52 years old – Director**

[born in Rome on 30 October 1958]

Mr. Machetti has a degree in Statistics from “La Sapienza” University in Rome. In March 2000 he has been appointed head of the Financial Department at Enel S.p.A. and in 2005 Financial Director. Since July 2009, he has been Chief Risk Officer. Within the Enel Group, he also served as Chairman of the Board of Directors of: Enel New.Hydro S.r.l., Enel Energy Europe S.r.l., Enel Capital S.r.l. (to be wound up) and as Director at: Enel Investment Holding BV, Enel Ireland Finance Ltd, Enel Re Ltd, Enel Trade S.p.A., Enel Distribuzione S.p.A., Enel Produzione S.p.A. and in the listed company Endesa SA. He began his managerial career in 1983 in the Financial Department of Banco di Roma. From 1992 to 2000, he held various positions with Ferrovie dello Stato S.p.A. (head of the Financial Markets Central Service, then Operating Finance Manager) taking over Fercredit S.p.A. in the FS Group as CEO in 1997. From April 2004 to November 2005 and then from March 2007 he was Director of Terna S.p.A.

• **Salvatore Machi, 73 years old – Director**

[born in Palermo on 28 May 1937]

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 held various positions up to 1999, including Manager of the Transmission Department, National Manager of Thermoelectrical Energy Generation and Procurement Manager. He was CEO (from July 1999 to April 2000) and, then, Chairman (up to July 2003) of the Gestore della Rete di Trasmissione Nazionale S.p.A., and Director of Gestore del Mercato Elettrico S.p.A. during that time.

He has been Chairman of the Board of Directors of CESI S.p.A. since March 2003, where he previously (from July 1999 to October 2001) served as CEO. He is currently Director of Api Energia S.p.A. and, since September 2004, a Director of Terna S.p.A. as well.

• **Michele Polo, 53 years old – Director**

[born in Milan on 7 August 1957]

He has a degree in Economics from the Luigi Bocconi University in Milan, and graduated in Economic Policy with a Masters in Economic Sciences from the London School of Economics. From 2003 he has been Ordinary Professor of Economic Policy and from 2007, Vice-Chancellor at the Luigi Bocconi University. He is a member of the Board of Directors of the



Institute for Economics and Policy of Energy and the Environment (IEFE) of the Bocconi University and carries out other scientific and academic activities: he is Director of the Journal of Economists and member of the Editors Committee of Economy of Energy Sources and the Environment and of the Editor's Committee of Market, Competition, Regulations. He is scientific advisor of the publishing house "Il Mulino", in Bologna. From 2003 to 2006 he was Economic Advisor of the General Department of Competition of the European Commission. He is also the author of numerous essays and monographs on themes such as antitrust, liberalization and energy sectors.

• **Vittorio Rispoli, 51 years old – Director**

[born in Soverato (Catanzaro) on 31 May 1959]

With a degree in Law from "La Sapienza" University in Rome, he is a lawyer and a registered auditor. Since November 2007 he has been General Manager and CEO of Fata Assicurazioni Danni S.p.A. and Fata Vita S.p.A. (Generali Group). He was also Director in subsidiaries of the insurance companies of the SARA Group (SARA Assicurazioni S.p.A. – SARA Vita S.p.A. – MC Gestioni). Manager since 1987, he has held various managerial positions, essentially in the legal and Corporate areas at first in the IRI Group (SOFIN S.p.A. and Alitalia S.p.A.) until 1997 and, subsequently, in the insurance field (INA-Assitalia and Generali). He has carried out, for approximately ten years, assignments of contract teaching at the Universities of Rome, Perugia and Cassino in Public Law and Economics, Civil Law and Insurance Law.

Upon appointment, the Board of Directors has confirmed the existence of the requirements of honor and professionalism held by each of its members.

The evaluation regarding the existence of the requirements of independence for each of the non-executive members was made, taking into account the information provided by each person, during the appointment and annually, and lastly during the Meeting held on 31 March 2011 according to the terms stated in the following paragraph "Independent Directors". The attached table 1 includes the information regarding the composition of the Board of Directors as of 31 March 2011.

**Maximum number of positions in other companies**

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 (also abroad), financial companies, banks, insurance companies and significantly large companies – and 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, in compliance with art. 1.C.3 of the Code of Conduct, Terna's 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 still enabling the efficient performance of the duties as Director of Terna S.p.A. included in the internal document "Orientations of the Board of Directors over the maximum number of positions as a Director or Auditor compatible with the assignment of Director of Terna S.p.A.". To 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 the prudent supervision by the Bank of Italy and registered within the special list provided for by art. 107 of Legislative Decree no. 385/1993 (so called "Consolidated banking act"); foreign companies are evaluated on the basis of 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 € 50 million or an annual financial statements total of € 43 million; companies that draw up consolidated financial statements.

The Board has identified different general criteria for the 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 (which, originating from the assignment itself, are not calculated in the total number). 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 at Terna is incompatible with the same role in other significantly large companies.

When 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 in office that were appointed by the Meeting on 28 April 2008, informed about the positions they held at the time the lists were submitted and subsequently when they accepted their appointment. Based on the updated information delivered to the Company in compliance with the approved guidelines, at 31 March 2011 all Directors hold a number of positions that is compatible with the guidelines set by the Board.

In the summaries of each Director's personal characteristics, all the positions held by them are indicated. The total number

of positions held as Directors or Statutory Auditors in significantly large companies is provided in the attached table 1. There have not been exceptions, issued by Terna's Shareholders' Meeting, to the prohibition of competition by the Directors provided for by art. 2390 of the Civil Code.

## Role of the Board of Directors

The Company's Board of Directors holds a crucial role in its organization. It has strategic and organizational functions and responsibilities with respect to the Company and the 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 addition to exercising the powers that are attributed to it by the law, the Company's Bylaws (art. 21.1) attributes the Board the competence to resolve on issues pertaining to the Shareholders' Meeting that can determine amendments to the bylaws as previously described in "Bylaws amendments."

Within the limits as per art. 2381 of the Civil Code, the Board of Directors may delegate its tasks to an executive Committee and/or to one or more of its members (art. 22.1 of the Bylaws).

In this context and in compliance with the law and the provisions of specific resolutions, and considering the provisions of art. 1 of the Code of Conduct, the Board of Directors carries out the following:

- 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 assigned to him give the CEO the widest powers for the administration of the Company, except for those assigned by the law or the Bylaws or reserved for the Board of Directors by resolutions thereof (art. 1.C.1, letter c) of the Code of Conduct);
- receives, similarly to the Board of Statutory Auditors, constant and exhaustive updates from the CEO on activities performed during the year in compliance with powers, through specific quarterly reports. In particular, with respect to all significant transactions carried out by the Company and its subsidiaries (including any related party transactions of lesser importance as identified in the specific Procedure adopted by Terna, which do not require approval by the Board of Directors) the CEO reports to the Board of Directors on their (I) characteristics of the transactions, (II) the parties involved and their relationship with the Company or its subsidiaries (art. 1.C.1, letter c) of the Code of Conduct);
- on the basis of proposals made by the specific Committee and with the approval of the Board of Statutory Auditors, determines the remuneration of the CEO and of other Directors with special duties (art. 1.C.1, letter d) of the Code of Conduct);
- evaluates the adequacy of the general organizational, administrative and accounting structure of the Company and its subsidiaries that hold strategic importance (in compliance 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, whose guidelines are defined by the Board, and to the management of conflicts of interest (art. 1.C.1, letter b) of the Code of Conduct). The adequacy and actual operation of the Terna Group's Internal Control System is reviewed at least on an annual basis. With regard to this matter, reference should be made to section XI;
- 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) (art. 1.C.1, letter a) of the Code of Conduct);
- defines the Corporate Governance system within the Company, provides for the appointment, role definition and rules of the Board's Internal Committees (art. 1.C.1, letter a) of the Code of Conduct);
- 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 such cases the support of the Internal Control Committee is provided as well as of the Committee for Related Party Transactions. In particular, the following significant transactions, *inter alia*, are submitted to the Board of Directors in advance: "significant transactions" carried out also through subsidiaries for which the underlying item, consideration, method or timing could have an impact on safeguarding the Company assets or the completeness and accuracy of Terna's accounting and other information which require Terna to disclose to the public an informative document in compliance with the supervisory authorities of financial markets and/or transactions for more than € 50 million, except for those approved in the budget and in financial plans as well as in agreements relating to dispatching and all other related services; subscription of loans, granted and received, of any type, medium and long term, for an amount exceeding €100 million that were not included in the approved budget and financial plans and not aiming at implementing measures that were already approved by the Board in the National Electricity Transmission Grid's Development Plan (art. 1.C.1, letter f) of the Code of Conduct);
- resolves regarding the establishment of new companies, the purchase and transfer of shares in companies, namely in companies or company branches with a value exceeding € 30 million euros (art. 1.C.1, letter a) of the Code of Conduct);
- 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 the Internal Control Committee, periodically checking that planned results have been achieved (art. 1.C.1, letter e) of the Code of Conduct);

- at least once a year, evaluates the size, composition and performance of the Board of Directors and its Committees (art. 1.C.1, letter g) of the Code of Conduct);
- reports to the shareholders during the Meeting.

The activities of the Board of Directors are coordinated by the Chairman. The latter summons the Board's Meetings, sets the agenda upon request by the CEO and guides Meeting's running, making sure that the Directors are timely provided with the documentation and the necessary information so that the Board can consciously express on the matters submitted to examination. Moreover, he verifies compliance with resolutions, chairs the Meeting and – in the same way as the CEO – has powers of legal representation of the Company.

### Board of Directors Meetings

The Directors gather regularly and carry out tasks based on their full knowledge and in autonomy, pursuing the objective of creating value for shareholders, taking into account the social aspects of the Group's activities and the resulting need to adequately consider all stakeholders in the performance of those activities.

During 2010, the Board met 8 times and each Meeting lasted an average of one hour and ten minutes with the Directors regularly participating as well as the Board of Statutory Auditors (art. 1.C.1, lett h) of the Code of Conduct).

For 2011, a Board Meeting is expected every month and all the Meetings have been scheduled relative to the examination of the economic and financial data by the Board of Directors according to what was officially communicated to the market on 31 January 2010. In the current year and as of the date of approval of the present report, the Board of Directors met 2 times.

### Assessment of the Board of Directors activity

In compliance with the Code of Conduct published by Borsa Italiana, Terna's Board of Directors also for 2010 assessed the Board size, composition and performance, as well as that of its Committees. The Board conducted such assessment, drawing on the assistance of the company Egon Zehnder International S.p.A. as an external consultant to ensure the utmost objectivity of its evaluations. This initiative follows similar ones that were undertaken by Terna's Board of Directors as of 2006.

The independent consultant's analysis started during the first quarter of 2011 and was carried out through qualitative questionnaires and individual interviews with each Director and through subsequent analysis of the information gathered; it focused on numerous aspects regarding: a) the efficiency of processes; b) the analysis of tasks within the Board; c) the development of the Board's strategic orientation and d) strong communication among the CEO, the Chairman and Directors. Such analysis highlighted how Terna's Board of Directors is totally in line with the Governance Code to the point that it fully represents a best practice both at the Italian and international level.

On the basis of the results of the analysis carried out, the Board of Directors passed an overall positive evaluation on the size, composition and performance of the Board and its Committees having positively evaluated all the principal profiles examined and committed to exercising their role as best as possible.

In particular, the Board having deemed that the Board's operation during 2010 confirmed its high efficiency level and the general trend to continuously improve some organizational issues, recognized the need to implement improvements for: a better coordination of strategic issues and investments; a stronger commitment on the part of the Top Management to involve the Board; a better atmosphere within the Board together with improved interpersonal relations; greater information on trends and investments regarding the technical and operational fields; appreciating the preliminary work carried out by the Committees, in particular the Internal Control Committee for creating greater exchange opportunities.

### Delegated bodies and other Executive Directors

#### CEOs

The current structure of the Board of Directors provides for only one CEO, to which the Board has attributed powers, defining their content, limits and any exercise modalities; no executive Committee was established.

The CEO has powers of legal representation of the Company and is entrusted with the widest powers for the administration of the Company, pursuant to Board Resolution, with exception of those differently attributed by the law, by the Bylaws or reserved for the Board of Directors.

The CEO informs the Board of Directors and the Board of Statutory Auditors of the activities and of the management of the Company as well as of the resolutions passed in exercising his powers pursuant to art. 21.3 of the Bylaws, at least on a quarterly basis and on occasion of Board Meetings.

On a quarterly basis, specific reports are prepared in order to inform the Board on major action and activities.

In addition, the Directors are kept constantly informed by competent departments on the main legislative and regulatory innovations concerning the Company and the exercise of own functions. On occasion of the appointment, they are adequately informed about the existing system of Company governance and the fundamental lines of governance.

Exception made for the CEO, the other 8 members of the Board of Directors (Luigi Roth, Cristiano Cannarsa, Paolo Dal Pino, Matteo Del Fante, Claudio Machetti, Salvatore Machi, Michele Polo, Vittorio Rispoli) must all be considered as non-executive. It must be noticed that also the Chairman does not play an executive role, since no proxies are attributed to him.

For their number, competence, authority and availability of time, the Non-executive Directors (since they are not provided with operating proxies and/or managing roles in the Company) are capable of guaranteeing that their judgment can have a significant weight in Board's decisions in line with what provided for by the Code of Conduct (art. 2.P.3 of the Governance Code).

The Non-executive Directors enrich with their specific competences the Board's discussions, so as to favor the examination of the subjects according to various perspectives and subsequently pass deeply analyzed, conscious and respectful resolutions in line with social interests.

During 2010 and up until the date on which this Report was approved, the Directors participated in specific Meetings with the Company's management in relation to the core business activities with particular reference to the preparation of the development plan for the National Transmission Grid.

#### Independent Directors

A suitable number, also for competence, of Non-executive Directors is independent.

The Board of Directors has evaluated the existence of the requirements of independence provided for by the law, the Bylaws and the Code of Conduct which Terna has adopted, for each Director in the first useful occasion after their appointment and on an annual basis. Moreover, the Board of Directors' Meeting of 31 March 2011 – on the basis of the criteria previously defined for the assessment of independence of the non-executive members, in compliance with the criteria indicated by the Code of Conduct and on the basis of the information supplied by the persons involved – confirmed the existence of the requirement of independence in each of the 4 Non-executive Directors: Paolo Dal Pino, Salvatore Machi, Michele Polo, Vittorio Rispoli (articles 3.C.1, 3.C.2 and 3.C.4 of the Code of Conduct).

At the same time, the correct application of the defined criteria and the procedures adopted by the Board of Directors was verified by the Auditors (art. 3.C.5 of the Code of Conduct).

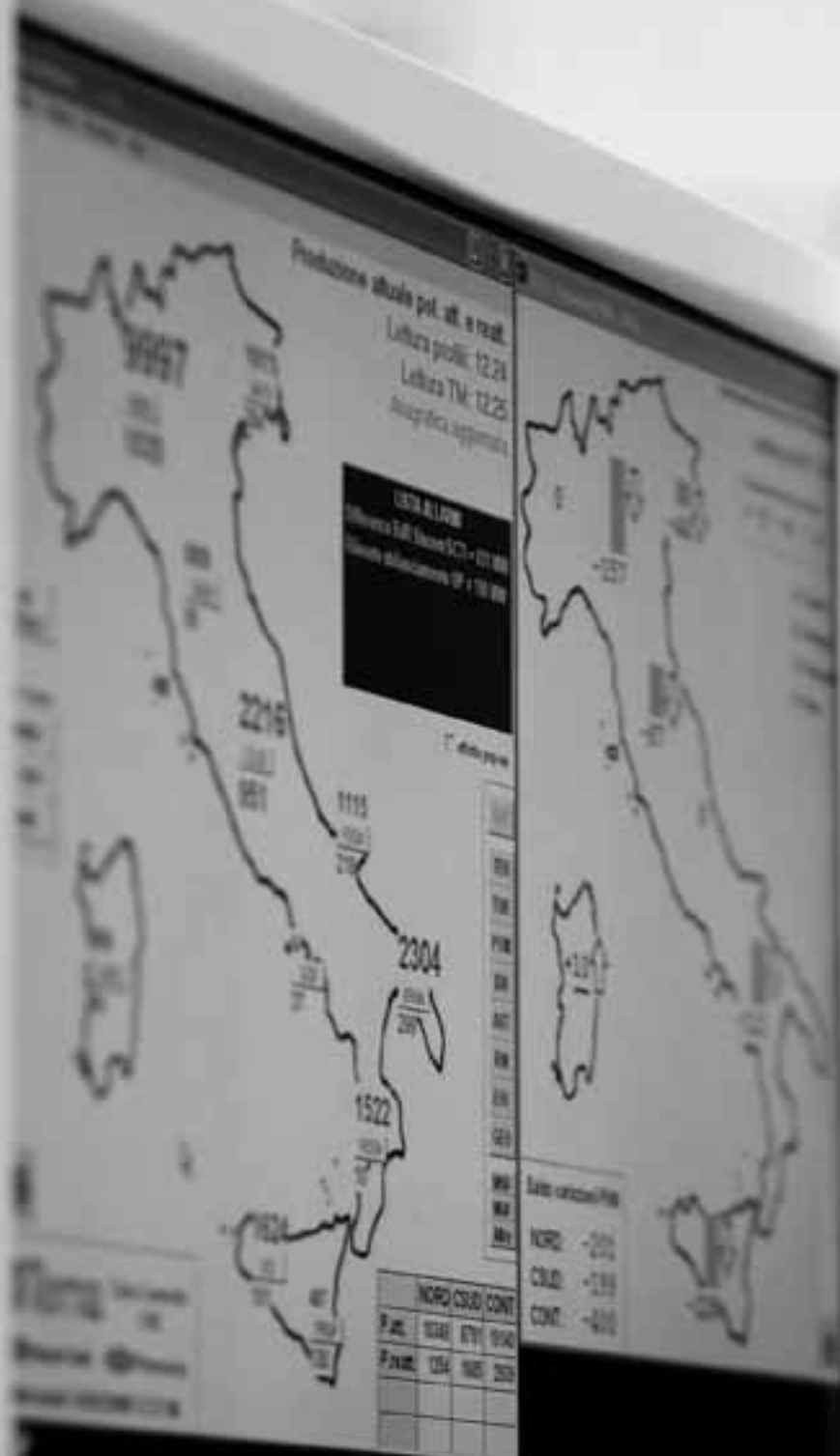
Although independence characterizes the activity of all the Directors, executives and non-, the presence of Directors that can be qualified as "independent" in compliance with the above-mentioned criteria, and whose role is significant both within the Board and its Committees, suitably ensures adequate consideration of all shareholding members' interests.

Among the assessments carried out by the Board, with reference to the 4 Directors, the existence is proven of the requirement of independence envisaged for in art. 15.4 of the Bylaws that demands that at least 1/3<sup>rd</sup> of the Directors in force – with rounding, in case of fractional number lower than the unit, to the following unit – meets the requirements of independence established for Statutory Auditors by art. 148, paragraph 3, of the Consolidated Law on Finance.

Following the work method of the Board of Directors, and the presence of Independent Directors in the composition of the Committees, in the operating system a constant exchange of information between the same Independent Directors has been taking place, both at Meetings of the Internal Committees and at the Board's Meetings, which has not required a specific Meeting to be held for them.

#### Lead Independent Director

The work method of the Board of Directors has assured the suitable coordination of the contributions and the requests of the Non-executive Directors and, in particular, of the Independent Directors; it also guaranteed a preventive exchange of information that rendered the work of the Board productive and focused on the true requirements of the Company. On the basis of such assumptions, confirmed by the outcomes of the Board review which the Board is subject to, and since the assumptions indicated by the Code of Conduct are not present, the position of Lead Independent Director was not established within Terna.





## Section V Management of confidential information

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During the Meeting of 21 December 2006, the Company's Board of Directors, in compliance with the provisions on the management of privileged information aimed at preventing insider trading and with the provisions of art. 4 of the new Code of Conduct, of art. 114, paragraph 1, and of art. 181 of the Consolidated Law on Finance, approved a specific regulation for the management and treatment of confidential information, which also includes the procedures for disclosing documents and information on the Company and its subsidiaries outside of the Company, with specific reference to the confidential information provided for by paragraph 1, art. 114 of the Consolidated Law on Finance.

This regulation represents an update to the measures included in the regulation that Terna approved as of April 2004, with specific reference to "price sensitive" information. It aims at maintaining 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 relating to Company's data. 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 bodies of the subsidiaries with the 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 mass communication means (i.e. financial analysts and Institutional Investors).

Lastly, the new regulation introduced specific "Measures for persons committing violations" into the regulation's provisions.

In compliance with the provisions of art. 115-*bis* of the Consolidated Law on Finance and with 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 should be held and updated. The same regulation requires that subsidiaries also create their own lists.

As of 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 S.p.A., establishing the market transparency requirement for listed companies with respect to significant transactions, involving the financial instruments of the Company or its subsidiaries, carried out by people with significant decision-making powers in the Company and with access to price sensitive information ("relevant persons").

Following the entrance into force of the new internal dealing regulations that were introduced by Law no. 62 dated 18 April 2005 ("2004 Community Law" that integrated the provisions of art. 114 of the Consolidated Law on Finance) and of the relative implementing provisions (articles from 152-*sexies* to 152-*octies* and Attachment 6 of the Issuer Regulations), Terna adopted a specific internal procedure to identify Terna's "relevant persons" and to manage, handle and disseminate to the market information regarding financial instruments of the Company.

Within this Procedure – that was updated on 19 March 2010 based on CONSOB explanations and on the structural asset of the Company – Terna deemed appropriate to maintain, for the "relevant persons" identified, the obligation to refrain – either directly or indirectly – from carrying out transactions that are subject to internal dealing regulations during two blocking periods in concomitance with the approval of the draft financial statement and of the half-year report by Terna's Board of Directors.

This procedure is available in the Company's website [www.terna.it](http://www.terna.it) in the "Investor Relations/Corporate Governance /Internal Dealing" section. The procedure includes the following qualifying elements, which are considered adequate in heightening the qualitative content:

- application of internal dealing transparency obligations towards "relevant persons" within the Company and its subsidiaries as identified in the procedure (in addition to Terna's actual Directors and Standing Auditors);
- "relevant persons" are not allowed to carry out transactions (other than the exercise of options) during the 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 violating the measures of this procedure.

## Section VI Committees within the Board

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Within the Board of Directors, the Remuneration Committee and the Internal Control Committee have been set up, both with proposal-making and advisory functions, and made up of at least three Directors, the majority of which independent, pursuant to Code of Conduct.

The Committees have been attributed the tasks provided for by the Code of Conduct. The criteria for the composition, the tasks and the responsibilities attributed in compliance with the Code of Conduct and the modalities of carrying out the Meetings have been ruled through proper internal organization regulations adopted by the Board of Directors as of 24 January 2007. The Meetings of the Committees include the drawing up of minutes. Each Committee has also the faculty to access the information and the necessary departments to carry out its tasks and can use possible external advisors in the limits provided for by the Board of Directors.

Within the Company budget, adequate financial resources are allocated for the implementation of the tasks of each Committee.

On invitation of the coordinator of each Committee, other subjects, whose presence can contribute to the best performance of the Committee, can participate in the Meetings.

During 2010, the Board of Directors created another Committee having advisory and consulting tasks, formed by at least three Directors, all independent, according to the provisions of the Governance Code, with the task of expressing its preliminary opinion necessary for the adoption of the Procedure for Related Party Transactions as established by the "Regulations regarding provisions for related party transactions" issued by CONSOB with Resolution no. 17221 dated 12 March 2010, subsequently amended by Resolution no. 17389 dated 23 June 2010.

On 12 November 2010, the Board of Directors identified in this Committee, which is totally formed by non executive, independent Directors as established by the Corporate Governance Code, the body in charge of carrying out the role required by the above-mentioned regulations both for approving transactions of greater importance and those of lesser importance as indicated in Terna's Procedure. The Committee is entrusted with preliminary, advisory and consulting tasks and powers for the evaluation and decision-making in the above-mentioned related party transactions as well as regarding possible amendment proposal to the Procedure adopted by Terna.

Within the Company budget, adequate financial resources are allocated to carry out the tasks of the Committee for Related Party Transactions. Furthermore, for its evaluations, the Committee may request the Company to utilize independent specialized experts that are external to the Company, according to the Committee's opinion; the costs for the services rendered by these consultants are to be incurred by the Company. The terms for organizing the Meetings are ruled by specific internal Organizational Regulations adopted by the Board of Directors on 12 November 2010 and effective as of 1 January 2011. Upon request of the Coordinator, the Meetings of the Committee for Related Party Transactions may be attended by other persons whose presence may contribute to a better outcome of the activity of the Committee.

The Committee for Related Party Transactions is presently formed by Salvatore Machì (acting as Coordinator), Paolo Dal Pino, and Michele Polo, all independent, non-executive Directors.

## Section VII Appointment Committee

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Currently, Terna has not set up, within the Board of Directors, a specific Appointment Committee, since up to now shareholders have not met difficulties in presenting adequate candidacies, such as to allow a composition of the Board in line with the provisions of the Code of Conduct for listed companies.

## Section VIII Remuneration Committee

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### Functions of the Remuneration Committee

As of 2004, within the Board of Directors a Remuneration Committee was set up, responsible for making proposals to the Board (I) for the remuneration of the CEO and of other Directors with special duties monitoring the implementation of the Board's Resolutions, and (II) for determining the remuneration criteria of the top management of the Company and its subsidiaries, periodically evaluating its criteria on the basis of indications provided by the CEO and submitting general recommendations to the Board on the matter.

Following the renewal of the Board of Directors during the Meeting held on 28 April 2008, the Remuneration Committee was also renewed as well as its members.



The Committee's tasks were reconfirmed as already identified by the Board within "Terna S.p.A.'s Organizational Rules for the Remuneration Committee" which was approved with Resolution dated 24 January 2007.

The Remuneration Committee is currently composed of Vittorio Rispoli (as coordinator), Paolo Dal Pino, Salvatore Machì and Luigi Roth, all Non-executive Directors and most of whom are also independent.

In 2010, the Remuneration Committee held 4 Meetings, with the regular participation of all members. The Meetings lasted an average of fifty minutes each. None of the Directors participated in the Committee Meetings in which proposals regarding their remuneration were submitted to the Board of Directors.

In 2011, the Committee will hold as many Meetings as are sufficient for carrying out the duties assigned. During the year, up to the date of approval of this report, the Committee has held 2 Meetings.

As part of its duties, the Remuneration Committee has a key role in implementing specific Stock Option Plans for the 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 2010, 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 2010, the Remuneration Committee examined the incentive plans for the Company's top management.

During the Meeting of 31 March 2011, the Board of Directors evaluated the duties and performance of the Committee. The altogether positive evaluation on the size, composition and operation of the Committee was confirmed by the Board of Directors, within the yearly review of the Board and the Committees.

The Committee has been granted adequate financial resources.

## Section IX Remuneration of Directors

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The compensation of the Directors is established by the Shareholders' Meeting for each Director (art. 24.1 of the Bylaws). Extra compensation for the members of the Committees formed within the Board of Directors in compliance with the Governance Code of Borsa Italiana was resolved, following the evaluation by the Board of Statutory Auditors, in compliance with art. 2389, paragraph 3, of the Civil Code and with art. 24.2 of the Bylaws, by the Board itself, following the evaluation of the Board of Statutory Auditors; the overall compensation for the Chairman and the CEO is also identified by the Board of Directors based on the proposal submitted by the Remuneration Committee and following the evaluation by the Board of Statutory Auditors.

A portion of the compensation of the CEO is bound to economic results achieved by the Company and to the attainment of objectives indicated in advance by the Board of Directors in line with art. 7.C.1 of the Code of Conduct.

The compensation of the Non-executive Directors is adequate to the commitment demanded to every one of them, considering the possible participation in one or more Committees. The compensation is not bound to the economic achievements of the Company. The Non-executive Directors are not eligible to share-based incentive plans.

The fees received by the members of the Board of Directors during the year are indicated in the note to the financial statements.

## Sezione X Internal Control Committee

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### Functions of the Internal Control Committee

As of 2004, the Board of Directors created a specific Internal Control Committee, with advisory and proposal-making functions.

Following the renewal of the Board of Directors during the Meeting of 28 April 2008, the Internal Control Committee was re-established and its members were appointed. The Committee was assigned the following duties, as already identified within "Terna S.p.A.'s Organizational Rules for the Internal Control Committee" which were approved on 24 January 2007:

- assisting the Board of Directors in establishing Internal Control System guidelines and periodically checking the adequacy and effective implementation thereof (art. 8.C.1 of the Code of Conduct);
- assessing, together with the Executive in Charge of the preparation of accounting documents and the Statutory Auditors, the correct application of accounting principles and their uniformity for the preparation of the consolidated financial statements (art. 8.C.3, letter a) of the Code of Conduct);

- expressing opinions on request of the CEO, on specific aspects concerning identification of main Company risks and planning, implementation and management of the Internal Control System (art. 8.C.3, letter b) of the Code of Conduct);
- examining the work plan prepared by the Executive in Charge of internal control as well as the periodical reports prepared by him (art. 8.C.3, letter c) of the Code of Conduct);
- evaluating the proposals coming from the auditing companies to obtain assignment as well as the work plan prepared for the auditing and results presented in the report and in the suggestion letter (art. 8.C.3, letter d) of the Code of Conduct);
- supervising the effectiveness of the auditing process (art. 8.C.3, letter e) of the Code of Conduct;
- reporting, at least every six months, to the Board of Directors about the activity carried out and the adequacy of the Internal Control System (art. 8.C.3, letter g) of the Code of Conduct);
- carrying out further duties potentially assigned by the Board of Directors especially concerning relations with the auditing company.

Additional specific duties are assigned to the Committee based on the Organizational Model adopted by Terna in compliance with Legislative Decree no. 231/01 and with Terna's Code of Ethics. The Committee is also assigned advisory functions for related party transactions as indicated in the section of this report devoted to "Directors' interests and related party transactions" (section XII).

The Internal Control Committee is currently composed of Salvatore Machi (as coordinator), Paolo Dal Pino, Matteo Del Fante and Michele Polo, who are all non-executive and mostly Independent Directors. At least one member has adequate accounting and financial experience.

In 2010, the Internal Control Committee met 4 times, with the regular participation of all members. Each Meeting lasted an average of one hour; 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 (art. 8.C.4 of the Code of Conduct).

Upon the Committee's request, the Meetings were also attended by Managers of the Company whose presence was deemed helpful for the best information regarding the items on the agenda.

In particular, in 2010, the Internal Control Committee evaluated the operation of the internal control system linked to and involving various interested parties and bodies, providing support to the Board of Directors for analyzing and following the photovoltaic project, providing a positive opinion on the effectiveness of the policies aiming at managing financial risks and the main financing transactions, positively examining the approach to managing the Company's risks regarding security and examining and monitoring the audit activities for 2010: it also met with the independent auditors that provided information regarding their work plan and the results obtained. Furthermore, it provided the Board of Directors with advisory support in significant transactions with related parties. Pursuant to what provided for by the Code of Conduct, the Committee assessed, together with the Executive in Charge, the correct use of the accounting standards and received information on control activities implemented for compliance with the provisions of Law 262/05 and subsequent amendments. The Committee also received due information from the supervisory Board under Legislative Decree no. 231/01 with reference to the adequacy and the development of the model and the activity carried out by this Board.

In 2011, the Committee will hold as many Meetings as are sufficient for carrying out the duties assigned. During the year up to the date of approval of this report, the Committee has held 1 Meeting.

During the Meeting of 31 March 2011, the Board of Directors evaluated the duties and operation of the Committee. The generally positive evaluation of the composition, size and responsibilities of the Committee was confirmed by the Board of Directors within the yearly review of the Board itself and of the Committees.

The Committee was granted adequate financial resources.

## Section XI Internal Control System

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With respect to internal control, on the basis of the Resolution adopted on 21 December 2006, the Board of Directors updated the “Terna Group’s Internal Control System” (ICS) definition, 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 (articles 8.C.1 and 8.C.2 of the Code of Conduct).

With reasonable certainty, the Group’s ICS contributes to reaching strategic objectives, 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 the electricity service continuity and guaranteed impartiality in concession activities. It is based on the following elements: control environment; risk management system; control activities; information, communications and monitoring. The coordinated implementation 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 the Group’s managerial style, personnel management policies and all employees’ conduct must be in compliance with.

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. In order to implement an integrated “risk management system”, in 2007 Terna created a Corporate Security Department significantly integrating its security tools and defining a transversal system for identifying, analyzing and controlling Corporate risks. The importance of using a structured method and a dedicated internal organization (Corporate Security Department), that promotes and supervises its implementation, derives from the fact that risks can influence Corporate activities, which, being of a varied type, are also characterized by the time variable between the moment a threat presents itself and the moment in which this threat materializes.

In addition to ensuring absolute compliance with legal provisions, this integrated model allows reaching Corporate security levels that exceed the regular standards attainable through a sectoral and fragmented security management.

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, opposing 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” aims at constantly verifying 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.

Terna has indeed an appropriate structure dedicated to preventing and managing Corporate fraud activities also aimed at spreading the culture of legality and respecting Corporate regulations. Continuously monitoring processes, verifying and managing reports of illegalities have led to introducing specific controls aimed at reducing such risks and at defining, for certain critical processes, specific procedures aimed at preventing illegal conduct.

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 implementation of the Internal Control System, on the basis of adequate preliminary assessments (art. 8.C.1 lett. a) of the Code of Conduct).

Attachment 1 to this report includes the principal characteristics of existing risk management and internal controls over financial reporting, also consolidated (ex art. 123-bis, paragraph 2, letter b) of the Consolidated Law on Finance).

Terna’s Board of Directors’ Meeting of 31 March 2011, in compliance with the opinion rendered by the Internal Control Committee on the basis of the analyses made in the course of 2010, judged the Terna Group’s Internal Control System suitable to achieve an acceptable risk profile, in consideration of the field in which Terna operates, of its size, organizational and Corporate structure (art. 8.C.1, letter c) of the Code of Conduct).

In its report, the Internal Control Committee also discussed 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.

## Executive Director in Charge of the Internal Control System

The CEO supervises the functionality of the ICS of the Group, implementing the guidelines defined by the Board of Directors and planning, implementing, managing and dealing with the identification of the main risks for the Group through the designated Company structures; he then periodically submits such risks to the Board of Directors (articles 8.C.1, letter b) and 8.C.5, letters a), b) and c) of the Code of Conduct).

## Executive in Charge for Internal Control

Within Terna, the Executive in Charge for internal control is the person responsible for the audit function, who is not responsible of any operating areas (articles 8.C.6, letter b, and 8.C.7 of the Code of Conduct).

The internal audit manager reports the results to the CEO, to the Internal Control Committee and to the Statutory Auditors concerning the audit activity results relative to risk management and to the suitability of the Internal Control System in order to achieve an acceptable overall risk profile (art. 8.C.6, letter e) of the Code of Conduct). He operates through audit activity, whose field of application is extended to the whole Group. The activities of Internal audit can be carried out in connection with the departments that carry out activities of internal control in subsidiaries.

The Internal Audit Department has free access to all information systems, deeds and business data, useful to express an independent judgment with respect to the suitability of the Internal Control System to achieve an acceptable risk profile (art. 8.C.6, letter c) of the Code of Conduct). For the exercise of its own tasks, the Audit Department is assured the availability of adequate means (art. 8.C.6, letter d) of the Corporate Governance Code).

Audit activities can be conducted on the basis of a yearly activity plan examined by the Internal Control Committee or can be determined each time by the Company's top management in relation to specific facts or as a result of particular events. In February 2009, as envisaged by the international standards issued by the Institute of Internal Audit (IIA), the External Quality Assessment of Terna's Audit Department ended that assessed the effectiveness of the Audit Department in bringing forth its mission and compliance of the activities carried out with the Standards for the practice of Internal Auditing issued by the IIA, obtaining the result of "general compliance", the highest positive assessment obtainable according to the IIA. The Board of Statutory Auditors, within its own activities, can request the Audit Department to carry out assessments on specific operating areas or Company operations.

The Statutory Auditors and the Internal Control Committee timely exchange important information for the accomplishment of the respective tasks.

## Code of Ethics and Organizational Model under Legislative Decree no. 231/2001

### Code of Ethics

In May 2002, aware of the moral aspects involved in its core activities, Terna's Board of Directors resolved to adopt its Code of Ethics (that was updated in March 2004) to allow employees and all those having relations with Terna, to operate in the right way in order to establish trust, strengthen the Company's positive reputation and create value.

In 2006, the Company updated the Code of Ethics to equip Terna, following the change that rendered it an independent operator in the electricity transmission market, with a set of rules and principles to follow on the basis of this new context. The new Code of Ethics, which was approved by the Board of Directors on 21 December 2006, explains, also in ethical terms, Terna's uniqueness. It underlines the need to respect universal ethical principles, that can be immediately recognized by everybody, and that should be fully adopted by companies. It is not by chance that the Code of Ethics is inspired by the 10 principles of the Global Compact, the most important expression of this vision.

Terna's Code of Ethics is broken down into five sections, which discuss, in this order:

- Terna's fundamental ethical principles, which are organized into general ethical principles (legality, honesty and accountability), that are universal and therefore to be recognized and shared by all, and into four main principles that Terna believes are particularly important, given its activities and nature (good management, respect, fairness and transparency);
- the conduct required, especially from employees, based on three important elements: loyalty to the Company, conflicts of interest and the integrity of Company assets;
- general instructions for the conduct to follow in relations 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. It applies to all of Terna Group's subsidiaries for sections 1 (Principles), 2 (Conflicts of interest, Company loyalty and the integrity of Company assets) and for section 3 (Relations with stakeholders) limited to the initial guidelines for the conduct to be followed with the individual categories of stakeholders.

On 16 December 2009 Terna's Board of Directors, based on sustainability, undertook an additional and coherent step resolving to officially join the Global Compact, the multi-stakeholder network promoted by the UN Organization that joins governments, companies, UN agencies, trade union organizations and the civil society with the aim of globally promoting the 10 universal principles of human rights, occupation, environmental protection and anti-corruption measures. In early 2010 the campaign was completed for disseminating the Code of Ethics which began at the end of 2009 to increasingly favor its total implementation also following the establishment of the Ethical Committee. To complete the Code of Ethics and the commitments undertaken therein, Terna decided to draw up a sustainability report to illustrate its work in the field of ethics and social responsibility which is published on a yearly basis.

#### Organizational Model under Legislative Decree no. 231/2001

Since 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 the Italian Law a system of administrative (and criminal) liability for companies with respect to certain types of offences committed by their Directors, managers or employees in the companies' interest or to their benefit. The model was updated in June 2004, after the Company's shares were listed.

During 2010, the Model was amended following changes in law provisions as per art. 24-ter regarding "organized crime offences" and article 25-bis, 25-novies and 25-novies (bis) regarding, respectively, "offences against industry and trade", crimes related to the violation of copyright and "crime of incitement to refrain from issuing statements or to issue false statements, introducing the new Special Section I, relative to organized crime offences and updating the "General Section" and the "Special Sections" "A", "B", "G" and "H" for the other offences.

In addition to identifying areas deemed to be mostly at-risk for committing offences (so called "At-risk Areas") the activity also involved defining conduct principles which all company representatives must comply with in order to prevent such offences, in addition to the provisions already included in the existing procedures within the Company.

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 those operating in the name and on behalf of Terna and its Group, so that their conduct be correct and transparent in the performance of their activities, to prevent the risk of the offences provided for by the Decree from being committed.

The Model is currently organized into ten sections:

- a "general section" which describes, *inter alia*, the content of Legislative Decree no. 231/2001, the objectives of the Model and its implementation, the duties of the supervisory Board – structured as a collective body – required to monitor the implementation and compliance of the Model, information flows and the penalty system;
- a "special section A", which covers offences committed in dealings with the public administration;
- a "special section B", which discusses Corporate offences;
- a "special section C", which deals with offences of terrorism or subversion of the democratic order;
- a "special section D", on offences against individuals;
- a "special section E", concerning market abuse offences, with the addition of specific "Compliance regulations for the prevention of offences and administrative market abuse offences";
- a "special section F", regarding dealing in stolen goods, money laundering and use of money or assets coming from illegal sources as introduced in Decree no. 231/01 consequent to Legislative Decree no. 231/07 becoming effective;
- a "special section G", regarding manslaughter and serious or very serious injuries committed in violation of the rules on occupational health and safety;
- a "special section H", regarding computer-related offences;
- a "special section I" relative to organized crime offences.

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

In order to guarantee wider diffusion of the knowledge of the adopted Model, the same is published in the Company's website ([www.terna.it](http://www.terna.it)) under the Investor Relations section and, in 2010 a widespread training and customized campaign was carried out involving all employees.

As a supplement to the Model, already in 2008, Terna also approved a specific "Compliance Regulation for preventing offences and administrative illegalities of market abuse" aimed at providing the recipients of the Model an additional operational tool for evaluating their conduct for integrating offences and administrative illegalities of market abuse and consequently for preventing conduct potentially representing a source of administrative responsibility for the Company.



## Independent Auditors

The audit engagement for the separate and consolidated financial statements has been entrusted, pursuant to the resolution passed by the shareholders' on 24 May 2007 on proposal of the Board of Statutory Auditors, to the audit company KPMG S.p.A. for the 2007-2010 period.

In elaborating the proposal for assignment of the audit engagement submitted to the shareholders for the Meeting held on 24 May, 2007, the Board of Statutory Auditors preventively verified the requirements of independence of the company assigned with reference to Terna and to the Group.

Considering provisions under art. 159 of the Consolidated Law on Finance and under art. 8, paragraph 7 of Legislative Decree no. 303 of 29 December 2006 (so called corrective Decree) of Law no. 262 of 28 December 2005, such assignment follows the previously attributed assignments to the KPMG company by the Shareholders' Meeting of 9 April 2002 (for 2002-2004) and by the Shareholders' Meeting of 3 March 2004 (for 2004-2006); the latter related to the listing of the Company on 23 June 2004.

The next annual Meeting will also be called to resolve on the audit assignment which will expire with the approval of the 2010 financial statement with no possibility of further renewal or postponement pursuant to art. 17 of Legislative Decree no. 39 dated 27 January 2010.

## Executive in Charge of the preparation of accounting documents

Pursuant to art. 154-*bis* of the Consolidated Law on Finance – introduced by Law no. 262 of 28 December 2005 and subsequently modified by Legislative Decree no. 303 of 29 December 2006 – Terna's Shareholders' Meeting of 24 May 2007 has provided for in the Bylaws (art. 21.4) the position of the Executive in Charge of the preparation of accounting documents (Executive in Charge), delegating his appointment to the Board of Directors, following the indication by the Board of Statutory Auditors, based on specific requirements of professionalism.

The choice to reserve the appointment and revoking of the Executive in Charge to the Board of Directors was carried out in line with Law provisions that directly acknowledge the Board of Directors a specific task of supervision (art. 154-*bis*, paragraph 4 of the Consolidated Law on Finance).

The Executive in Charge must also be in possession of requirements of honor indicated by Law and of professionalism indicated in the Bylaws.

In particular, the Executive in Charge of the preparation of accounting documents must have a total experience of at least three years in:

- a) a managerial position in administration activities, finance and control and/or managing functions inherent to the activity of preparation and/or analysis and/or evaluation and/or verification of Company documents whose complexity is comparable to accounting documents of the Company; or
- b) activity of legal control of the accounts in companies listed in Italian regulated markets or in those of other countries of the European Union; or
- c) professional activities or university teaching in financial or accounting subjects.

The Board of Directors, in compliance with the regulations, has immediately appointed as Executive in Charge Luciano Di Bacco, Head of the Administration Department of Terna, after verification of the requirements of honor and professionalism. Such appointment has also involved the adjustment of the organizational structure of the Company attributing to the Executive autonomy and authority regarding the structure of his Department and granting him a top role directly reporting to the CEO.

The Executive in Charge has certified, as of the 2007 half-year report, compliance, under art. 154-*bis*, paragraph 2 of the Consolidated Law on Finance, with the action and communications of the Company provided for by Law or communicated to the market, with reference to annual and interim financial reporting of the Company, documentary evidences, ledgers and the accounting books.

The Executive in Charge carries out all the activities necessary to give the Board of Directors the possibility to comply with its supervision tasks as per art. 154-*bis*, paragraph 4 of the Consolidated Law on Finance.

Under art. 154-*bis*, paragraph 3 of the Consolidated Law on Finance, the Executive in Charge prepares suitable administrative and accounting procedures for the preparation of the financial statements, consolidated financial statements and half-year reports, and certifies, together with the delegated administrative bodies, their adequacy and effective application, under paragraph 5 of art. 154, according to the model established in the Issuer Regulations, as of the financial statements as at and for the year ended 31 December 2007.

During 2010, in compliance with the provisions of both Law no. 262/2005 and of the Model adopted by the Company, activities were implemented relating to the adjustment of administrative and accounting procedures, consequent to the normal changes made to processes. Testing operations were also conducted for verifying the implementation of the actual control.

According to the Code of Conduct, the Executive in Charge assessed, together with the Internal Control Committee, the correct use of the accounting standards.

## Section XII Directors' interests and related party transactions

Within the Company and its subsidiaries, Terna, even before listing its shares in the stock market, deemed appropriate to establish the conditions 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 (art. 9.P.1 of the Code of Conduct). As of 22 February 2007, in implementing the provisions of the new Code of Conduct, Terna defined these conditions as part of specific internal procedures submitted in advance to the Internal Control Committee and approved by the Board of Directors. Among other things, these procedures established for the entire 2010 a specific reporting to the Board of Directors and Board of Statutory Auditors that was periodically implemented.

Following the publication of "Regulations regarding related party transactions" issued by CONSOB with Resolution no. 17221 dated 12 March 2010, subsequently amended with Resolution no. 17389 dated 23 June 2010 ("CONSOB Related Party Regulations"), Terna's Board of Directors – as announced to the market on 12 November 2010 – defined these conditions within a new Procedure ("Procedure for Related Party Transactions"), effective as of 1 January 2011, taking into account the new regulations regarding the provisions of the Civil Code and those of the Governance Code of listed companies (art. 9.P.1 of the Corporate Governance Code). The resolution was approved unanimously following the positive opinion of the Committee established for this purpose and formed by independent Directors only (as established by art. 4, paragraph 3, of CONSOB Regulations for Related Parties) whose members were identified among the Internal Control Committee (art. 9.C.1 of the Governance Code). The new Procedure was published, as of 12 November 2010, on the Company's website ([www.terna.it](http://www.terna.it), under the Investor Relations/Corporate Governance section).

Within the new Procedure and pursuant to article 4 of CONSOB Related Party Regulations, the following was implemented:

- related parties were identified, related party transactions were defined and the new terms for identifying, approving and implementing the various categories of related party transactions were ruled;
- lower amount Transactions were identified as well as those cases in which the provisions of the Procedure should not be applied (in line with the provisions of articles 13 and 14 of CONSOB Related Party Regulations);
- the terms for forming the Director Committee were identified called upon to express its opinion on the single Transactions of greater or lesser importance, as well as the contents of such opinion and the independence requirements of the Committee member. Furthermore, specific measures were identified should at least 3 independent, non related Directors not be present;
- the rules were established regarding cases in which Terna shall examine or approve transactions of Italian or foreign subsidiaries;
- the terms and time frames were established with which Directors and the Committee for Related Party Transactions should be provided with information on related party transactions and relative documentation;
- the choices were identified as made by the Company with reference to the possibilities included in CONSOB Related Party Regulations.

Compared to previous conduct principles regarding related party transactions adopted by Terna, the new Procedure envisaged lowering the relevance thresholds regarding certain types of Transactions which should be reported to the Board of Directors, so that an enlargement of entitled related party transactions could be obtained, according to the definition indicated by CONSOB in the above-mentioned resolution - as transactions of lesser importance.

Lastly, the document establishes that, as a first application, Terna's Board of Directors shall carry out a review and, wherever necessary, a revision of the "Procedure for Related Party Transactions" within one year from its entry into force and, subsequently, at least every three months also considering the organizational structure of the Company and of the Group, the assets owned and the effectiveness of the Procedure in its application.

Terna has also identified specific terms for approving significant transactions carried out by the Company, also through subsidiaries (art. 1.C.1 lett. f) of the Corporate Governance Code) and for recognizing and managing situations in which a Director holds his own interest or an interest of third parties regarding a transaction that he should evaluate (art. 9.C.2 of the Corporate Governance Code), in compliance with the rules of the Governance Code, according to a specific internal procedure adopted as of 2007 and subsequently updated. For this purpose:

- significant transactions subject to the procedure are identified as: a) transactions that have as their object, amount and terms/time frames of implementation an impact on safeguarding the company assets or the completeness and correctness of Terna's information also of accounting information and that as such create an obligation for Terna to make available to the public an informative document in compliance with provisions by supervisory authorities of financial markets; b) financial transactions whose value exceeds € 50 million with the exception for transactions included in the budget and in approved financial plans as well as those regarding dispatching activity and all related services;
- significant transactions are subject to prior approval or analysis (in the case of transactions falling under the field of activity of Terna's directly or indirectly controlled companies) of Terna's Board of Directors that may rely on the assistance of one or more independent experts that should express their opinion on the economic conditions and/or the executive terms of the transactions, with the exception for the powers assigned to the CEO for particularly urgent situations;



- the Board of Directors is duly informed on the methods of execution of significant transactions, the time frames and economic conditions to implement such transactions, the evaluation process followed, the underlying interests and motivations and any possible risks for Terna and its subsidiaries linked to these transactions;
- the of significant transactions, approved beforehand or subject to the evaluation by the Board of Directors is communicated to the Board of Directors and the Board of Statutory Auditors at least every three months.
- 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;
  - 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.

## Section XIII Appointment of Statutory Auditors

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### Appointment and requirements of Statutory Auditors

The terms for appointing the members of the Board of Directors are ruled by article 26 of the Bylaws.

In compliance with the provisions of the Company's Bylaws, 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 honor and professionalism requirements as per the special legislation for Statutory Auditors of listed companies (art. 148, paragraph 4 of the Consolidated Law on Finance) now under Ministry for Justice Decree no. 162 of 30 March 2000, as integrated by appropriate Bylaws provisions (art. 26.1 of Bylaws). No Statutory Auditor may be Standing Auditor of five or more companies that have issued securities and can hold other assignments of administration and control in share capital companies according to Book V, Title V, Chapters V, VI and VII of the Civil Code within the limits established by art. 144-*terdecies* of the Issuer Regulations implementing the provisions of art. 148-*bis* of the Consolidated Law on Finance.

All the members of the Board of Statutory Auditors must also possess requirements of independence under art. 148, paragraph 3 of the Consolidated Law on Finance.

In implementing law provisions on the matter of privatizations and pursuant to Italian laws regarding listed companies, the entire Board of Statutory Auditors must be appointed using the voting list system, to ensure that the Board includes one Standing Auditor and one Alternate Auditor from minority lists.

On 18 October 2010, Terna's Board of Directors approved the amendments to the Bylaws necessary to adjust it to the novelties introduced by law provisions regarding shareholders' rights of listed companies aiming at favouring the participation of shareholders in the life of the Company (Directive 2007/36/CE and relative implementing Legislative Decree no. 27 dated 27 January 2010). Among other things, amendments involved art. 26.2 of the Bylaws regarding the appointment procedure for the Board of Statutory Auditors and the terms and modalities for depositing the lists.

Such amendments will be applied for the first time on occasion of the next annual Meeting which will also have to resolve about the renewal of the expiring company bodies with the approval of the 2010 financial statements.

On the basis of these amendments and according to the Bylaws, the deposit and publication of lists are ruled by the provisions for appointing the entire Board of Directors, in cases where this is compatible with the existing applicable law and the provisions of art. 26 of the Bylaws for the appointment of the Board of Statutory Auditors.

This system provides – in line with art. 4, paragraph 1-*bis* of Legislative Decree no. 332 of 31 May 1994 converted into Law no. 474/94 ("Privatization Law"), modified by Legislative Decree 27 January 2010, by art 148 of the Consolidated Law on Finance and by the implementing rules for the above-mentioned provisions included in articles 144-*ter* and following of the Issuer Regulations, – 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 or a lower amount as envisaged by the law – of shares with voting rights in the Meeting. For this purpose CONSOB, implementing the provisions of 148 of the Consolidated Law on Finance and articles 144-*ter* and following of the Issuer Regulations, has established, with Resolution n.17633 dated 26 January 2011 and for the year that ended on 31 December 2010 – the participation stake required for submitting candidate lists to be appointed in Terna's administration and control bodies at 1% of the share capital, taking into account the Company's capitalization, floating capital and owned assets and without prejudice to the lower share contemplated by the Bylaws.

The presentation and filing of lists must occur at least 25 days from the day established for the Meeting on first call.

Ownership of the minimum share required to submit lists shall be determined by taking into account the shares that are

registered in the name of the shareholder(s) on the day in which the lists are filed with the Company.

In order to prove the legitimacy of presentation of the lists, entitled Shareholders must present and/or deliver the relative documentation even after the lists have been filed but within the time period set for the publication of the lists.

Pursuant to art. 144-*sexies*, paragraph 5, of the Issuer Regulation, in the event that on the date due for the submission of the lists for the Board of Statutory Auditors only one list has been filed, that is only lists submitted by members who are connected to each other pursuant to applicable law provisions, lists may be submitted up to the third day following said date; In this case the thresholds set forth above shall be reduced by half.

Each shareholder may present or assist in the presentation of one single list and each candidate may be on one list only or he will be considered ineligible. The lists shall list candidates according to a progressive number and will be divided into two sections, one for the candidates to the office of Standing Auditor and the other for the candidates to the office of Alternate Auditor. The first one of the candidates of each section of the lists must be registered in the register of statutory auditors and must have exercised the activity of legal control of the accounts for a period of at least three years.

Pursuant to art. 148, paragraph 2 of the Consolidated Law on Finance, at least one standing member is appointed by the minority shareholders who are not connected, not even indirectly, with the shareholders who have introduced or voted the list winning for a number of votes.

In compliance with the Italian legislation for listed companies, the Bylaws (art. 26.2) attribute the chairmanship of the Board of Statutory Auditors to the Standing Auditor appointed by the minority list.

To ensure transparency in the procedure for the appointment of the Board of Statutory Auditors, also in line with the provisions of the Code of Conduct, lists are provided, pursuant to art. 144-*sexies*, paragraph 3 of Issuer Regulations and also based on the provisions of art. 10.C.1 of the Code of Conduct, with:

- a) information on the identity of the shareholders who have submitted the lists, indicating the total percentage of the shares held;
- b) a declaration by shareholders other than those who hold, also as a group, a controlling interest or relative majority, indicating the absence of relationships as set forth in art. 144-*quinquies* of the “Issuer Regulation” with them. With Communication no. DEM/9017893 dated 26 February 2009, CONSOB recommended shareholders who submit a “minority list” to submit the information indicated in such Communication;
- c) an accurate description of the personal and professional characteristics of the candidates and, pursuant to art. 2400, last paragraph of the Civil Code, with the list of administration and control positions held within other companies as well as a statement by the candidates certifying possession of the requirements set by the law (including possession of independence requirements pursuant to art. 148, paragraph 3 of the Consolidated Law on Finance and their acceptance of the candidacy.

Such documents are deposited at the registered offices of the Company, and are published in the Company’s website according to the terms established by CONSOB , at least 21 days before the day of the Shareholders’ Meeting (art. 10.C.1 of the Code of Conduct).

For any replacement of the Statutory Auditors, the terms of art. 26.2 of the Bylaws will be applied. In case one of the Statutory Auditors is replaced, the Alternate Statutory Auditor first on the list takes his place. If the Chairman of the Board of Statutory Auditors is replaced, this position will be taken by the Alternate Statutory Auditor taken from the same list.

For the appointment of the Statutory Auditors occurring outside the provisions for renewing the entire Board of Statutory Auditors, the Shareholders’ Meeting resolves based on the majority envisaged by the Law and without respecting the above-mentioned procedure, but nonetheless so as to ensure a composition of the Board of Statutory Auditors in compliance with the requirements of honor and professionalism established by the Law.

## Section XIV Statutory Auditors

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### Composition of the Board of Statutory Auditors

The Board of Statutory Auditors currently in office, appointed by the shareholders during the ordinary Meeting of 28 April 2008, will be in office until the approval of the financial statements as of and for 2010.

According to the resolution passed during the Meeting on 28 April 2008, the Board of Statutory Auditors is formed by Luca Aurelio Guarna (Chairman of the Board of Statutory Auditors appointed by the minority list submitted by the Assicurazioni Generali Group), Marcello Cosconati and Lorenzo Pozza (Standing Auditors appointed by the majority list submitted by Cassa Depositi e Prestiti S.p.A.).

Alternate Auditors were also appointed: Stefania Bettoni (included in the minority list submitted by the Assicurazioni Generali Group) and Mario Paolillo (included in the majority list submitted by Cassa Depositi e Prestiti S.p.A.). The latter passed away on 30 November 2010.

The Statutory Auditors appointed represent two of the three lists submitted for said Meeting. Following the statements made for the appointment, the vote count and after the voting, a standing member was appointed by the minority members that are not connected, not even indirectly, with the members who have submitted or voted the list that came first for the number of votes.

From its appointment, the Board of Statutory Auditors is unchanged. A summary of their professional background is provided below.

• **Luca Aurelio Guarna, 38 years old – Chairman of the Board of Statutory Auditors**

[born in Milan on 20 December 1972]

He has a degree in Business Administration from the Luigi Bocconi University; he qualified for the title of Tax Consultant in 2000 and since 2002 he has been enrolled as Auditor. He has carried out professional activity with prestigious legal and tax offices and since 2001 he has been a member of the administrative, tax and Corporate consulting Spadaccini office in Milan. He is presently the Chairman of the Board of Statutory Auditors at Gemina S.p.A. and Standing Auditor in other companies such as: Aereopoli di Roma S.p.A., Delmi S.p.A. (company belonging to the A2A Group which is part of Edison S.p.A.'s holding chain), Eagle Pictures S.p.A. and Bieffe Medital S.p.A. He has worked as a Professor for the Arthur Andersen network and for the Foundation of Tax Consultants in Milan.

• **Marcello Cosconati, 61 years old – Standing Auditor**

[born in Presenzano (Caserta) on 25 September 1949]

He has a degree in Law and Political Science and Economics and is an auditor. He is an official of the Ministry of Economics and Finance and General Director of the Central Budget Office at the Ministry of Interior, Department of the State's General Accounting. With the Ministry of Economics and Finance he has held positions in different offices. In representation of the Ministry of Economics and Finance, he has held various assignments as auditor. He is presently Chairman of the Board of Statutory Auditors of SACE S.p.A. and of SACE Fct S.p.A., as well as of Tirrenia Navigazione S.p.A. He is also a tax judge with the Tax Commission in Caserta. He has worked as a Professor for seminars organized by the Public Authorities and by the Roll of Accountants in the Province of Caserta.

• **Lorenzo Pozza, 44 years old – Standing Auditor**

[born in Milan on 11 October 1966]

He has a degree in Business Administration from the Luigi Bocconi University, tax consultant and auditor. Since 2001, he has been Associate Professor of Business Administration at the Luigi Bocconi University and Professor of Methodology and quantitative standards for companies after having held various positions as a Professor in International Accounting and Accounting and Budget since 1991 at the same university, and since 1992 at the Corporate Management School (SDA) and since 1996 at the University in Italian part of Switzerland. He holds the position of Director or Auditor in various different listed or unlisted companies in the industrial, financial, real estate and insurance sectors, among which: Telecom Italia S.p.A., Gas Plus S.p.A., Bracco Imaging S.p.A. and Leonardo & Co S.p.A. He also carries out professional activity since 1990 and has been a founding member of the Partners S.p.A. consulting firm. He is the author of three books on budget and company evaluation as well as of numerous other publications and has also written articles and essays on this subject for national and international magazines.

During the appointment and taking account of the information provided by the individuals involved, the Board of Directors, based on the envisaged terms, has confirmed and verified the existence of the requirements of honor, professionalism and independence of the members of the Board of Statutory Auditors appointed by the Shareholders' Meeting held on 28 April, 2008.

In the attached table 2 information are included regarding the composition of the Board of Statutory Auditors as of 31 March 2011.

No standing Statutory Auditor holds five assignments in other companies issuing stocks listed in the Italian regulated markets or in other countries of the European Union.

The total number of assignments as a Director or Statutory Auditor in other companies according to Book V, Title V, Chapters V (S.p.A.), VI (S.A.p.A.) and VII (S.r.l.) of the Civil Code, relevant according to art. 148-bis of the Consolidated Law on Finance, is indicated in the attached table 2. The total number of assignments according to art. 144-*quinqüesdecies* of the above-mentioned Issuer Regulations based on CONSOB Resolution no. 17326 dated 13 May, 2010, is published by CONSOB and is available on its website ([www.consob.it](http://www.consob.it)).

During 2010, the Board of Statutory Auditors held 9 Meetings which lasted on average approximately 2 hours each, with the regular participation of the Standing Auditors.

In 2011, all the preliminary Meetings are scheduled for reviewing the economic-financial data on the part of the Board of Directors. During the year in progress up to the date of approval of this report, the Board of Statutory Auditors held 3 Meetings. The Board of Statutory Auditors of 14 February 2011 – utilizing all the criteria indicated by the Governance Code of listed

companies published by Borsa Italiana in March 2006 regarding the independence of Directors and on the basis of the information provided by each single member – certified that all Standing Auditors met the independence requirement.

The Board of Statutory Auditors, already since 16 March 2007, decided to voluntarily adapt to a system of transparency analogous to that of the Directors in case of operations in which they bear an interest for themselves or third parties (art. 10.C.4 of the Code of Conduct). This orientation was also confirmed by the new Board of Statutory Auditors in the Meeting held on 12 February 2009.

During 2010, the Board of Statutory Auditors carried out the activities that are typical to auditing as envisaged by the national regulations regarding (I) the observance of the Law and of the founding deed, including the respect of principles of proper administration in carrying out Corporate activities, (II) the adequacy of the organizational structure, of the internal auditing system and of the Company's administrative-accounting system. It has also verified the implementation of the provisions pursuant to art. 114, paragraph 2 of the Consolidated Law on Finance relative to the communication obligations. The Board of Statutory Auditors also monitored the independence of the auditing company verifying both the respect of the provisions applicable on the matter, and the nature and entity of the services different from the accounting and auditing provided to Terna and to its subsidiaries by KPMG and the bodies belonging to its network (art. 10.C.5 of the Code of Conduct).

The Board of Statutory Auditors verified the proper application of criteria and of procedures adopted by the Board of Directors for evaluating the independence of its members and also analyzed the implementation of the regulations pursuant to Legislative Decree no. 231/01 and of the Regulations for the Executive in Charge of the preparation of financial documents pursuant to Law no. 262/05.

In carrying out its activity, the Board of Statutory Auditors was coordinated with the internal Audit Department and with the Internal Control Committee according to the terms included in the previous "Section XI: Internal Control System" (articles 10.C.6 and 10.C.7 of the Code of Conduct), with the Control Body pursuant to Legislative Decree no. 231/01, with the Executive in Charge pursuant to Law no. 262/05, as well as with the Boards of Statutory Auditors of the holding company and with the independent auditors.

## Section XV Investor Relations

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Since its listing on the Stock Exchange, the Company has believed that establishing a 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 included 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 was decided that this dialogue should be facilitated by the creation of specific Company structures.

Accordingly, the Company has set up the (I) Investor Relations Department, which currently reports to the CEO and has the task of keeping contacts with Institutional Investors under the responsibility of Mrs. Elisabetta Colacchia (Viale Egidio Galbani, 70 - 00156 Rome - ph. 06 8313 8145 - fax 06 8313 9312 - e-mail: investor.relations@terna.it and (II) a department for relations with general shareholders within the Corporate and Legal Affairs Department under the direction of Attorney Filomena Passeggio (Viale Egidio Galbani, 70 - 00156 Roma - ph. 06 8313 8136 - fax 06 8313 8218 - e-mail: azionisti.retail@terna.it) - (articles 11.C.1 and 11.C.2 of the Code of Conduct).

Furthermore, the Company has further encouraged dialogue with investors by creating a specific section in its website ([www.terna.it](http://www.terna.it)), where they can find both 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 structure, the Bylaws and regulations 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, etc.) (art. 11.C.1 of the Code of Conduct).

## Section XVI Shareholders' Meetings

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The Code of Conduct establishes that the Shareholders' Meetings should be considered 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 adequately improve the Meetings, in addition to guaranteeing the participation of its Directors (art. 11.C.4 of Borsa Italiana's Code of Conduct).

Also on the basis of special legislation enacted as expected in relation to listed companies, Terna introduced into its Bylaws 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.

In particular, pursuant to art. 11.1 of the Bylaws, every shareholder that has the right to attend the Shareholders' Meeting can be represented according to the Law, through a written proxy.

In order to facilitate the notification of proxies to the Company, on 18 October 2010, Terna's Board of Directors approved the amendments to the Bylaws necessary for adjusting the company Bylaws to the novelties introduced by law provisions regarding shareholders' rights of listed companies aiming at favoring the participation of shareholders in the life of the Company (Directive 2007/36/EC and relative implementing Legislative Decree no. 27 dated 27 January 2010) including notification of proxies by electronic means and, according to art. 125-*bis* of the Consolidated Law on Finance, mentioning such terms from time to time in the notice of call. On that occasion, the Board of Directors deemed it appropriate to allow shareholders the possibility to grant proxies together with specific voting instructions to a Designated Company Representative according to art. 135-*undecies* of the Consolidated Law on Finance without exercising the so-called opt out possibility set by the Consolidated Law on Finance (art. 11.C.3 of the Governance Code).

In order to facilitate the collection of proxies with the shareholders' employed with the Company and its subsidiaries associated with shareholders' associations that meet the requirements envisaged by the existing laws, according to the terms and modalities agreed upon each time with their legal representatives, these associations have made spaces available to be used for communication and for carrying out activities for collecting proxies.

The Bylaws, instead, does not envisage attendance to the Shareholders' Meeting through telecommunications means or through the expression of the right to vote by correspondence.

With regard to the right to attend a Shareholders' Meeting, the Bylaws (art. 10.1) – as modified by the Board of Directors on 18 October, 2010 implementing the above-mentioned Legislative Decree no. 27 dated 27 January 2010 – envisages that attendance in the Shareholders' Meeting is allowed only to those who have the right to participate in the Meeting and to exercise the voting right pursuant to law provisions in force.

On the basis of this provision and according to existing art. 83-*sexies* of the Consolidated Law on Finance, eligibility to participate in the Meeting and exercising the voting right is certified by a notice to the Company, made by an intermediary, in compliance with own accounting books, in favor of the person entitled to voting right on the basis of evidence related to the close of the accounting day of the seventh open-market day prior to the date set for the Shareholders' Meeting on first call, the so-called "record date".

These provisions do not entail any obstacles to the subsequent negotiations of shares. The credit and debit registrations made on accounts subsequent to said term are not material for purposes of legitimizing the exercise of the right to vote in the Shareholders' Meeting. Therefore, those who appear as owners of the Company shares subsequent to said date will not be allowed to participate and vote in the Meeting.

The right for integration of the agenda on the part of the shareholders, by virtue of the postponement of general nature pursuant to art. 30 of the Bylaws, is held by the shareholders that, also jointly, represent at least 1/40<sup>th</sup> of the share capital according to the direct provisions of the Law (art. 126-*bis* of the Consolidated Law on Finance). On the basis of this forecast, the deadline in which the shareholders can request the integration of the agenda is of ten days as of the publication of the notice of call of the Shareholders' Meeting filing, within the same time frame, a report on the subjects to be discussed: the integration of the list of items to be discussed is allowed only for those topics on which the Shareholders' Meeting is authorized to resolve pursuant to the Law. These topics exclude those for which the Law itself envisages that a resolution is made on the proposal by the Directors or on the basis of one of their projects or of a report they have prepared. In case of an integration to the agenda, the modified list of subjects to be discussed during the Meeting must be published according to the same terms as for the notice of call, at least fifteen days prior to the day scheduled for the Meeting.

Furthermore, during the Meeting of 3 March 2004, the shareholders resolved to implement a specific regulation for the Company, aimed at ensuring the exact and functional running of Shareholders' Meetings, with detailed rules for the various sectors, in compliance with each shareholders' fundamental right to request clarifications on the various issues being discussed, express an opinion and submit proposals (art. 11.C.5 of Borsa Italiana's Code of Conduct).

In particular, with regard to the right of each shareholder to take the floor regarding the items on the agenda, art. 6 of the



Shareholders' Meetings regulations envisages that those entitled to exercising the right to vote can ask for the floor only once regarding the topics being discussed, presenting observations, requesting information and formulating proposals. The request to have the floor can be submitted at the time the Shareholders' Meeting is held and – unless otherwise stated by the Chairman – until the Chairman himself has not declared the discussion on the topic closed. The terms for such request, for taking the floor and relative order, are established by the Chairman. Considering the topic and the importance of each item discussed as well as of the number of those requesting the floor, the Chairman predetermines the duration of the reports and the response – usually not to exceed ten minutes for reports and five minutes for the responses – in order to guarantee that the Shareholders' Meeting can end its activity in a single session. The Chairman and, by invitation, all those who assist him, respond to the speakers at the conclusion of all the reports or questions. Those that have requested the floor may reply briefly.

Although said regulation is not included in the Bylaws, it is approved by ordinary Meetings under the specific power given to the shareholders by the Bylaws (art. 11.2). The contents of the regulation have been aligned to the most sophisticated models prepared by trade associations (Assonime and ABI), for listed companies. The "Regulations for Terna S.p.A.'s Shareholders Meetings" can be found in the Company's website under the section: "Investor Relations/Corporate Governance".

The Board of Directors reports to the Shareholders' Meeting on the activities carried out and planned during the financial statements approval and regarding the report on management and provides the shareholders with adequate information in a timely manner, so that they may pass resolutions with full knowledge of the facts (art. 11.C.4 of Borsa Italiana's Code of Conduct).

The Shareholders' Meeting is chaired by the Chairman of the Board of Directors, or, in case of his absence or impossibility, by the Deputy Chairman, if appointed, or, in the absence of both, by another person designated by the Board of Directors; should all the above conditions not apply, the Shareholders' Meeting appoints its own Chairman (art. 12.1 of the Bylaws). The Chairman of the Shareholders' Meeting is assisted by a secretary, even if not a shareholder, designated by those present, and can appoint one or more vote counters (art. 12.2 of the Bylaws). The assistance of the secretary, according to the terms envisaged by the Law, is not necessary when the minutes of the Shareholders' Meeting are prepared by a notary public.

The Shareholders' Meeting, unless otherwise stated by the terms envisaged by art. 21.2 of the Bylaws, assigns to the Board of Directors, according to the terms established by the Law, the power to adopt certain resolutions that fall under the Shareholders' Meetings duties that can determine amendments to the Bylaws and resolves on all the topics as established by the Law (art. 13.1 of the Corporate Bylaws).

The resolutions adopted by the Shareholders' Meeting of significant impact on the Company, capable of amending the Bylaws indicated in art. 6.3 of the Corporate Bylaws are subject to the "special power" of veto by the Ministry of Economics and Finance as mentioned above in section II "Information on Shareholding" in paragraphs "Restrictions in share transfer and shares granting special powers" and "Bylaws".

The resolutions, both for ordinary and extraordinary Shareholders' Meetings, both on first, second or third call, are passed with the majority required by the Law in each case (art. 13.2 of the Bylaws).

During 2010 – with reference to the regulations for minority rights and compatibly with the regulations and rules for the Company mentioned above – no significant changes were made in market capitalization of the Company's shares or in the composition of its Corporate bodies for which the Board of Directors had to evaluate the opportunity of proposing to the Shareholders' Meeting any amendments to the Bylaws regarding the percentages established for exercising shares and of the prerogatives set for minority protection (art. 11.C.6 of Borsa Italiana's Code of Conduct).

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The hereby attached two tables summarize some of the most significant information included in the fourth, ninth and fourteenth sections of the document. An "Attachment 1" is also enclosed that includes the description of the "Principal characteristics of existing risk management and internal controls over financial reporting" (pursuant to art. 123-bis, paragraph 2, letter b) of the Consolidated Law on Finance).

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#### DIRECTORS WHO RESIGNED FROM THEIR POSITION DURING THE YEAR UNDER CONSIDERATION

LEGAL NUMBER NECESSARY FOR SUBMITTING THE LISTS DURING THE LAST APPOINTMENT: 1%

## NUMBER OF MEETINGS HELD DURING THE YEAR UNDER CONSIDERATION:

Key:

|   |  |
|---|--|
| <b>BoD:</b>                               | Board of Directors.  |
| <b>EC:</b>                                | Executive Committee.   |
| <b>AC:</b>                                | Appointment Committee.   |
| <b>RC:</b>                                | Remuneration Committee.  |
| <b>ICC:</b>                               | Internal Control Committee.  |
| <b>RPTC:</b>                              | Related Party Transaction Committee established for approving the Procedure for Related Party Transactions as indicated by the "Regulations regarding related party transactions" issued by CONSOB with Resolution no. 17221 dated 12 March 2010, as subsequently modified by Resolution no. 17389 dated 23 June 2010 ("CONSOB Regulations for Related Parties").  |
| <b>Position:</b>                          | indicates whether is Chairman, Deputy Chairman, CEO etc.   |
| <b>List:</b>                              | indicates M/m whether the Director was appointed from the majority list (M) or from the minority list (m).   |
| <b>Exec.:</b>                             | it is ticked if the Director can be qualified as an executive.   |
| <b>Non exec.:</b>                         | it is ticked if the Director can be qualified as a non executive.  |
| <b>Indep.:</b>                            | it is ticked if the Director can be qualified as independent according to the criteria of the Governance Code.   |
| <b>Indep. Based on Cons. Law on Fin.:</b> | it is ticked if the Director has the independence requirements as per art. 148, paragraph 3 of the Consolidated Law on Finance as indicated by art. 147-ter, paragraph 4 of the same Law.  |
| <b>%:</b>                                 | indicates the attendance in percentage terms of Directors at the Meetings of, respectively, the Board of Directors and of the Committees (in calculating this percentage the number of Meetings was considered which the Director attended compared to the number of Meetings of the Board or of the Committee that were held during the year under consideration or after his appointment).   |
| <b>Other assignments:</b>                 | indicates the total number stated of assignments as Directors or Auditors in other companies listed in regulated markets (also foreign markets), in financial, banking and insurance companies or in large companies, identified on the basis of criteria defined by the Board. In calculating the indicated assignments, those held in subsidiaries, either directly or indirectly controlled, namely Terna's subsidiaries, were not included. When more assignments are held within the same Group, also for a work relation with a company belonging to the Group itself, only the most important assignment is considered. For the list of assignments held by each Director, please see the brief professional resumes included in this report. |
| <b>X:</b>                                 | "X" indicates that the Board Director belongs to the Committee.  |



## Table 2

### COMPOSITION OF THE BOARD OF STATUTORY AUDITORS

| Board of Statutory Auditors |                                       |                    |                                       |      |                         |        |                             |
|-----------------------------|---------------------------------------|--------------------|---------------------------------------|------|-------------------------|--------|-----------------------------|
| Position                    | Members<br>(Last name and first name) | Appointed<br>since | In office<br>until                    | List | Indep. based<br>on Code | %      | Number other<br>assignments |
| Chairman                    | Guarna Luca Aurelio                   | 28 Apr., 2008      | Financial statements<br>at 31.12.2010 | M    | ●                       | 100%   | 21                          |
| Standing Auditor            | Cosconati Marcello                    | 28 Apr., 2008      | Financial statements<br>at 31.12.2010 | M    | ●                       | 77.78% | 3                           |
| Standing Auditor            | Pozza Lorenzo                         | 28 Apr., 2008      | Financial statements<br>at 31.12.2010 | M    | ●                       | 100%   | 9                           |
| Alternate Auditor           | Bettoni Stefania                      | 28 Apr., 2008      | Financial statements<br>at 31.12.2010 | M    | -                       | -      | -                           |

### AUDITORS WHO RESIGNED FROM THE POSITION DURING THE YEAR UNDER CONSIDERATION

|                   |                               |            |                     |   |   |   |   |
|-------------------|-------------------------------|------------|---------------------|---|---|---|---|
| Alternate Auditor | Paolillo Mario <sup>(1)</sup> | 28.04.2008 | Bilancio 31.12.2010 | M | - | - | - |
|-------------------|-------------------------------|------------|---------------------|---|---|---|---|

LEGAL NUMBER NECESSARY FOR SUBMITTING THE LISTS DURING THE LAST APPOINTMENT: 1%

NUMBER OF MEETINGS HELD DURING THE YEAR UNDER CONSIDERATION: 9

(1) Passed away on 30 November 2010.

#### Key

**Position:** Indicates whether is Chairman, Standing Auditor, Alternate Auditor.  
**List:** Indicates M/m whether the Auditor was appointed from the majority list (M) or from the minority list (m).  
**Indep. based on Code:** it indicates "●" if the Standing Statutory Auditor can be qualified as independent according to the criteria of the Code.  
**%:** indicates the attendance in percentage terms of the Statutory Auditor at the Meetings of the Board (in calculating this percentage the number of Meetings was considered which the Statutory Auditor attended compared to the number of Meetings of the Board that were held during the year under consideration or after his appointment).  
**Number other assignments:** indicates the total number of assignments as Directors or Statutory Auditors in companies as per Book V, Title V, Chapters V (S.p.A.), VI (S.A.p.A.) and VII (S.r.l.) of the Civil Code that are important according to art. 148-bis of the Consolidated Law on Finance. The total list of the assignments, pursuant to art. 144-*quinqüesdecies* of the above-mentioned Issuer Regulations based on CONSOB Resolution no. 17326 dated 13 May 2010 is published by CONSOB and is available on its website ([www.consob.it](http://www.consob.it)).





## Attachment 1

### Principal characteristics of existing risk management and internal controls over financial reporting process (pursuant to art. 123-bis, paragraph 2, letter b) of the Consolidated Law on Finance)

#### Foreword

The Terna Group drafted the “262 Control Model” with the objective of defining operational modalities for assessing the “Internal Control System” hereinafter referred to as (ICS) that oversees the drafting of the financial statements in order to issue the certification required as per paragraphs 2 and 5 of art. 154-bis of the Consolidated Law on Finance.

The ICS that oversees the drafting of the financial statements is in line with the criteria envisaged in the Guidelines of the “Terna Group’s Internal Control System” approved by the Board of Directors on 21 December 2006, in which the ICS is recognized as “the entirety of regulations, procedures and organizational structures that through an appropriate identification, measuring and managing process and monitoring of the principal risks, allow a proper Corporate management that is in line with the objects set by Terna”.

The provisions of Law no. 262 (dated 28 December 2005 subsequently modified by Legislative Decree no. 303 dated 29 December 2006) relative to the ICS that oversees the drafting of the financial statements have the principal objective of ensuring that the financial informative note provides a truthful and proper representation of the Company’s shareholders’ equity as well as its economic and financial position in compliance with the commonly accepted accounting principles.

On the basis of the provisions envisaged by art. 154-bis of the Consolidated Law on Finance, the ICS that oversees the drafting of the financial statements, actively involving all the Corporate departments, is focused on the reliability objectives pursued by establishing adequate “accounting administrative procedures” and by verifying their actual implementation. Updating the field of activity (scoping) and processes to be analyzed must be carried out by the Executive in Charge (hereinafter referred to as “EIC”) at least once a year in order to analyze the variations that have impacted the ICS and integrate/modify accordingly the administrative and accounting procedures.

This update must be appropriately substantiated in order to guarantee the traceability of activities.

#### Description of the principal characteristics of the existing risk management and internal controls over financial reporting

##### a) Phases of the existing risk management and internal controls over financial reporting.

The analysis approach of the ICS that oversees drafting the financial statements adopted by Terna is based on a twofold method of analysis:

##### Individual Company Analysis

Overall analysis (brief) of the individual companies of the Group with reference to 5 elements that form the CoSO report, specifically focusing on the adequacy of the financial informative note. This is mainly an analysis of the infrastructural components of the Internal Control System (the overseeing activities carried out by the Board of Directors, by the Internal Control Committee, by the Board of Statutory Auditors, as well as the Corporate policies and general group policies etc.) conducted in general terms but with a particular focus on the consequences of the quality of the economic and financial information.

The establishment, management and assessment of the ICS at the individual company level is to be carried out by those in charge of the various company departments (management) with regard to their respective duties, in line with the structure of the “individual company” being analyzed.

The objective of the individual company analysis is to identify any shortcomings in the general control of the individual company that would potentially render ineffective even the best structure of controls overseeing the processes.

The assessment is expressed with a “benchmarking” activity with respect to the reference procedures defined or referred to by official bodies or with the international best-practices adopted by companies similar to the Terna Group.

This method is applied by filling out a check list based on the five components of the control system (Control Environment, Risk Assessment, Control Activity, Information System and Communication Flows, Monitoring), developed in specific control objectives.

Controls are assessed on the basis of the following requirements, where applicable:

- existence of the control tool (organizational structure, legal structure, process);
- adequate communication regarding the existence of the control tool identified for all the bodies referred to;



- understanding on the part of the company's employees of their role and responsibility in implementing the identified control tool;
- appropriate and effective monitoring of the control tool;
- management support in implementing the control tool;
- application, or action undertaken by the management aimed at ensuring compliance with the implemented control tool.

### Individual Process Analysis

Analysis of relevant processes by establishing guidelines that define the principal risks on the financial informative note and relative controls aimed at mitigating them. The individual process analysis allows assessing the action plan and operational level of the controls on Corporate processes and sub-processes on which the financial informative note is based. The terms for carrying out this analysis are the establishment of administrative and accounting procedures for preparing the half-year report/consolidated report that include the execution of specific control activities aimed at preventing the occurrence of risks with significant errors in financial statements during the development of the processes. The process analysis and the subsequent establishment of administrative and accounting procedures requires the selection of "significant processes". For this purpose, it is necessary to carry out specific "scoping" in order to identify both the significant items in the financial statements/financial informative note as well as associate the significant information to the processes. The relevance of the financial informative note is assessed with reference to the possible consequence that its omission or misrepresentation could determine in decisions made by the individuals who are notified about the note through the financial statements.

With regard to the above, quantity parameters are identified, that are normally defined in terms of percentages compared to income before taxes, as well as quality parameters capable of rendering an information relevant, even if the amount is lower than the level of relevance identified.

Identifying significant information is carried out through the combination of quantitative parameters, linked to the level of significance defined for Terna and quality parameters linked to the specific risk for financial statements sections or informative notes. Identifying quality parameters consists in considering possible "factors" that render significant various calculations, even if these do not exceed the threshold of materiality, by themselves. Investors could demonstrate a certain interest in various calculations in the financial statements that represent an important performance indicator or an important indicator for the sector they belong to.

The association of the information identified as being significant for the relative processes they are based on allows concentrating identification activities on those processes that can determine significant errors regarding the financial information. Each selected significant information/item in the financial statements must be associated with the processes that contribute to its elaboration, in order to determine the significant processes.

On the basis of quality and quantity parameters, after having defined the significant information and having selected the relevant processes, the EIC establishes the guidelines for "risk activities and controls" that represent administrative and accounting procedures and assesses their adequacy and effective implementing (assessment of their operational level). For this purpose, the analysis of significant processes occurs through the following operational steps:

- defining and analyzing activities that form the processes ("mapping");
- identifying and assessing risks for each activity and their being associated with the control objectives;
- identifying and assessing existing controls;
- assessing the operational level of existing controls.

Analyzing activities that form the processes ("mapping") is aimed at clearly identifying the process that creates the data or the comment to be represented in the financial statements, from identifying the initial event that originates it up to its being included in the accounting prospects or in the notes.

Mapping activities that form the processes are functional to the final objective of applying controls along the entire process of data creation or for the notes commenting the financial statements and should be capable of ensuring that the information having an administrative impact is collected, processed and sent correctly and in a timely fashion.

For every process, for mapping purposes and the subsequent association of the risks and controls, the "key" elements must be identified that are useful in identifying existing risks and controls.

Verifying the effectiveness of the action plan and the actual operational level of the "key" controls is carried out through a testing activity that is conducted by a dedicated structure, using sampling techniques that are recognized by the international best practices.

Control assessment, where deemed necessary, can involve identifying compensatory controls, corrective measures and improvement plans. The results of these activities are submitted to the evaluation of the Executive in Charge who in turn notifies the company executives.

### b) Roles and Departments involved.

#### The Executive in Charge

Is responsible for:

- annually updating the scope of activity and the significant processes considering the factors of change/risk communicated by the Directors of Terna S.p.A. and by the management of the companies that are individually significant;

- establishing and updating adequate administrative and accounting procedures for drafting the financial statements and the consolidated financial statements;
- providing, with the collaboration of the Human Resource and Organization Department, to disseminate administrative and accounting procedures and action plans;
- supporting the Directors of Terna S.p.A. and the management of the companies that are individually significant in executing operational, control and reporting activities that are part of their specific duties.

The EIC can rely on the assistance of qualified external companies with specialized professional staff for carrying out plan assessment activities and the assessment of the operational levels of controls over administrative and accounting procedures.

### **Internal Audit e Risk Management**

Are responsible for:

- supporting the EIC in its activities for assessing the adequacy and actual application of administrative and accounting procedures for drafting the financial statements and the consolidated financial statements and the suitability and the proper operation of the Internal Control System and relative mechanisms for risk management;
- coordinating with the EIC in defining the Annual Audit Plan for administrative and accounting processes in order to take into account the results of the operational risk analysis carried out by the company departments;
- providing the EIC with a suitable information flow regarding the results of activities connected with the audit plan for administrative and accounting processes, with the modalities shared with the EIC;
- in case of involvement in specific testing activities, ensuring the necessary collaboration and changes in the audit plan and in defining priorities also, if necessary, with the assistance of the administrative body in charge.

### **Terna S.p.A.'s Directors**

Are responsible for:

- coordinating those in charge of individual controls in executing the controls they are responsible for;
- coordinating individual controls in establishing and implementing the Action Plan;
- supporting the activities carried out by the EIC and ensure access to all documents/information useful in carrying out his activities;
- preparing and forwarding in the time frames established by the reporting calendar the certifications regarding the control activities and their operational level.

### **The management of the companies that are individually significant**

Is responsible for:

- coordinating those in charge of individual controls in executing the controls they are responsible for;
- assessing, in collaboration with the EIC, the ICS of the company that is individually significant;
- preparing and forwarding, in the time frame established by the reporting calendar, the certifications regarding the ICS of the company that is individually significant.

To enable the EIC and the administrative bodies in charge to issue the certificates in compliance with art. 154-*bis* of the Consolidated Law on Finance introduced with Law no. 262/2005, it was necessary to define a system of "chain" certificates with the objective of ensuring the adequacy and actual implementation of administrative and accounting procedures drafted as part of the "262 Project", of preparing and disseminating the Plan for corrective measures, where necessary, and to update such procedures.

The certification, issued with the CONSOB form, is based on a complex evaluation process that includes:

- collecting internal "chain" certificates issued by the Directors of Terna S.p.A. and by the management of the companies that are individually significant. The existence of a periodic reporting flow allows carrying out the following:
  - periodic assessment of the plan for existing controls and consequent updating of administrative and accounting procedures;
  - assessment of the operational level of existing controls and the subsequent certification of the actual implementation of administrative and accounting procedures;
  - assessment of the shortcomings (absence of control or failure to execute controls) that emerge with reference to their impacting the informative note on the financial statements;
- the assessment of the actual operational level of administrative and accounting procedures carried out by the EIC;
- the final assessment of the adequacy of administrative and accounting procedures by the CEO and the EIC. This activity is supported by the assessment of the plan for specific controls as well as by that for their operational level as mentioned above. It is therefore carried out overall with reference to the probability that following one or more significant shortcomings an error in the financial statements could occur and with reference to the risk that this error may have been significant.

Any significant shortcomings highlighted by the assessment process must be immediately notified jointly with the outcome of the compensatory controls carried out by the CEO and the EIC, to the Internal Control Committee, to the Supervisory Body and to the Board of Statutory Auditors of Terna S.p.A.





# Glossary

## 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.

## 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.

## 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.

## 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".

## 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.

## Gigawatt (GW)

Unit of measurement equal to one billion watts (1,000 megawatts).

## 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.

## Gross production of electricity

Sum of the quantities of electrical energy produced, measured at the electrical generator terminals.

## High voltage

Nominal voltage greater than 35 kV and less than or equal to 220 kV.

## High-voltage electricity line

An electricity line is a system that connects two power stations, or a power station and an energy input or withdrawal point. The length of an electricity line (km/line) is expressed as the length of the circuits projection over the ground (geographical length).

## High-voltage power station

A transfer power station is the part of the grid used both for dividing electricity among the grid's lines and for transferring electricity among grids with different voltages.

## Interconnection line

High-voltage power line in alternating current (a.c.) or direct current (d.c.) which links two different electrical transmission or distribution grids or even two generation plants.

## 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.

## kilowatt-hour (kWh)

Unit of measurement that expresses the quantity of electricity equal to 1,000 watts provided or requested in one hour.

## kW

Unit of measurement of power (1 kW=1000 J/sec).

## kWh

Unit of measurement of energy.

## 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.

**Megavolt-ampere (MVA)**

Unit of measurement of the apparent electrical power.

**Megawatt (MW)**

Unit of measurement equal to one million watts.

**National Transmission Grid (NTG)**

National electricity transmission grid as defined by the Decree of the Ministry of Industry of 25 June 1999 and subsequent amendments and additions.

**Net production of electricity**

Sum of the quantities of electrical energy produced, measured at the outgoing points of the production plants.

**Operations planning**

Preparation of plans and schedules for operation of the electricity system.

**Peak power**

The highest value of electrical power supplied or absorbed at any point of the system during a specific time interval.

**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.

**Power station**

Part of a grid, 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.

**Producer**

Natural or legal person that produces electricity, regardless of ownership of the generation plant.

**Production**

Generation of electrical energy, in any way.

**RAB (Regulatory Asset Base)**

Value of the net capital invested, as recognised by the Italian Authority for Electricity and Gas for transport and distribution companies for the purposes of determining the applicable tariffs.

**Requirement**

Demand for electrical energy to be satisfied by the national electricity system. It shows a variable trend throughout the day, month and year.

**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.

**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.

**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.

**Transformation station**

Part of a grid consisting of the set of equipment used to transfer electricity between grids with different voltages.

**Transformer**

Electrical machine used for the connection and transfer of energy between grids at different voltage levels.

**Transmission**

Electricity transport and transformation activities along the interconnected high- and very-high-voltage grid for the purposes of delivery to clients, distributors and recipients of self-produced energy.

**Transmission activity**

The activity of transporting and transformation electricity across the grid.

**Transmission line**

High- and very-high-voltage power line, overhead or cable, used for the transport of electricity from the production plants to the distribution systems or to users.

**Unified management of the grid**

Coordinated management of all portions of the Grid.

**Very-high voltage**

Nominal voltage over 220 kV.

**Volt**

Unit of measurement of voltage.

**Watt**

Unit of measurement of electric power.

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