Naturgy

Naturgy Energy Group, S.A.
Annual Financial Report

2021

Auditor's Report on Naturgy Energy Group, S.A.

(Together with the annual accounts and directors' report of Naturgy Energy Group, S.A. for the year ended 31 December 2021)

(Translation from the original in Spanish. In the event of discrepancy, the Spanish-language version prevails.)

KPMG Auditores, S.L.
Paseo de la Castellana, 259C
28046 Madrid

Independent Auditor's Report on the Annual Accounts

(Translation from the original in Spanish. In the event of discrepancy, the Spanish-language version prevails.)

To the shareholders of Naturgy Energy Group, S.A.

REPORT ON THE ANNUAL ACCOUNTS

Opinion

We have audited the annual accounts of Naturgy Energy Group, S.A. (the "Company"), which comprise the balance sheet at 31 December 2021, and the income statement, statement of changes in equity and statement of cash flows for the year then ended, and notes.

In our opinion, the accompanying annual accounts give a true and fair view, in all material respects, of the equity and financial position of the Company at 31 December 2021, and of its financial performance and its cash flows for the year then ended in accordance with the applicable financial reporting framework (specified in note 2 to the accompanying annual accounts) and, in particular, with the accounting principles and criteria set forth therein.

Basis for Opinion

We conducted our audit in accordance with prevailing legislation regulating the audit of accounts in Spain. Our responsibilities under those standards are further described in the Auditor's Responsibilities for the Audit of the Annual Accounts section of our report.

We are independent of the Company in accordance with the ethical requirements, including those regarding independence, that are relevant to our audit of the annual accounts pursuant to the legislation regulating the audit of accounts in Spain. We have not provided any non-audit services, nor have any situations or circumstances arisen which, under the aforementioned regulations, have affected the required independence such that this has been compromised.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

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Key Audit Matters

Key audit matters are those matters that, in our professional judgement, were of most significance in the audit of the annual accounts of the current period. These matters were addressed in the context of our audit of the annual accounts as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

Recoverable amount of non-current investments in Group companies and associates See notes 3.3, 3.19, 4 y 7 to the annual accounts	
Key audit matter	*How the matter was addressed in our audit*
At 31 December 2021 the Company has recognised non-current investments in Group companies and associates amounting to Euros 31,284 million. The recoverable amount of these investments in Group companies and associates is determined, for those companies in which there is objective evidence of impairment, by applying valuation techniques which often require the exercising of judgement by the Directors and the use of assumptions and estimates. Due to the significance of the investments and the uncertainty associated with these estimates, this has been considered a key audit matter.	Our audit procedures included the following: • Evaluating the design and implementation of the key controls related to the process of calculating the recoverable amount. • Assessing the existence of evidence of impairment, as well as the reasonableness of methodology and assumptions used to estimate the recoverable amount with the involvement of our specialists. • Assessing whether the disclosures in the annual accounts meet the requirements of the financial reporting framework applicable to the Company.

Other Information: Directors' Report

Other information solely comprises the 2021 directors' report, the preparation of which is the responsibility of the Company's Directors and which does not form an integral part of the annual accounts.

Our audit opinion on the annual accounts does not encompass the directors' report. Our responsibility regarding the information contained in the directors' report is defined in the legislation regulating the audit of accounts, as follows:

a) Determine, solely, whether the non-financial information statement and certain information included in the Annual Corporate Governance Report and the Annual Report on Directors' Remuneration, as specified in the Spanish Audit Law, have been provided in the manner stipulated in the applicable legislation, and if not, to report on this matter.

b) Assess and report on the consistency of the rest of the information included in the directors' report with the annual accounts, based on knowledge of the entity obtained during the audit of the aforementioned annual accounts. Also, assess and report on whether the content and presentation of this part of the directors' report are in accordance with applicable legislation. If, based on the work we have performed, we conclude that there are material misstatements, we are required to report them.

Based on the work carried out, as described above, we have observed that the information mentioned in section a) above has been provided in the manner stipulated in the applicable legislation, that the rest of the information contained in the directors' report is consistent with that disclosed in the annual accounts for 2021, and that the content and presentation of the report are in accordance with applicable legislation.

Directors' and Audit and Control Committee's Responsibilities for the Annual Accounts

The Directors are responsible for the preparation of the accompanying annual accounts in such a way that they give a true and fair view of the equity, financial position and financial performance of the Company in accordance with the financial reporting framework applicable to the entity in Spain, and for such internal control as they determine is necessary to enable the preparation of annual accounts that are free from material misstatement, whether due to fraud or error.

In preparing the annual accounts, the Directors are responsible for assessing the Company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the Directors either intend to liquidate the Company or to cease operations, or have no realistic alternative but to do so.

The Audit and Control Committee is responsible for overseeing the preparation and presentation of the annual accounts.

Auditor's Responsibilities for the Audit of the Annual Accounts

Our objectives are to obtain reasonable assurance about whether the annual accounts as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion.

Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with prevailing legislation regulating the audit of accounts in Spain will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these annual accounts.

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As part of an audit in accordance with prevailing legislation regulating the audit of accounts in Spain, we exercise professional judgement and maintain professional scepticism throughout the audit. We also:

– Identify and assess the risks of material misstatement of the annual accounts, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.

– Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control.

– Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the Directors[2].

– Conclude on the appropriateness of the Directors' use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Company's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the annual accounts or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Company to cease to continue as a going concern.

– Evaluate the overall presentation, structure and content of the annual accounts, including the disclosures, and whether the annual accounts represent the underlying transactions and events in a manner that achieves a true and fair view.

We communicate with Naturgy Energy Group, S.A.'s Audit and Control Committee regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide the entity's Audit and Control Committee with a statement that we have complied with the applicable ethical requirements, including those regarding independence, and to communicate with them all matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

From the matters communicated to the Audit and Control Committee of the entity, we determine those that were of most significance in the audit of the annual accounts of the current period and which are therefore the key audit matters.

We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter.

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REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS

European Single Electronic Format

We have examined the digital file of Naturgy Energy Group, S.A. for 2021 in European Single Electronic Format (ESEF) comprising an XHTML file with the annual accounts for the aforementioned year, which will form part of the annual financial report.

The Directors of Naturgy Energy Group, S.A. are responsible for the presentation of the 2021 annual financial report in accordance with the format requirements stipulated in Commission Delegated Regulation (EU) 2019/815 of 17 December 2018 (hereinafter the "ESEF Regulation"). In this regard, they have incorporated the Annual Corporate Governance Report and Annual Report on Directors' Remuneration by means of a reference thereto in the directors' report.

Our responsibility consists of examining the digital file prepared by the Company's Directors, in accordance with prevailing legislation regulating the audit of accounts in Spain. This legislation requires that we plan and perform our audit procedures to determine whether the content of the annual accounts included in the aforementioned digital file fully corresponds to the annual accounts we have audited, and whether the annual accounts have been formatted, in all material respects, in accordance with the requirements of the ESEF Regulation.

In our opinion, the digital file examined fully corresponds to the audited annual accounts, and these are presented, in all material respects, in accordance with the requirements of the ESEF Regulation.

Additional Report to the Audit and Control Committee

The opinion expressed in this report is consistent with our additional report to the Company's Audit and Control Committee dated 3 February 2022.

Contract Period

We were appointed as auditor by the shareholders at the ordinary general meeting on 9 March 2021 for a period of three years, from the year ended 31 December 2021.

KPMG Auditores, S.L.
On the Spanish Official Register of
Auditors ("ROAC") with No. S0702

(Signed on original in Spanish)

Eduardo González Fernández
On the Spanish Official Register of Auditors ("ROAC") with No. 20435

3 February 2022

Naturgy Energy Group, S.A.
Annual Report
2021

Annual Report

Balance sheet.
Income statement.
Statement of recognised income and expense.
Statement of changes in equity.
Cash flow statement.
Notes to the annual accounts.

This 2021 Annual Report is a translation of a report originally issued in Spanish. In the event of a discrepancy, the Spanish language version prevails.

Naturgy Energy Group, S.A.
Balance sheet (million euro)

	Note	31.12.2021	31.12.2020
NON-CURRENT ASSETS	**Note**	**31,809**	**31,048**
Intangible assets	5	2	3
Patents, licences, trademarks and other		1	1
Other intangible assets		1	2
Property, plant and equipment	6	110	113
Land and buildings		98	101
Other property, plant and equipment		12	12
Long-term investments in group companies and associates	7	31,284	30,594
Equity instruments		16,138	15,417
Loans to companies		15,146	15,177
Long-term investments	8	9	9
Equity instruments		4	5
Other financial assets		5	4
Other non-current assets	9-14	231	136
Derivatives		231	136
Deferred tax assets	17	173	193
CURRENT ASSETS		**6,927**	**3,845**
Trade and other receivables	9-14	2,282	312
Trade receivables for sales and services		56	37
Trade receivables, group companies and associates		213	143
Derivatives		1,865	123
Other sundry receivables		12	3
Current tax assets		134	4
Other amounts receivable to Public Administrations		2	2
Short-term investments in group companies and associates	7	2,379	743
Loans to companies		2,376	628
Other financial assets		3	115
Short-term investments	8	57	171
Other financial assets		57	171
Short-term prepayments and accrued expenses		1	1
Cash and cash equivalents	10	2,208	2,618
Cash at banks and in hand		889	1,076
Other cash equivalents		1,319	1,542
TOTAL ASSETS		**38,736**	**34,893**

Notes 1 to 30 form an integral part of these annual accounts.

Naturgy Energy Group, S.A.

Balance sheet **(million euro)**

	Note	31.12.2021	31.12.2020
EQUITY	11	**18,858**	**18,393**
SHAREHOLDERS' FUNDS		**18,901**	**18,471**
Capital		970	970
Authorised capital		970	970
Share premium		3,808	3,808
Reserves		11,304	11,291
Legal and statutory		300	300
Other reserves		11,004	10,991
Treasury shares		(4)	(1)
Profit/(loss) for the year		1,706	98
Retained earnings		1,778	—
Interim dividend		(679)	(785)
Other equity instruments		18	14
VALUE CHANGE ADJUSTMENTS		**(43)**	**(78)**
Available-for-sale financial assets		—	(1)
Hedging operations		(43)	(77)
NON-CURRENT LIABILITIES		**12,335**	**13,079**
Long-term provisions	12	309	373
Long-term post-employment obligations		242	258
Other provisions		67	115
Long-term borrowings	13	2,434	2,829
Bank borrowings		2,372	2,720
Derivatives	14	61	108
Other financial liabilities		1	1
Amounts owing to group companies and associates falling due in more than one year	15	9,110	9,530
Deferred tax liabilities	17	250	211
Other liabilities	14-16	232	136
Derivatives		232	136
CURRENT LIABILITIES		**7,543**	**3,421**
Short-term borrowings	13	421	399
Bank borrowings		402	257
Derivatives		19	21
Other financial liabilities		—	121
Amounts owing to group companies and associates falling due in less than one year	15	4,823	2,560
Trade and other payables	16	2,298	461
Trade payables		259	141
Trade payables, group companies and associates		103	59
Derivatives	14	1,873	123
Other sundry payables		12	10
Personnel (outstanding remuneration)		33	18
Current tax liabilities		—	93
Other amounts payable to Public Administrations		18	17
Short-term prepayments and accrued expenses		1	1
TOTAL EQUITY AND LIABILITIES		**38,736**	**34,893**

Notes 1 to 30 form an integral part of these annual accounts.

Naturgy Energy Group, S.A.

Income statement

		(million euro)	
		2021	2020
Revenue	18	2,082	2,292
Sales		802	667
Income from services rendered		—	1
Income from equity instruments of group companies and associates	7	932	1,271
Income from marketable securities and other financial instruments of group companies and associates		348	353
Raw materials and consumables	19	(803)	(667)
Consumption of goods		(803)	(667)
Other operating income	22	81	156
Supplementary income and other operating income		81	155
Operating grants released to the income statement		—	1
Personnel expenses	20	(126)	(115)
Wages, salaries and related expenses		(112)	(98)
Social Security		(9)	(11)
Provisions		(5)	(6)
Other operating expenses	21	(110)	(170)
External services		(109)	(171)
Taxes		(2)	(1)
Impairment losses and variation in trade provisions		1	2
Fixed asset depreciation/amortisation	5 - 6	(13)	(14)
Impairment and results on disposals of fixed assets		871	(1,087)
Gain/(loss) on disposals of tangible fixed assets	6	1	—
Impairment of and losses from equity instruments of group companies and associates	7	869	(1,088)
Gain/(loss) on disposals of equity interests in Group companies and associates	7	1	1
OPERATING PROFIT/(LOSS)		**1,982**	**395**
Financial income		3	5
Negotiable securities and other financial instruments		3	5
- In third parties		3	5
Financial expenses		(349)	(339)
Borrowings from group companies and associates		(303)	(292)
Borrowings from third parties		(46)	(47)
Impairment and gains/(losses) on disposals of financial instruments		(1)	—
Impairments and losses		(1)	—
Variation in fair value of financial instruments		—	1
Fair value through profit and loss		—	1
Exchange differences		—	(2)
NET FINANCIAL INCOME	23	**(347)**	**(335)**
PROFIT/(LOSS) BEFORE TAXES		**1,635**	**60**
Income tax	17	71	38
PROFIT FOR THE YEAR		**1,706**	**98**
Basic and diluted earnings per share in euro		1.77	0.10

Notes 1 to 30 form an integral part of these annual accounts.

Naturgy Energy Group, S.A.
Statement of changes in equity

A) STATEMENT OF RECOGNISED INCOME AND EXPENSE	Note		(million euro)
		2021	2020
PROFIT FOR THE YEAR		1,706	98
INCOME AND EXPENSE RECOGNISED DIRECTLY IN EQUITY		38	(22)
Cash flow hedges		27	(37)
Actuarial gains and losses and other adjustments	12	22	7
Tax effect	17	(11)	8
RELEASES TO INCOME STATEMENT		14	12
Cash flow hedges		19	16
Tax effect	17	(5)	(4)
TOTAL INCOME AND EXPENSE RECOGNISED IN EQUITY		**1,758**	**88**

Notes 1 to 30 form an integral part of these annual accounts.

Naturgy Energy Group, S.A.

Statement of changes in equity

B) TOTAL STATEMENT OF CHANGES IN EQUITY **(million euro)**

	Share capital	Share premium	Reserves	Treasury shares	Profit or loss brought forward	Retained Earnings	Profit of the year	Interim dividend	Other instruments	Value changes adjustments	Total
Balance at 1.1.2020	**984**	**3,808**	**11,573**	**(121)**	**—**	**—**	**4,415**	**(754)**	**9**	**(61)**	**19,853**
Total recognised income and expense	—	—	2	—	—	—	98	—	5	(17)	88
Operations with shareholders or owners											
- Capital reduction	(14)	—	(284)	298	—	—	—	—	—	—	—
- Dividend distribution	—	—	—	—	(9)	—		(1,361)	—	—	(1,370)
- Trading in treasury shares	—	—	—	(178)		—		—	—	—	(178)
Other changes in equity	—	—		—	9	3,076	(4,415)	1,330	—	—	—
Balance at 31.12.2020	**970**	**3,808**	**11,291**	**(1)**	**—**	**3,076**	**98**	**(785)**	**14**	**(78)**	**18,393**
Total recognised income and expense	—	—	14	—	—	—	1,706	—	4	34	1,758
Operations with shareholders or owners											
- Capital reduction	—	—	—	—	—	—	—	—	—	—	—
- Dividend distribution	—	—	—	—	(611)	—	—	(679)	—	—	(1,290)
- Trading in treasury shares	—	—	—	(3)	—	—	—	—	—	—	(3)
Other changes in equity	—	—	(1)	—	611	(1,298)	(98)	785	—	1	—
Balance at 31.12.2021	**970**	**3,808**	**11,304**	**(4)**	**—**	**1,778**	**1,706**	**(679)**	**18**	**(43)**	**18,858**

Notes 1 to 30 form an integral part of these annual accounts.

Naturgy Energy Group, S.A.
Cash flow statement **(million euro)**

	Note	31.12.2021	31.12.2020
Profit for the year before tax		**1,635**	**60**
Adjustments to results		**(1,790)**	**(196)**
Fixed asset depreciation/amortisation	5 and 6	13	14
Impairment adjustments		(869)	1,086
Change in provisions		(2)	(7)
Profit/(loss) on write-offs and disposals of fixed assets		(1)	—
Profit/(loss) on write-offs and disposals of financial instruments		(1)	(1)
Financial income		(1,283)	(1,629)
Financial expenses		349	339
Variation in fair value of financial instruments		—	(1)
Other income and expenses		4	3
Changes in working capital		**(416)**	**(242)**
Debtors and other receivables		(2,280)	163
Creditors and other payables		1,863	(405)
Other cash flows from operating activities		**2,157**	**1,821**
Interest paid		(318)	(346)
Dividends received		1,749	1,381
Interest collected		344	350
Income tax collections/(payments)		382	436
Cash flows from operating activities		**1,586**	**1,443**
Amounts paid on investments		**(3,392)**	**(270)**
Group companies and associates		(3,255)	(232)
Intangible assets		—	(1)
Property, plant and equipment		(10)	(8)
Other financial assets		(127)	(29)
Amounts collected from divestments		**847**	**547**
Group companies and associates		845	486
Property, plant and equipment		2	6
Other financial assets		—	55
Cash flows from investing activities		**(2,545)**	**277**
Collections and payments on equity instruments		**(3)**	**(185)**
Acquisition of own equity instruments		(3)	(185)
Collections and payments financial liability instruments		**1,842**	**1,279**
Issuance		5,195	3,887
Bank borrowings		52	1,225
Payables to Group companies and associates		5,046	2,662
Other payables		97	—
Repayment/redemption of		(3,353)	(2,608)
Bank borrowings		(255)	(247)
Payables to Group companies and associates		(3,086)	(2,288)
Other payables		(12)	(73)
Dividend payments		**(1,290)**	**(1,370)**
Cash flow from financing activities		**549**	**(276)**
NET INCREASE/DECREASE IN CASH OR CASH EQUIVALENTS		**(410)**	**1,444**
Cash and cash equivalents at the beginning of the year		2,618	1,174
Cash and cash equivalents at the year end		2,208	2,618

Notes 1 to 30 form an integral part of these annual accounts.

Contents of the notes to the annual accounts for 2021

Notes to the annual accounts of Naturgy Energy Group, S.A. for the year ended 31 December 2021

Note 1. General information

Naturgy Energy Group, S.A. (“the Company”), the parent company of the Naturgy group (“Naturgy”), was incorporated as a public limited company in 1843 and its registered office for corporate purposes is in Avda. América 38, Madrid. On 27 June 2018, the shareholders, in general meeting, agreed to change the company’s business name to Naturgy Energy Group, S.A., formerly Gas Natural SDG, S.A.

The company’s corporate objects, as per its articles of association, comprise the following activities:

a. All types of activities related to the gas and electricity business and any other type of existing energy source, the production and selling of electrical, electro-mechanical and electronic equipment and components, management of architectural projects, civil engineering works, public services and gas and hydro-carbon distribution in general; management of communications and telecommunications networks and maintenance of electro- and gas-related appliances; as well as consulting, business and energy planning services and the rationalisation of energy use, research, development and exploitation of new technologies, communications, computer and industrial security systems; training and selection of human resources and real estate management and development.

b. Acting as a holding company, incorporating companies or holding shares as a member or shareholder in other companies no matter what their corporate purpose or nature, by subscribing, acquiring or holding shares, participation units or any other securities deriving from the same, subject to compliance with the legal requirements in each case.

The Company’s most relevant ordinary activity is the administration and management of its shareholdings in subsidiaries. In 2021 it also has had gas supply contracts for other Naturgy companies.

The Company’s shares are listed on the four Spanish stock exchanges, the continuous market and form part of the Ibex 35 stock index.

On 26 January 2021, Global InfraCo O (2), S.à.r.l., wholly owned by the Australian fund IFM (IFM GIF), announced the terms and conditions of the partial voluntary offer to acquire shares in Naturgy Energy Group, S.A. for a maximum of 220 million shares, equivalent to 22.689% of Naturgy's share capital ("the Offer"). On 18 February 2021, it was admitted for processing by the Spanish National Securities Market Commission (CNMV).

The Offer price of 23 €/share was adjusted to 22.37 €/share due to the supplementary dividend of 0.63 €/share paid by Naturgy on 17 March 2021 and finally to 22.07 €/share due to the supplementary dividend of 0.30 €/share paid by Naturgy on 4 August 2021.

On 18 March 2021, the Mexican Federal Competition Commission (COFECE) unanimously and unconditionally authorised the business concentration that would result from the Offer, thus fulfilling one of the conditions to which the Offer was subject.

On 8 September 2021, the CNMV authorised the partial voluntary offer. Previously, on 3 August 2021 the offeror obtained authorisation from the Council of Ministers for the foreign direct investment in Spain, subject to certain conditions which were accepted by the offeror.

On 14 October 2021 the acceptance level of the offer was released, consisting of 105,021,887 shares which represented 10.83% of Naturgy's share capital, and the offeror decided to waive the 17% minimum acceptance condition. The offer was settled on 19 October 2021 and IFM GIF became a significant shareholder of Naturgy.

Note 2. Basis of presentation

The Company’s annual accounts for 2020 were approved at the annual general meeting of shareholders on 9 March 2021.

The annual accounts for 2021, which were drawn up and signed by the Company’s Board of Directors on 3 February 2022, will be submitted to the general shareholders’ meeting for approval; they are expected to be approved without any changes.

The accompanying annual accounts are presented in accordance with current mercantile legislation and with the rules laid down in the National Chart of Accounts approved by Royal Decree 1514/2007 of 16 November and the amendments incorporated therein by Royal Decree 1159/2010 of 17 September, Royal Decree 602/2016 of 2 December, and Royal Decree 1/2021 of 12 January, as well as by the adoption of the Resolution of 10 February 2021 of the Spanish Institute of Accounting and Auditing which lays down rules for the recognition, valuation and preparation of the annual accounts for the recognition of income from sales of goods and services.

These annual accounts have been prepared based on the Company's accounting records in order to fairly present its equity and financial position at 31 December 2021, as well as the Company's results, changes in equity and cash flows for the year then ended.

At 31 December 2021, the Company's working capital was negative by Euros 616 million. In this respect, the Company's liquidity statements envisaged for this year together with the amounts available under credit lines (Note 14) will ensure coverage of the goodwill.

The figures set out these annual accounts are expressed in million euros, which is the Company's functional and presentation currency, unless otherwise stated.

The annual accounts present for comparative purposes, for each item in the balance sheet, income statement, statement of changes in equity, cash-flow statement and notes to the accounts, the figures corresponding to the previous year which formed part of the 2020 annual accounts as well as the figures for 2021.

The accounting principles and the main measurement standards used by the Company to prepare the annual accounts for the year are the same as those applied in the Company's annual accounts for the year ended 31 December 2020, except for the adoption of Royal Decree 1/2021 and the adoption of the Resolution of 10 February 2021 of the Spanish Institute of Accounting and Auditing, which lays down rules for the recognition, valuation and preparation of the annual accounts for the recognition of income from sales of goods and services.

The main changes essentially concern the transposition to local accounting regulations of a major part of the standards contained in IFRS-EU 9, IFRS-EU 15, IFRS-EU 7 and IFRS-EU 13.

The impacts on the Company resulting from the adoption of Royal Decree 1/2021 are as follows:

Financial instruments

In relation to financial assets and liabilities, new policies are introduced for their classification, measurement and derecognition, and new rules for hedge accounting are introduced.

In the first application of this standard at 1 January 2021, the Company has opted for the practical solution of not restating comparative information for 2020, opting for prospective application for hedge accounting and the classification of financial instruments.

The option of changing the classification of 2020 assets and liabilities without affecting their valuation has been applied. There has been no adjustment to the carrying amount of financial assets and liabilities in reserves at 1 January 2021.

The impacts derived from initial application have been as follows:

Classification of financial assets

Investments in equity instruments classified as available-for-sale financial assets at 31 December 2020 have been classified as financial assets carried at cost, as their fair value cannot be determined by reference to a quoted market price. In addition, in relation to financial assets that are debt instruments and are not derivatives, the Company holds such assets mainly in order to obtain contractual cash flows and therefore they continue to be measured at amortised cost as from 1 January 2021.

The only impact on the Company arising from the adoption of Royal Decree 1/2021 relates to the classification and valuation of financial assets. In accordance with transitional provision two of Royal Decree 1/2021, the Company has applied the new criteria for the classification and valuation of financial assets and liabilities retroactively, in accordance with the provisions of recognition and measurement standard 22 "Changes in accounting policies, errors and accounting estimates" of the Spanish National Chart of Accounts. As a result, the Company has recognised financial investments in equity instruments at cost amounting to Euros 4 million (31 December 2020: Euros 5 million), which at the end of the previous year were recognised as available-for-sale financial assets. There has been no adjustment to the carrying amount of financial assets and liabilities in reserves at 1 January 2021 as a result of the application of the new accounting legislation.

The equivalence between the amounts classified by category of financial assets as of 31 December 2020 and 1 January 2021 is as follows:

	31.12.2020	01.01.2021
Trade and other receivables	16,164	
Financial assets at amortised cost		16,164
Other fair value financial assets through profit or loss	379	
Fair value financial assets through profit or loss		379
Investments in the equity of Group companies and associates	15,417	
Available-for-sale financial assets	5	
Financial assets at cost		15,422
Total	**31,965**	**31,965**

Except for the changes in the designations of the financial asset categories, Royal Decree 1/2021 has had no impact on equity.

The classification of the Company's financial liabilities for valuation purposes has not changed with respect to that included in the Annual accounts for 2020, with the exception of "Debts and payables", which have been reclassified as "Liabilities at amortised cost", without affecting the valuation criteria previously applied.

Accordingly, financial assets classified by class and category at 31 December 2020 beak down as follows:

At 31 December 2020	Amortised cost	At cost	Assets at fair value through profit and loss	Total
Equity instruments	—	15,417	—	15,417
Loans	15,177	—	—	15,177
Investments in group companies and associates	**15,177**	**15,417**	**—**	**30,594**
Equity instruments	—	5	—	5
Other financial assets	4	—	—	4
Non current investments	**4**	**5**	**—**	**9**
Derivatives (Note 14)	—	—	136	136
Other non-current assets	**—**	**—**	**136**	**136**
Total non current assets	**15,181**	**15,422**	**136**	**30,739**
Derivatives (Note 14)	—	—	123	123
Other assets	189	—	—	189
Trade and other receivables	**189**	**—**	**123**	**312**
Loans	628	—	—	628
Other financial assets	115	—	—	115
Investments in group companies and associates	**743**	**—**	**—**	**743**
Other financial assets	51	—	120	171
Current investments	**51**	**—**	**120**	**171**
Total current investments	**983**	**—**	**243**	**1,226**

Financial liabilities classified by class and category at 31 December 2020 break down as follows:

At 31 December 2020	Fair value through profit and loss	Amortised cost	Hedging derivatives	Total
Bank borrowings	—	2,720	—	2,720
Derivatives (Note 14)	—	—	108	108
Other financial liabilities	—	1	—	1
Non-current borrowings	**—**	**2,721**	**108**	**2,829**
Payable to group companies and associates	**—**	**9,530**	**—**	**9,530**
Derivatives (Note 14)	136	—	—	136
Other non-current financial liabilities	**136**	**—**	**—**	**136**
Total non-current borrowings	**136**	**12,251**	**108**	**12,495**
Bank borrowings	—	257	—	257
Derivatives (Note 14)	—	—	21	21
Other financial liabilities	—	121	—	121
Current borrowings	**—**	**378**	**21**	**399**
Payable to group companies and associates	**—**	**2,560**	**—**	**2,560**
Derivatives (Note 14)	123	—	—	123
Other financial liabilities	—	338	—	338
Trade and other payables	**123**	**338**	**—**	**461**
Total Current borrowings	**123**	**3,276**	**21**	**3,420**

Hedge accounting

The Company has chosen to apply hedge accounting under the standard. However, it has not made any substantial changes in its hedging model, confirming that its current hedging relationships qualify as hedges in accordance with the adoption of the new standard. The Company will record, in a separate equity item, the temporary value of the option contracts, the forward element of forward contracts and the base exchange rate differential in financial instruments in the event of their being excluded from the hedging relationship.

Revenue recognition

The standard has brought in a new model for the recognition of revenue derived from contracts with customers whereby revenue is recognised based on compliance with performance obligations with customers. Revenue reflects the transfer of goods or services to customers at an amount that reflects the consideration to which the entity expects to be entitled in exchange for such goods or services.

In addition, an asset (or inventory item) is recognised for the costs of fulfilling a contract with a customer and an expense accrual is recognised for the incremental costs of obtaining a contract with a customer, in both cases if they are expected to be recovered.

The Company has chosen the practical solution of applying the new standard for new contracts as from 1 January 2021 as the first-time application method at that date, opting not to restate comparative information for 2020.

In addition, the Company decided to apply the practical solution of not considering the financing component to be material when the payment period is less than one year, and recognising the incremental costs of obtaining contracts as an expense when their expected period of allocation to profit and loss is one year or less.

The impacts derived from the initial application of the standard are as follows:

a. The internal revenue recognition policies for the different types of contracts with customers were analysed, identifying the performance obligations, the determination of a schedule for meeting these obligations, transaction price and allocation thereof, in order to identify possible differences with respect to the revenue recognition model under the new standard. No significant differences between them, or performance obligations that could lead to the recognition of liabilities due to contracts with customers, were detected.

b. The standard requires the recognition of an accrual for the expense associated with the incremental costs of obtaining a contract with a customer. Based on the evaluations carried out at the date of entry into force of the new standard, no such expenses have been detected in the Company.

The consolidated annual accounts of Naturgy for 2021 have been prepared in accordance with the International Financial Reporting Standards adopted by the European Union (IFRS-EU), in accordance with Regulation (EU) 1606/2002 of the European Parliament and of the Council. The main figures disclosed in the consolidated annual accounts, which have been audited, are as follows:

Total assets	38,249
Equity attributed to the parent company	5,889
Non-controlling interests	2,984
Revenue	22,140
Profit after tax attributed to the parent company	1,214

Note 3. Accounting policies

The main accounting principles applied by the Company to prepare these annual accounts are described below.

3.1 Intangible assets

Intangible assets are carried at acquisition price or production cost, or at fair value in the case of assets acquired through a business combination, less accumulated amortisation and any recognised impairment losses.

a. Goodwill

Goodwill represents the excess of the cost of the acquisition over the fair value of the net identifiable assets acquired at the date of the operation. Consequently, goodwill is only recognised when it has been acquired for valuable consideration and relates to the future economic profits from assets that have not been identified individually and recognised separately.

Goodwill is amortised over ten years using the straight-line method. Goodwill is tested annually to analyse possible impairment losses. It is recognised in the balance sheet at cost value less amortisation and any cumulative impairment adjustments.

The impairment of goodwill cannot be reversed.

b. Computer software

Costs associated directly with the production of computer software programs that are likely to generate economic benefits greater than the costs related to their production are recognised as intangible assets. The direct costs include the personnel costs of the employees involved in developing the programs.

Computer software development costs recognised as assets are amortised on a straight–line basis over a period of five years as from the time the assets are ready to be brought into use.

c. Other intangible assets

Research expenditure is recognised in the income statement when incurred.

The Company has no intangible assets with an indefinite useful life.

3.2. Property, plant and equipment

Property, plant and equipment are carried at cost less accumulated depreciation and any impairment provision.

a. Cost

Property, plant and equipment are carried at acquisition price or production cost, or at the value attributed to the asset if it is acquired as part of a business combination.

Financial costs relating to financing for plant projects during the plant construction period to the date the asset is ready for use form part of property, plant and equipment.

Renewal, extension or improvement costs are capitalised as an increase in the asset's value only when its capacity, productivity or useful life increases.

Own work capitalised under Property, plant and equipment relates to the direct cost of production.

Expenses arising from actions designed to protect and improve the environment are expensed in the year they are incurred.

When such costs entail additions to property, plant and equipment the purpose of which is to minimise the environmental impact and to protect and improve the environment, they are accounted for as an increase in the value of property, plant and equipment.

Gains and losses on disposals are determined by comparing proceeds with carrying amounts. These are included in the Income statement.

b. Depreciation

Assets are depreciated on a straight-line basis over their useful lives or the concession term, if shorter. Estimated useful lives are as follows:

	Estimated useful life years
Buildings	33 – 50
Computer hardware	4
Vehicles	6
Other	3 – 20

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at each balance sheet date.

When the carrying value of an asset is greater than its estimated recoverable amount or when it is no longer useful, its value is written down immediately to its recoverable amount (Note 3.3).

3.3 Asset impairment

Assets are tested for impairment provided that an event or change in circumstances indicates that their carrying amount might not be recoverable. Additionally, investments in group companies, goodwill and intangible assets that are not in use are tested annually for impairment.

When the recoverable amount is less than the asset's carrying amount, an impairment loss is recognised in the income statement for the amount of the difference between the two. The recoverable amount is calculated at the higher of an asset's fair value less costs of sale and value in use calculated by applying the discounted cash flow method. The Company considers value in use as the recoverable amount, calculated as described below.

For the purposes of assessing impairment losses, assets are grouped together at the lowest level for which there are separately identifiable cash flows. Assets and goodwill are assigned to these cash-generating units (CGUs).

For investments in group companies and associates, barring investments the recoverable amount of which is determined based on the investee's equity (Note 3.4), which have required an analysis of potential impairment losses, the cash flows employed are based on the best prospective information available for the next five years, on the basis of regulations and expected market evolution, drawing on available industry forecasts and historical experience of price trends and volumes produced.

The extension in five years of the projections of cash flows or in the period of remaining useful life of the assets and concessions is motivated because in many cases long-term energy sales contracts have been signed, estimated price curves are available that are used in the group's normal operations (for contracts, hedges, etc.), the electricity and gas trading business is influenced by long-term government policies and supported by stable relationships with customers, there are long regulatory periods and in the case of electricity and gas transportation and distribution concessions, because the mechanism for calculating the new rate that the corresponding regulator will use at the beginning of the new regulatory period is foreseen.

Naturgy considers that its projections are reliable and that it can reliably predict the additional cash flows for the initial five-year period.

The cash flows after the ten-year projected period are extrapolated using the growth rates estimated for each CGU, and in no case exceed the average long-term growth rate for the business in which they operate. In all cases, they are lower than the growth rates stated in the available prospective information. Additionally, in order to estimate future cash flows in the calculation of residual values, all maintenance investments have been considered and, if applicable, renewal investments necessary to maintain the CGUs' production capacity.

The parameters taken into account to determine the growth rates, which represent the long-term growth of each line of business, are in line with the long-term growth of the country, obtained from inflation estimates from various sources: analyst consensus (Bloomberg), International Monetary Fund (IMF), OECD, Central Banks and other government agencies, European Commission for the period 2021-2025 and from 2026 onwards the Economist Intelligence Unit (EIU).

The parameters taken into account for the composition of the discount rates before taxes are as follows:

- Risk-free rate: Based on the sovereign bond market and CGU benchmark term as well as studies or other sources of information (Damodaran, EIU and others).
- Market risk premium: Premium based on studies and other sources of information (IESE Business School: Pablo Fernández, Damodaran and others).
- Deleveraged Beta: Based on estimated betas for each CGU based on comparables (Bloomberg).
- Local current interest rate swaps: Swap between 10 years and 30 years, depending on the CGU's business (Bloomberg).
- Debt-equity ratio: Based on industry comparables.

The impairment loss of an asset, individually considered, is recognised in the income statement, reducing the carrying value of the asset to its recoverable amount. The depreciation charges for the asset are adjusted in future periods in order to apportion the revised carrying amount of the asset, less its residual value, in a systematic manner over its remaining useful life.

An impairment loss is recognised for an asset if its recoverable amount is less than the carrying amount. The carrying amount of an asset is not reduced below the higher of its recoverable value and zero.

Impairment adjustments to values recognised in previous periods for investments in Group companies and associates may be reversed if and only if there is a change in the estimates used to determine their recoverable amount since the latest impairment loss was recognised.

3.4 Financial assets and liabilities

Financial assets

The Company classifies its financial assets based on their valuation category, which is determined on the basis of the business model and the characteristics of the contractual cash flows, and it reclassifies financial assets if and only if it changes its business model for managing those assets.

Purchases and sales of investments are recognised on the trade date, which is the date on which the Company undertakes to purchase or sell the asset, classifying the acquisition under the following categories:

a. Financial assets at cost

This category includes investments in the equity of group companies and associates, as well as investments in equity instruments whose fair value cannot be determined by reference to a quoted price in an active market for an identical instrument or cannot be estimated reliably.

They are carried at the lower of acquisition cost, which is equivalent to the fair value of the consideration provided plus directly-attributable transaction costs, or fair value in the case of investments acquired through business combinations, and recoverable value. The recoverable value is determined as the higher of fair value minus selling costs and the present value of the cash flows generated by the investment. If there is no better evidence of recoverable value, it is taken to be the equity of the investee company adjusted by any unrealised capital gains subsisting at the valuation date. The value adjustment and, where appropriate, its reversal, is recognised in the income statement in the year in which it takes place.

b. Financial assets at amortised cost

These are non-derivative financial assets held to collect contractual cash flows when such cash flows represent only payments of principal and interest. They include current assets, except for those maturing after twelve months as from the balance sheet date, which are classified as non-current assets.

They are initially recorded at fair value and subsequently at amortised cost using the effective interest rate method. Interest revenues on these financial assets are recognised as financial revenues, any gain or loss arising on their derecognition is recognised directly in profit or loss, and impairment losses are presented as a separate item in the income statement.

c. Fair value financial assets through profit or loss

These are assets acquired for short-term sale. Derivatives form part of this category unless they are designated as hedges. These financial assets are stated, both initially and in later valuations, at their fair value, and the changes in their value are taken to the income statement for the year.

Equity instruments in this category are recognised at fair value, and fair value changes or the proceeds from their sale are recognised in profit or loss.

The fair values of listed investments are based on current listed prices (Level 1). In the case of shareholdings in unlisted companies, fair value is determined using valuation techniques that include the use of recent transactions between willing and knowledgeable parties, references to other instruments that are substantially the same, and the analysis of discounted future cash flows (Level 2 and 3). If none of these techniques can be used to determine fair value, investments are carried at cost less any impairment loss.

d. Equity instruments at fair value through equity

These are equity instruments for which the company has made an irrevocable choice at the time of initial recognition to account for them in this category. They are recognised at fair value, and fair value changes are recognised in equity. Nevertheless, impairment losses and the dividends from such investments are recognised in profit or loss. At the time of sale, gains or losses are reclassified to profit or loss.

The fair value measurements made in these half-yearly financial statements are classified using a fair value hierarchy that reflects the materiality of the inputs used to perform these measurements. This hierarchy consists of three levels:

- Level 1: Valuations based on the quoted price of identical instruments in an active market. Fair value is based on quoted market prices at the balance sheet date.

- Level 2: Valuations based on variables that are observable for the asset or liability. The fair value of financial assets in this category is determined by using valuation techniques. The valuation techniques maximise the use of available observable market data and place as little reliance as possible on specific estimates made by the company. If all significant inputs required to calculate fair value are observable, the instrument is classified as Level 2. If one or more of the significant inputs are not based on observable market data, the instrument is classified as Level 3.

- Level 3: Valuations based on variables that are not based on observable market data.

Financial assets are written off when the contractual rights to the asset's cash flows have expired or they have been transferred; in the latter case, the risks and rewards of ownership must have been substantially transferred. Financial assets are not written off, and a liability is recognised in the same amount as the payment received, in asset assignments where the risks and rewards of ownership are retained.

Contracts for the assignment of receivables are classified as non-recourse factoring provided that they entail a transfer of the risks and rewards inherent in ownership of the transferred financial assets.

Impairment of financial assets is based on their recoverable value. The company recognises impairment of financial assets at each reporting date.

Financial liabilities

a. Financial liabilities measured at amortised cost

Borrowings are initially recognised at fair value, net of any transaction costs incurred. Any difference between the amount received and the repayment value is recognised in profit or loss over the debt repayment period using the effective interest rate method, and the financial liabilities are classified as being measured subsequently at amortised cost.

In the event of contractual modifications to a liability at amortised cost that do not result in derecognition, any transaction costs or fees incurred are adjusted in the carrying amount of the financial liability. Thereafter, the amortised cost of the financial liability is determined by applying the effective interest rate that matches the carrying amount of the financial liability with the cash flows payable under the new terms.

The difference between the carrying amount of a derecognised financial liability and the consideration paid is recognised in profit or loss.

Borrowings are classified as current liabilities unless they mature in more than twelve months as from the balance sheet date, or include tacit renewal clauses at the Company's election.

Additionally, trade and other current payables are financial liabilities that fall due in less than twelve months, are recognised initially at fair value and do not accrue explicit interest are recognised at their nominal value. Those maturing in more than twelve months are considered non-current payables.

b. Financial liabilities at fair value through profit or loss

These are liabilities acquired for short-term sale. Derivatives form part of this category unless they are designated as hedges. These financial liabilities are stated, both initially and in subsequent remeasurements, at fair value, and fair value changes are recognised in profit or loss.

3.5 Financial derivatives and other financial instruments

Derivatives are initially recognised at fair value on the date a derivative contract is entered into and are subsequently remeasured at their fair value. The method of recognising the resulting gain or loss depends on whether the derivative is designated as a hedging instrument, and if so, the nature of the asset being hedged.

The Company aligns its accounting with its management of financial risk. Risk management objectives and the hedging strategy are reviewed periodically and a description of the risk management objective pursued is carried out.

In order for each hedging operation to be considered effective, the Company documents that the economic relationship between the hedging instrument and the hedged asset is aligned with its risk management objectives.

The market value of the various financial instruments is calculated using the following procedures:

- Derivatives listed on an official market are calculated on the basis of their year-end quoted price (Level 1).
- Derivatives that are not traded on official markets are calculated on the basis of the discounting of cash flows based on year-end market conditions or, in the case of non-financial items, on the best estimate of forward price curves for those items (Level 2 and 3).

The fair values are adjusted for the expected impact of observable counterparty credit risk in positive valuation scenarios and the impact of observable credit risk in negative valuation scenarios.

Derivatives embedded in other financial instruments or in other host contracts are recorded separately as derivatives only when their financial characteristics and inherent risks are not strictly related to the instruments in which they are embedded and the whole item is not being carried at fair value through profit or loss.

For accounting purposes, the operations are classified as follows:

1. Derivatives eligible for hedge accounting

a. Fair value hedge

Changes in the fair value of derivatives that are designated and qualified as fair value hedges are recognised in the income statement together with any changes in the fair value of the hedged asset or liability that are attributable to the hedged risk.

b. Cash flow hedge

The effective portion of changes in the fair value of derivatives that are designated and qualify as cash flow hedges are recognised in equity. The gain or loss relating to the ineffective portion is recognised immediately in the Income statement.

When options contracts are used to hedge forecast transactions, the Group only designates the intrinsic value of the options contract as the hedging instrument.

Amounts accumulated in equity are transferred to the income statement in the period in which the hedged item affects the gain or loss, as follows:

- The gain or loss relating to the effective portion of interest rate swaps is recognised in the financial expense at the same time as the interest expense in the hedged loans.
- When a hedging instrument covers a forecast transaction, the accumulated amounts remain in equity until the forecast transaction takes place. When the forecast transaction does not occur, the amount accumulated in equity is immediately reclassified to income for the period.

However, if this amount is a loss, and for an amount that is not expected to be recovered, it will be immediately reclassified in the income statement as a reclassification adjustment.

If the hedged item subsequently results in the recognition of an asset, the amount accumulated in equity will be recognised in the initial cost of the asset.

c. Hedges of net foreign investments

The accounting treatment is similar to cash flow hedges. The variations in value of the effective part of the hedging instrument are carried in the Balance sheet under “Value change adjustments”. The gain or loss from the non-effective part is recognised immediately under “Exchange differences” in the income statement. The accumulated amount of the valuation recorded under “Value change adjustments” is released to the income statement as the foreign investment that gave rise to it is sold.

2. Derivatives that do not qualify for hedge accounting

Certain derivative instruments do not qualify for hedge accounting. Changes in the fair value of any derivative instruments that do not qualify for hedge accounting are recognised immediately in the income statement.

Additionally, commodity derivatives not classified as hedges for accounting purposes are recognised inside the operating profit since they essentially constitute an economic hedge because the critical terms of the derivative coincide with those of its hedged item.

3. Energy purchase and sale agreements

In the normal course of its business the Company enters into energy purchase and sale agreements which in most cases include “take or pay” clauses. by virtue of which the buyer takes on the obligation to pay the value of the energy contracted irrespective of whether the buyer receives it or not. These agreements are executed and maintained in order to meet the needs of receipt or physical delivery of energy expected by the Company in accordance with regular energy purchase and sale estimates, which are monitored systematically and adjusted in all cases through physical delivery. Consequently, these are contracts for “own use” and therefore fall outside the scope of the standard on the valuation of financial instruments.

3.6 Non-current assets held for sale and discontinued operations

The Company classifies as held-for-sale assets those assets for which, at the year end, active measures have been initiated for their sale, which is estimated to take place within the next twelve months.

Additionally, the Company considers discontinued activities the components that make up a business line or geographic area of operations, which are significant and which can be considered separately from the rest, and which have been sold or disposed by other means or which meet the conditions to be classified as held-for-sale. Entities acquired solely for resale are also classed as discontinued operations.

These assets are stated at the lower of their carrying value and fair value minus the costs necessary for their sale and are not subject to depreciation from the date on which they are classified as non-current assets held for sale.

In the event of delays caused by events or circumstances beyond Naturgy's control and if there is sufficient evidence that the commitment to the plan to sell those classified as held for sale is maintained, the classification is maintained even though the period to complete the sale is extended beyond one year.

3.7 Share capital

Share capital is represented by ordinary shares.

Issuance costs of new shares or options, net of taxes, are deducted from equity as a reduction in reserves or the share premium account in the case of issuances with a share premium.

Dividends on ordinary shares are recognised as a deduction from equity in the period they are approved.

Acquisitions of treasury shares are recorded at acquisition cost, deducted from equity until disposal. The gains and losses on disposals of treasury shares are recognised under "Reserves" in the balance sheet.

3.8 Share-based payments

Share-based payments settled in shares are valued on the basis of the fair value of the equity instruments granted on the grant date. In addition, the effects of changes that increase the fair value of share-based payment arrangements will be recognised.

The resulting cost is recognised under Personnel expenses in the income statement as the services are rendered by the employees during relevant vesting period, with a balancing entry in Other equity instruments in the balance sheet.

The amounts recognised in equity are not subject to a subsequent reassessment due to trends in external market conditions.

3.9 Borrowings and equity instruments

Borrowings and equity instruments issued by the Company are classified based on the nature of the issue.

The Company treats all contracts that represent a residual share in net assets as equity instruments.

Equity instrument issuance costs are presented as a deduction in equity.

3.10 Provisions for employee obligations

a. Post-employment pension obligations and similar

-Defined contribution plans

The Company, together with other Naturgy companies, is the promoter of a joint occupational pension plan, which is a defined contribution plan for retirement and a defined benefit plan for the so-called risk contingencies, which are insured.

Additionally, there is a defined contribution plan for a group of executives, in which the Company undertakes to make certain contributions to an insurance policy, guaranteeing this group a yield of 125% of the CPI of the contributions made to the insurance policy. All the risks have been transferred to the insurance company, since it insures the guarantee indicated above.

The contributions made have been recognised under Personnel expenses in the income statement.

-Defined benefit plans

For certain groups of employees there are commitments for defined benefit schemes in relation to the payment of supplements on retirement, death and disability pensions, in accordance with the benefits agreed by the entity, which have been externalised through single premium insurance policies under Royal Decree 1588/1999 of 15 October, which approved the Regulations on the arrangement of companies' pension commitments.

The liability recognised in the balance sheet in respect of defined benefit pension plans is the present value of the defined benefit obligation at the balance sheet date less the fair value of plan assets, together with adjustments for unrecognised actuarial gains or losses and past service costs. The defined benefit liability is calculated annually by independent actuaries using the projected unit credit method. The current value of the liability is determined discounting the estimated future cash flows at interest rates on bonds denominated in the currency in which the benefits will be paid and having similar maturities to those of the respective liabilities.

Actuarial losses and gains arising from changes in actuarial assumptions or from differences between assumptions and the actual situation are recognised in full in the period in which they arise, directly under Equity in Reserves.

Past service costs are recognised immediately in the Income statement under Personnel expenses.

b. Other post-employment benefit obligations

The Company provides post-employment benefits to its retirees. The entitlement to these benefits is usually conditional on the employee remaining in service up to retirement age and the completion of a minimum service period. The expected costs of these benefits are accrued over the period of employment using an accounting methodology similar to that used for defined benefit pension plans. Actuarial gains and losses arising from changes in actuarial assumptions, are charged or credited to Reserves.

c. Termination benefits

Termination benefits are payable when employment is terminated before the normal retirement date, or when an employee accepts voluntary redundancy in exchange for these benefits. The Company terminates the employment of current employees according to a detailed formal plan without possibility of withdrawal; or providing termination benefits. In the event that mutual agreement is required, the provision is only recorded in those situations in which the Company has decided to give its consent to voluntary redundancies once they have been requested by the employees.

3.11 Provisions

Provisions are recognised when the Company has a legal or implicit present obligation as a result of past events; it is more likely than not that an outflow of resources will be required to settle the obligation; and the amount has been reliably estimated. Provisions are not recognised for future operating losses.

Provisions are measured at the best estimate of the present value of the amount required to settle the obligation at the balance sheet date.

When it is expected that part of the disbursement needed to settle the provision will be paid by a third party, the payment is recognised as a separate asset, provided that its receipt is practically assured.

In contracts in which the obligations undertaken include unavoidable costs greater than the economic benefits expected to be received from them, the expenses and respective provisions are recognised in the amount of the current value of the existing difference. The unavoidable costs of the contract will reflect the lower net costs of terminating the contract, i.e. the lower of the cost of complying with the terms of the contract and the compensation derived from non-compliance.

3.12 Leases

a. Finance leases

Leases of property, plant and equipment where the lessee substantially bears all the risks and rewards of ownership are classified as finance leases.

These leases are capitalised at the lease's inception at the lower of the fair value of the leased property and the present value of the lease payments, including the purchase option. Each lease payment is allocated between the liability and finance charges so as to achieve a constant rate on the finance balance outstanding. The payment obligation derived from the lease, net of the finance cost, is recognised under liabilities in the balance sheet. The interest component of the finance cost is charged to the income statement over the lease period so as to obtain a constant periodic rate of interest on the remaining balance of the liability for each period. The property, plant and equipment acquired under finance leases are depreciated over the asset's useful life.

b. Operating leases

Leases in which substantially all the risks and rewards of ownership are retained by the lessor are classified as operating leases. Operating lease payments are charged to the income statement on a straight-line basis over the lease term.

3.13 Corporate income tax

Income tax expense includes the deferred tax expense and the current tax expense which is the amount payable (or refundable) on the tax profit for the year.

Deferred taxes are recorded by comparing the temporary differences that arise between the taxable income on assets and liabilities and their respective accounting figures in the annual accounts used the tax rates that are expected to be in force when the assets and liabilities are realised. No deferred taxes are recognised for profits not distributed by subsidiaries when Naturgy can control the reversal of the temporary differences and it is likely that they will not reverse in the foreseeable future.

Deferred tax arising from direct charges or credits to equity accounts are also charged or credited to equity.

Deferred tax assets and tax credits are recognised only to the extent that it is probable that future taxable income will be available against which to offset temporary differences and apply tax credits.

When tax rates change, deferred tax assets and liabilities are reestimated. These amounts are charged or credited to losses or profits, or to reserves, depending on the account to which the original amount was charged or credited.

3.14 Recognition of income and expense

a. General

Revenue derived from contracts with customers is recognised based on compliance with performance obligations with customers.

Revenue reflects the transfer of goods or services to customers at an amount that reflects the consideration to which the Company expects to be entitled in exchange for such goods or services.

Five steps are established for the recognition of revenue:

1. Identify the customer's contract(s).
2. Identify the performance obligations.
3. Determine the price of the transaction.
4. Allocate the transaction price to the performance obligations.
5. Recognise the revenue according to the fulfilment of each obligation.

Based on this recognition model, sales are recognised when products are delivered to the customer and have been accepted by the customer, even if they have not been invoiced, or if applicable, services are rendered, and it is probable that the economic benefits associated with the transaction will flow to the entity.

Expenses are recognised on an accruals basis, immediately in the case of disbursements that are not going to generate future economic profits or when the requirements for recording them as assets are not met.

Sales are stated net of tax and discounts.

b. Other income and expenses

The holding of shares in Group companies and associates is deemed to be the Company's most relevant ordinary activity from which regular revenue is obtained. In accordance with the approach taken by the Spanish Institute of Accounting and Auditing ("ICAC") in connection with the calculation of revenue in holding companies (ruling request number 2 in ICAC Official Gazette number 79), dividends from Group companies and associates, and interest received on loans granted to Group companies and associates, are recognised as “Revenue”. Additionally, the item “Impairment and results on disposal of equity instruments of Group companies and associates” is included in “Operating profit/(loss)”.

Revenue from a contract is recognized as control over the promised goods or services is transferred to the customer.

Revenue derived from the commitments (in general, of provision of services) that are fulfilled over time are recognized based on the degree of progress or progress towards the complete fulfillment of the contractual obligations.

When, at a given date, the stage of fulfilment of the obligation cannot be reasonably measured, revenue and the related consideration are recognised only to the extent of the costs incurred up to that date.

Interest incomes and expenses are recognised using the effective interest method.

Dividend income is recognised when the right to collect the dividend is established. If the dividends are unequivocally derived from reserves generated prior to the acquisition, the value of the investment is adjusted.

3.15 Foreign currency transactions

Foreign currency transactions are translated to euro using the exchange rates in force at the transaction dates. Gains and losses resulting from the settlement of these transactions and translation at the year-end exchange rates of monetary assets and liabilities denominated in foreign currency are recognised in the income statement.

3.16 Transactions between related parties

In general, transactions between related parties are recorded initially at their fair value. If the agreed price differs from its fair value, the difference is recorded taking into account the economic reality of the operation. The later valuation is made in accordance with the provisions of the respective legislation.

Notwithstanding the above, in mergers, de-mergers or non-cash contributions of a business, the assets that make up the acquired business are valued at the amount at which they are recognised after the operation takes place in the consolidated annual accounts of the Company.

In these cases, the difference that could arise between the net value of the assets and liabilities of the acquired company, adjusted by the balance of the groupings of grants, donations and bequests received, or any value adjustments or capital or share premiums, as the case may be, issued by the acquiring company, is recorded under Reserves in the balance sheet.

3.17 Business combinations

Business combinations are recorded using the acquisition method. The cost of an acquisition is calculated using the fair value of the assets given, the equity instruments issued and the liabilities incurred or borne on the transaction date plus the costs directly attributable to the acquisition. The valuation process required in order to use the acquisition method is completed within the period of one year as from the acquisition date.

The identifiable assets acquired and the liabilities or contingent liabilities incurred or borne as a result of the transaction, are initially stated at their fair value at the date of acquisition, provided that this can be reliably measured.

The surplus cost of the acquisition in relation to the fair value of the shareholding of the Company in the net identifiable assets acquired is recorded as goodwill. If the cost of acquisition is less than the fair value of the net assets acquired, the difference is recognised directly in the Income statement.

3.18 Cash flow statement

The cash flow statements has been prepared using the indirect method and contain the use of the following expressions and their respective meanings:

a. Operating activities: activities that constitute ordinary Company revenues, as well as other activities that cannot be qualified as investing or financing.
b. Investing activities: acquisition and disposal of non-current assets and other investments not included in cash and cash equivalents.
c. Financing activities: activities that result in changes in the size and composition of the equity and borrowings of the Company that are not operating activities.

3.19 Significant accounting estimates and judgments

The preparation of annual accounts requires the use of estimates and judgments. The measurement standards that require a large number of estimates are set out below:

a. Property, plant and equipment (Note 3.2)

The determination of useful life of property, plant and equipment requires estimates of their degree of use, as well as expected technological developments. The assumptions regarding the degree of use, technological framework and future development involve a significant degree of judgement, insofar as the timing and nature of future events are difficult to foresee.

b. Impairment of investments in group companies and associates (Note 3.3)

In accordance with applicable accounting regulations, the Company performs impairment tests on investments in group companies and associates that show impairment indicators. These impairment tests require an estimate of future business performance and the most appropriate discount rate in each case. The Company believes that the estimates made are appropriate and consistent with the current market situation.

Note 4 details the main assumptions used to determine the recoverable value of investments in group companies and associates.

c. Derivatives and other financial instruments (Note 3.5)

The fair value of financial instruments traded in active markets is based on quoted market prices at the balance sheet date. The quoted market price used for financial assets is the current bid price.

The fair value of financial instruments that are not traded in an active market is determined by using valuation techniques. The Company uses a variety of methods and makes assumptions that are based on market conditions existing at each balance sheet date. Other techniques, such as estimated discounted cash flows, are used to determine fair value for the remaining financial instruments. The fair value of interest rate swaps is calculated as the present value of the estimated future cash flows. The fair value of forward foreign exchange contracts is determined using quoted forward exchange rates at the Balance sheet date. The fair value of commodity derivatives is calculated by using forward prices curves. The recoverable value of the investments in the equity of group and multi-group companies and associates is determined as the greater of their fair value less costs of sale and the current value of the cash flows from the investment.

The carrying value less impairment provision of trade receivables and payables are assumed to approximate their fair values. The fair value of financial liabilities for disclosure purposes is estimated by discounting the future contractual cash flows at the current market interest rate that is available to the Company for similar financial instruments.

d. Provisions for employee benefits (Note 3.10)

A number of assumptions must be used to calculate pension costs, other costs of post-retirement benefits and other post-retirement liabilities. The Company estimates at each year end the provision necessary to meet its pension commitments and similar obligations, in accordance with the advice from independent actuaries. The changes affecting such assumptions may result in the recording of different amounts and liabilities. The most significant assumptions for the measurement of pension or post-retirement benefit liabilities are energy consumption by beneficiaries during retirement, retirement age, inflation and the discount rate employed. Social security coverage assumptions are also essential to determine other post-retirement benefits. Future changes to these assumptions will have an impact on future pension costs and liabilities.

e. Provisions (Note 3.11)

The Company makes an estimate of the amounts to be settled in the future, including amounts relating to contractual obligations, onerous contracts, outstanding litigation or other liabilities. These estimates are subject to the interpretation of current events and circumstances, projections of future events and estimates of their financial effects, as well as the result of the negotiations associated with the gas supply contracts.

f. Corporate income tax (Note 3.13)

The calculation of the income tax expense requires interpretations of tax legislation in the jurisdictions in which the Company operates. The determination if the tax authority will accept an uncertain tax treatment and the expected outcome of litigation requires the preparation of significant estimates and judgment. The Company evaluates the recoverability of the deferred income tax assets based on estimates of future taxable income. Deferred tax liabilities are recognised based on estimates of the net assets that will not be tax deductible in the future.

g. COVID-19

The COVID-19 pandemic raised major challenges to commercial activities and introduced a high degree of uncertainty as to economic performance and world energy demand.

In 2020, the confinement of a large proportion of the world population depressed economic activity and triggered widespread declines in macroeconomic indicators, energy demand and prices of the main energy variables.

In 2021, the effects of the COVID-19 pandemic increased the uncertainty about the outlook for individual companies and for the economy in general, and there was a supply and demand shock in the international markets for energy commodities that commenced in the third quarter of 2021, consisting of a sharp recovery in demand while supply lagged behind.

The Group monitors the evolution of the economic cycle in the short and long term, as a result of the impact of COVID-19 or other factors, with the objective of minimising the likelihood that further deteriorations or sharp recoveries in the current economic situation in the markets in which it operates might have material adverse effects on the Group's business, prospects, financial position and the results of its operations.

In making the estimates and hypotheses necessary for the preparation of the Annual accounts, these perspectives have been considered, detailing them in the corresponding Notes.

h. Climate change and the Paris Agreement

Naturgy's strategy takes into consideration the objectives of the Paris Agreement to keep the global temperature increase below 2ºC and achieve climate neutrality by 2050, and they have been taken into account in the preparing the annual accounts for 2021.

In this regard, in the context of its preparation, the effect of the commitments assumed by Naturgy has been considered in the estimates of the useful life of the assets, in the costs of closure and decommissioning of electricity facilities and in the analysis of the impairment of financial assets.

As detailed in Note 4, the projections used in the impairment tests of assets were based on the best available prospective information and reflect the investment plans existing in each CGU at that time. These plans are in line with Naturgy's strategy, which takes account of the objectives of the Paris Agreement. Those projections also took into account the expected effect on wholesale and retail electricity market prices of the entry into operation of new renewable generation facilities and the possible evolution of gas, oil and emission rights prices.

Note 4. Asset impairment

Definition of Cash Generating Unit

At 31 December 2021 the Cash Generating Units (CGUs) are renamed and regrouped following the new business structure reorganisation carried out by Naturgy in 2020.

Energy and Network Management:

- Iberian Networks:
  - Gas networks Spain: Is a single CGU as the development, operation and maintenance of the gas distribution network is managed jointly.
  - Electricity networks Spain: This makes up a single CGU since the network comprises a group of interrelated assets the development, operation and maintenance of which is managed jointly.
- Latin American Networks: A CGU is understood to exist for each business and country in which there are operations since the businesses are subject to different regulatory frameworks. Includes the regulated gas distribution business in Argentina, Brazil, Chile, Mexico and Peru (until the resolution agreement with the Peruvian government in December 2020) and the regulated electricity distribution business in Argentina, Panama and Chile (until July 2021).
- Energy Management:
  - International LNG: There is considered to be a single CGU, since the supply of liquefied natural gas and the maritime transport activity are managed on a global level.
  - Markets and supplies: A CGU is considered to exist since it manages supply and other gas infrastructures, as well as sales to major energy-intensive consumers. It also includes Unión Fenosa Gas following the transaction described in Note 7.
  - Gas pipelines: It includes the CGU which manages the Maghreb-Europe gas pipeline, as well as the CGU for the Medgaz gas pipeline.
  - Thermal generation Spain: A single CGU is considered to exist for thermal power generation in Spain (nuclear and combined cycle).
  - Thermal generation Latin America: A thermal power generation CGU is understood to exist in each country in which there are operations (Mexico, Dominican Republic and Puerto Rico) since the businesses are subject to different regulatory frameworks and are managed independently.

Renewables and New Business:

- Spain: One CGU is considered for renewable electricity generation (wind, mini-hydro, solar and cogeneration) and another CGU for hydroelectric power generation.
- USA: One CGU is considered which encompasses all projects in the country.

- Latin American: A renewable power generation CGU is understood to exist in each country in which there are operations (Brazil, Costa Rica, Mexico, Panama and Chile) since the businesses are subject to different regulatory frameworks and are managed independently.

- Australia: One CGU is considered which encompasses all projects in the country.

Supply:

The commercial management of natural gas, electricity and services is carried out on a comprehensive basis, maximising the value of the portfolio through a customer-based approach and with high potential for growth in services and solutions, for which there is a single CGU.

The grouping of assets considered in the previous CGUs has not changed since the previous estimation of their recoverable value.

Information on impairment tests performed

Naturgy has evaluated the recoverable value of investments in group companies and associates based on the Strategic Plan 2021-2025 presented on 28 July 2021, taking into account the investment plans that maintain the productive capacity of the businesses involved and the market conditions in which they operate. As indicated in Note 3.3, this period has been extended by an additional five years or by the remaining useful life for certain assets and concessions. Various potential future scenarios have also been considered when estimating cash flows, if they provide more relevant information to reflect possible future economic developments.

In general, and in accordance with the new Plan 21-25, the flows reflect Naturgy's new positioning to drive the energy transition and decarbonisation with a focus on digital transformation, with increasing investments in networks and renewables located in stable geographies and regulatory frameworks.

Cash flows have taken into account short-term volatility in international gas markets and transitory high electricity prices. In particular, the regulatory measures approved in Spain for generation, distribution and supply have been estimated, together with the commercial proposals for avoiding high pool prices.

Likewise, although in 2021 the effects of the pandemic continued to generate strong uncertainty in the economy in general and the final scope and the moment in which the definitive recovery from the COVID-19 health crisis will take place is still unknown, the estimated cash flows contemplate, in general terms, a recovery path to pre-pandemic levels and a limitation of its effect on energy demand.

Information on recognised impairments (Note 7)

In 2021 an income has been recognised due to the reversal of impairments of shareholdings in Group companies and associates amounting to Euros 869 million (increase in impairment of Euros 1,088 million in 2020) under the heading “Impairment of and losses from equity instruments of Group companies and associates” in the income statement, detailed below:

- Impairment reversal of Euros 154 million (impairment of Euros 1,005 million in 2020) for the holding in Naturgy Generación, S.L.U., which includes the Spanish hydroelectric power generation CGU following the spin-off detailed in Note 7. In 2020, the CGUs for Hydraulic Generation and Thermal Generation were included in this company.

The assumptions and projections affecting the Hydroelectric power generation CGUs are based on the best forward-looking information available to date.

The assumptions taken into consideration are the following:

	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030
Evolution of Spanish GNP	**4.80%**	5.70%	3.60%	2.30%	2.10%	1.80%	1.30%	0.90%	0.60%	0.40%
Pool price €/MWh	**111.4**	152.2	80.9	75.7	69.5	58.1	56.3	57.0	59.6	60.7

The most sensitive aspects that are included in the estimate of the recoverable amount determined according to the value in use and applying the methodology detailed in Note 3.3 are the following:

Electricity generated. For the Hydroelectric power generation CGU, production has been estimated considering an average hydraulic year and in addition compensation has been considered through a mechanism that remunerates the firm capacity contributed that is expected to be implemented to make the NECP forecasts viable.

Electricity price. Market electricity prices used have been calculated using models that cross expected demand with supply forecasts, taking into account the foreseeable evolution of generation capacity in Spain, based on sector forecasts, the evolution of the energy scenario on the basis of the futures curves and analysts' forecasts.

The projected flows take into account the most relevant extraordinary regulatory changes derived from the increase in electricity prices in 2021 on the wholesale market:

- The allocation of energy produced by the hydraulic installations to the new long-term energy purchase auctions, aimed at industrial customers and independent marketers.
- The estimated impact of the reduction in the remuneration of non-emitting installations, for an amount proportional to the value of the gas price quote, as well as the project for the reduction in remuneration for CO_2 not emitted from the electricity market.
- The measures envisaged to regulate water impounded for hydroelectric use.

Operation and maintenance costs. These have been estimated from historical costs of the managed park.

Taxes established by Law 15/2012 and extraordinary temporary suspensions.

Investments: those required to maintain the regular use of the facilities have been taken into account.

In addition, a long-term growth rate of 2% and a pre-tax discount rate of 6% have been used. The discount rate has been determined based on the associated risks in a manner consistent with those considered in the estimates of future cash flows.

In 2020, the long-term growth rate was 2.1% and the pre-tax discount rate was 6.2% for the Hydroelectric power generation CGU.

The accumulated impairment at 31 December 2021 relating to the holding in Naturgy Generation, S.L.U. following the demerger mentioned in Note 7 amounts to Euros 2,186 million (Euros 4,678 million at 31 December 2020).

- An impairment reversal of Euros 784 million (an impairment of Euros 47 million in 2020) relating to the 100% shareholding in Unión Fenosa Gas (UFG).

In March 2021, Naturgy, ENI and the Arab Republic of Egypt completed the agreement reached on 1 December 2020 to amicably resolve the disputes affecting UFG. As a result, UFG received a number of cash payments for the sale of the assets in Egypt, UFG's business activities in Spain and one of its vessels, as well as the receipt of compensation agreed with the Egyptian government. Simultaneously, Naturgy completed the acquisition of the remaining 50% holding in UFG for Euros 466 million, bringing Naturgy's holding to 100% and enabling it to obtain control. This also entailed the termination of the annual gas supply contract of around 3.5 bcm for supplying combined cycle plants in Spain that was due to end in 2029, while maintaining the contract with Oman which expires in 2025.

As a result of the acquisition of the additional 50% holding, Euros 108 million have been reversed for the valuation of the previous 50% holding in Unión Fenosa Gas.

From the valuation of the expected flows corresponding to the gas supply contract with Oman that expires in 2025 and the estimate of the dividends for its 7.36% holding in the company Qalhat LNG S.A.O.C., an additional Euros 676 million have been reversed.

In addition, a pre-tax discount rate of 12.2% was used. The discount rate has been determined based on the associated risks in a manner consistent with those considered in the estimates of future cash flows.

The accumulated impairment at 31 December 2021 relating to the 100% interest in Unión Fenosa Gas amounts to Euros 1,395 million (Euros 2,179 million at 31 December 2020 for a 50% interest). At 31 December 2021, the recoverable amount calculated as the value in use of UFG, which is equivalent to its carrying value, was Euros 1,294 million (Euros 262 million at 31 December 2020) (Note 7).

In addition, the following impairments have been recognised based on the companies' equity:

- Euros 49 million relating to the holding in Naturgy LNG, S.L. (Euros 9 million in 2020), due to the company's unfavourable performance.

The accumulated impairment at 31 December 2021 relating to the holding in Naturgy LNG, S.L. amounts to Euros 59 million (Euros 10 million in 2020).

- Euros 9 million relating to the holding in Naturgy Informática, S.A. (Euros 9 million in 2020).

The accumulated impairment at 31 December 2021 relating to the holding in Naturgy Informática, S.A. amounts to Euros 155 million (Euros 146 million at 31 December 2020).

- Euros 8 million relating to the shareholding in Naturgy Engineering, S.L. (Euros 4 million in 2020).

The accumulated impairment at 31 December 2021 relating to the holding in Naturgy Engineering, S.L. amounts to Euros 12 million (Euros 4 million in 2020).

- Euros 8 million for the shareholding in Naturgy Nuevas Energías, S.L.U. The accumulated impairment at 31 December 2021 is Euros 2 million. A provision for future liabilities amounting to Euros 6 million has been included under "Other long-term provisions".

- Euros 7 million for the holding in Naturgy Almacenamientos Andalucía, S.A. Accumulated impairment at 31 December 2021 amounts to Euros 8 million (Euros 3 million at 31 December 2020). A provision for future liabilities amounting to Euros 2 million has been included under "Other long-term provisions".

- Euros 1 million in 2021 for the impairment of the 32.3% holding in Petroleum Oil & Gas España, S.A.(Euros 3 million at 31 December 2020).

The accumulated impairment at 31 December 2021 relating to the holding in Petroleum Oil & Gas España, S.A. amounts to Euros 74 million (Euros 73 million in 2020).

- Impairment reversal of Euros 13 million relating to Naturgy Participaciones, S.A.U. Accumulated impairment at 31 December 2021 amounts to Euros 8 million (Euros 21 million in 2020).

- Impairment of Euros 1 million of the holding in Gas Natural Exploración, S.L. (Euros 0 million at 31 December 2020).

The accumulated impairment at 31 December 2021 relating to the holding in Gas Natural Exploración, S.L. amounts to Euros 214 million (Euros 213 million in 2020).

- Other reversals of impairment in holdings in Naturgy companies amounting to Euros 1 million (Euros 16 million in 2020).

Information on other impairment tests performed:

As regards the remaining CGUs or groups of CGUs that have been allocated goodwill or intangible assets with an indefinite useful life or evidence of impairment, in 2021 and 2020 the recoverable amounts, calculated according to the methodology described in Note 3.3, have been higher than the carrying values of holdings in Group companies recorded in these annual accounts. The most sensitive aspects included in the projections used are as follows:

<u>Gas and Electricity Networks Spain:</u>

- Remuneration. Amount and growth of remuneration. In relation to the regulatory framework, the future cash flows of these business lines have been reviewed taking into account the publications by the regulator in 2020 and 2021 on the remuneration methodology for the regulated electricity and gas distribution activity from 2021, respectively.

- Operation and maintenance costs. Estimated on the basis of the historical cost of the network managed.

- Investments. Considering the investments required to maintain the regular use of the network and the quality of supply, as well as the digitalisation of electricity networks and the estimated investment in line with sector requirements and the digital transition in the operation of gas networks.

- In addition, long-term growth rate of 0.5% - 2.0% (0.5% - 1.9% in 2020) and pre-tax discount rate of 4.7% - 5.4% (5.2% - 5.9% in 2020) have been used.

<u>Latin American networks:</u>

For gas networks CGUs in Brazil, Chile, Argentina and México and electricity networks CGUs in Argentina and Panama:

- Variations in rates. Valuation of rates in each country, based on existing regulatory conditions and rate reviews, taking into account the experience gained from previous rate reviews in each country.

- Cost of raw materials and consumables. Estimated on the basis of predictive modelling based on an understanding of energy markets in each country.

- Operation and maintenance costs. Estimated on the basis of the historical cost of the network managed.
- Investments. Taking into account the necessary investments to maintain the regular use of the network and supply quality and safety.
- In addition, long-term growth rate of 2% - 8.8% (2.5% - 11.4% in 2020) and pre-tax discount rate of 7.7% - 18.1% (7.9% - 15.8% in 2020, after homogenization) have been used.

Thermal generation Spain:

The assumptions and projections affecting this CGU have been based on the best forward-looking information available to date, generally considering the possible effects on generation of the transition expected due to the increase in renewable energy sources set out in the rules on the first NECP in the Climate Change and Energy Transition Bill. The above projections consider a production path considering the prospects of the NECP, which contemplate the need for all the installed power of combined cycle generation units in the projection horizon (2030).

The assumptions taken into consideration are the following:

	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030
Evolution of Spanish GNP	**4.8%**	5.7%	3.6%	2.3%	2.1%	1.8%	1.3%	0.9%	0.6%	0.4%
Pool price €/MWh	**111.4**	152.2	80.9	75.7	69.5	58.1	56.3	57.0	59.6	60.7
Brent (USD/bbl)	**70.7**	66.7	71.6	67.3	64.6	63.7	65.1	66.6	68.3	70.1
Gas Henry Hub (USD/MMBtu)	**3.8**	3.9	3.5	3.2	3.0	3.3	3.4	3.6	3.9	4.1
Coal (API2 CIF ARA) (USD/t)	**119.9**	110.4	85.8	80.6	80.5	79.0	81.2	83.5	85.9	88.3
CO2 €/t	**53.2**	77.1	60.2	61.0	62.0	67.6	71.7	75.8	80.1	84.6

The most sensitive aspects that are included in the estimate of the recoverable amount determined according to the value in use and applying the methodology detailed in Note 3.3 are the following:

Electricity generated. Demand evolution has been estimated based on projections from the CNMC and analysts. The market share has been estimated based on Naturgy's market share in each technology and the expected evolution of the share of each technology in the total market, in line with the expected future evolution of the generation mix, maintaining the expected decrease in thermal production offset by a mechanism that rewards the firm capacity provided, which is expected to be established to make the PNIEC forecasts viable.

Electricity price. Market electricity prices used have been calculated using models that cross expected demand with supply forecasts, taking into account the foreseeable evolution of generation capacity in Spain, based on sector forecasts, the development of the energy scenario on the basis of futures curves, and analysts' forecasts.

The projected flows take into account the most relevant extraordinary regulatory changes derived from the increase in electricity prices on the wholesale market:

- The allocation of energy produced by the hydraulic installations to the new long-term energy purchase auctions, aimed at industrial customers and independent marketers.
- The estimated impact of the reduction in the remuneration of non-emitting installations, for an amount proportional to the value of the gas price quote, as well as the project for the reduction in remuneration for CO_2 not emitted from the electricity market.

Fuel costs. Estimated on the basis of market prices. Operation and maintenance costs. Estimated from historical costs of the managed park.

Taxes established by Law 15/2012 and extraordinary temporary suspensions.

In addition, a long-term growth rate of 2% and a pre-tax discount rate of 7.1% (growth rate of 2.1% and pre-tax discount rate of 7.4% in 2020) have been used.

Thermal generation Latin American:

For thermal electricty generation CGUs in México, Dominican Republic and Puerto Rico:

- Thermal generation in Mexico is carried out over most of its useful life under energy sale-purchase contracts through stable business models and which are not subject to fluctuation risks on the basis of market variables. In the Dominican Republic and Mexico, upon termination of the contracts energy prices are set based on the market and are estimated on the basis of developments in the country's energy scenario, including the foreseeable evolution of the generation pool and taking into account expected supply and demand, and production costs.

- The main estimates considered in the flows generated by the Puerto Rico thermal genertion CGU relate to the contract with Puerto Rico Electric Power Authority (PREPA), which will remain in force until the end of 2032.

- Operation and maintenance costs have been estimated from historical costs of managed park.

- In addition, long-term growth rate of 2% (1.8% in 2020) and pre-tax discount rate of 9% - 12.5% (9% - 13.2% in 2020) have been used.

<u>Renewables Spain:</u>

The assumptions and projections affecting the Renewable generation CGU (wind, mini-hydro, solar and cogeneration) are based on the best forward-looking information available to date.

The assumptions concerning changes in GDP and the Pool price coincide with those considered in the Thermal Generation Spain CGU.

The most sensitive matters included in the impairment test are as follows:

- Electricity generated. Projections of hours of operation of each park consistent with their historical output and predictions based on historical records of similar parks have been used when there were no historical data.

- Electricity price. Market electricity prices used have been calculated using models that cross expected demand with supply forecasts, taking into account the foreseeable evolution of generation capacity in Spain, based on sector forecasts, the evolution of the energy scenario on the basis of the futures curves and analysts' forecasts.

- Remuneration. For the renewable generation CGU facilities entitled to specific remuneration, the remuneration has been estimated on the basis of the remuneration parameters for the established regulated income period.

- Operation and maintenance costs have been estimated from historical costs of managed park.

- Taxes established by Law 15/2012 and extraordinary temporary reductions.

- In addition, long-term growth rate of 2% (2.1% in 2020) and pre-tax discount rate of 5.4% (5.7% in 2020) have been used.

<u>Renewables USA:</u>

As the acquisition was made in 2021, the main assumptions used in the business plan considered in the acquisition of the portfolio of 8 GW of solar projects together with 4.6 GW of energy storage projects are considered unchanged.

<u>Renewables Latin America:</u>

Includes the Brazil, Costa Rica, México, Panama and Chile electricity generation CGUs.

- Renewable electricity generation in Latin America is managed under energy sale-purchase contracts through stable business models which are not subject to fluctuation risks on the basis of market variables.

- Operation and maintenance costs. Estimated on the basis of historical costs and on the basis of best forecasts when no historical data are available.

- In addition, long-term growth rate of 2% - 3.3% (1.9% - 3.2% in 2020) and pre-tax discount rate of 8.4% - 14.6% (8.6% - 15% in 2020) have been used.

Renewables Australia:

- Electricity generation in Australia is managed during the majority of its useful life under energy sale-purchase contracts through stable business models and which are not subject to fluctuation risks on the basis of market variables. Upon termination of the contracts, energy prices are set based on the market and are estimated on the basis of developments in the country's energy scenario, including the foreseeable evolution of the generating fleet and taking into account expected supply and demand, as well as production costs.

- Operation and maintenance costs. Estimated on the basis of historical costs and on the basis of best forecasts when no historical data are available.

- In addition, long-term growth rate of 2.8% (2.7% in 2020) and pre-tax discount rate of 7.7% (7.4% in 2020) have been used.

Supply:

- Supply margin. Projections have been used on the evolution of the number of customers and unitary margins based on existing contracts and the knowledge of the markets in which it operates.

- In addition, long-term growth rate of 0.5% (0.5% in 2020) and pre-tax discount rate of 6.5% (6.8% in 2020) have been used.

Naturgy has carried out a sensitivity analysis with respect to the following fluctuations:

Thermal electricity generation Spain:

- an increase in the discount rate of 50 basis points would entail an impairment of Euros 40 million.
- a decrease in the growth rate of 50 basis points would entail an impairment of Euros 36 million.
- a decrease in electricity output of 5% would entail an impairment of Euros 94 million.
- a decrease in the electricity price of 1 €/MWh together with the related variation in the cost of gas would entail an impairment of Euros 74 million.

Hydraulic electricity generation Spain: the result of the sensitivity analysis carried out is:

- an increase in the discount rate of 50 basis points would entail an impairment of Euros 61 million.
- a decrease in the growth rate of 50 basis points would entail an impairment of Euros 18 million.
- a decrease in electricity output of 5% would entail an impairment of Euros 94 million.
- a decrease in the electricity price of 1 €/MWh would entail an impairment of Euros 74 million.

Gas distribution Argentina: the result of the sensitivity analysis carried out is:

- an increase in the discount rate of 50 basis points would entail an impairment of Euros 3 million.
- a decrease in the growth rate of 50 basis points would equalize value in use with carrying value.
- a decrease of 5% in the rate/remuneration evolution would entail an impairment of Euros 13 million.
- an increase of 5% in operating and maintenance costs would entail an impairment of Euros 7 million.
- an increase of 5% in investments would entail an impairment of Euros 4 million.

Electricity generation Dominican Republic: The result of the sensitivity analysis carried out is as follow:

- an increase in the discount rate of 50 basis points would result in the recognised reversal remaining unchanged.

Electricity generation Panama: The result of the sensitivity analysis carried out is as follow:

- an increase in the discount rate of 50 basis points would entail an impairment of Euros 1 million.

Electricity generation Costa Rica: The result of the sensitivity analysis carried out is as follow:

- an increase in the discount rate of 50 basis points would entail an impairment of Euros 6 million.

For other investments in group companies and associates, Naturgy has carried out a sensitivity analysis for 2021 and 2020 of the unfavourable variations which, drawing on historical experience, may reasonably impact the aforementioned sensitive parameters on which the recoverable amounts have been determined. Specifically, the most relevant sensitivity analyses performed are as follows:

	Increase	Decrease
Discount rate	50 basis points	—
Growth rate	—	50 basis points
Electricity generated	—	5%
Electricity price	—	5%
Fuel supply costs	5%	—
Tariff/remuneration performance	—	5%
Operating and maintenance costs	5%	—
Investments	5%	—

These sensitivity analyses performed separately for each basic assumption would not affect the conclusions drawn to the effect that the recoverable amount exceeds the carrying amount for investments in Group companies recorded in these annual accounts.

Note 5. Intangible assets

This heading breaks down as follows:

	Patents, licences, trademarks and other	Computer software	Subtotal	Goodwill	Total
Cost	—	6	6	815	821
Accumulated amortisation	—	(3)	(3)	(815)	(818)
Carrying value at 1.1.2020	—	3	3	—	3
Amortisation charge	—	(1)	(1)	—	(1)
Carrying value at 31.12.2020	1	2	3	—	3
Cost	1	6	7	815	822
Accumulated amortisation	—	(4)	(4)	(815)	(819)
Carrying value at 1.1.2021	**1**	**2**	**3**	**—**	**3**
Investment	—	—	—	—	—
Amortisation charge	—	(1)	(1)	—	(1)
Carrying value at 31.12.2021	1	1	2	—	2
Cost	1	6	7	815	822
Accumulated amortisation	—	(5)	(5)	(815)	(820)
Carrying value at 31.12.2021	**1**	**1**	**2**	**—**	**2**

Brands worth Euros 1 million were acquired in 2020.

Goodwill derives from the vertical merger of Unión Fenosa, S.A. completed in 2009 and is attributable to the benefits and synergies arising from the integration with Naturgy. It has been fully amortised since 2019.

At 31 December 2021, intangible assets include fully amortised goodwill.

In 2021 and 2020 there have been no disposals of fully-amortised assets.

Note 6. Property, plant and equipment

Set out below is an analysis showing movements in Property, plant and equipment during 2021 and 2020:

	Land and buildings	Other property, plant and equipment	Total
Cost	184	35	219
Accumulated amortisation	(72)	(23)	(95)
Carrying value at 1.1.2020	**112**	**12**	**124**
Investment	5	2	7
Divestment	(5)	—	(5)
Amortisation charge	(11)	(2)	(13)
Carrying value at 31.12.2020	**101**	**12**	**113**
Cost	177	34	211
Accumulated amortisation	(76)	(22)	(98)
Carrying value at 1.1.2021	**101**	**12**	**113**
Investment	9	2	11
Divestment	(2)	—	(2)
Amortisation charge	(10)	(2)	(12)
Carrying value at 31.12.2021	**98**	**12**	**110**
Cost	169	25	194
Accumulated amortisation	(71)	(13)	(84)
Carrying value at 31.12.2021	**98**	**12**	**110**

In 2021 there have been disposals of fully-depreciated assets totalling Euros 24 million (Euros 2 million at 31 December 2020). In addition, in 2021 various properties and vehicles have been sold resulting in net asset disposals of Euros 1 million with a positive result of Euros 1 million on the income statement reflected under "Impairment and gains/losses on fixed asset disposals".

Property, plant and equipment include fully-depreciated assets still in use totalling Euros 17 million at 31 December 2021 (Euros 19 million in 2020).

It is the Company’s policy to take out insurance where deemed necessary to cover risks that could affect its property, plant and equipment.

At 31 December 2021 and 31 December 2020, the Company had no investment commitments.

Note 7. Investments in Group companies and associates

The classification of investments in Group companies and associates by category at 31 December 2021 and 31 December 2020 is as follows:

At 31.12.2021	Financial assets at cost	Financial assets at amortised cost	Total
Equity instruments	16,138	—	16,138
Loans	—	15,146	15,146
Non-current	**16,138**	**15,146**	**31,284**
Loans	—	2,376	2,376
Other financial assets	—	3	3
Current	**—**	**2,379**	**2,379**
TOTAL	**16,138**	**17,525**	**33,663**

At 31.12.2020	Financial assets at cost	Financial assets at amortised cost	Total
Equity instruments	15,417	—	15,417
Loans	—	15,177	15,177
Non-current	**15,417**	**15,177**	**30,594**
Loans	—	628	628
Other financial assets	—	115	115
Current	**—**	**743**	**743**
TOTAL	**15,417**	**15,920**	**31,337**

Movements during the year in non-current investments in group companies and associates are as follows:

	Holdings in group companies	Loans to group companies	Holdings in associates	Total
Balance at 01.01.2020	**16,548**	**16,202**	**4**	**32,754**
Additions	83	—	—	83
Divestments	(130)	(1)	—	(131)
Reclassification	—	(1,024)	—	(1,024)
Charge/reversal provisions	(1,088)	—	—	(1,088)
Balance at 31.12.2020	**15,413**	**15,177**	**4**	**30,594**
Additions	550	578	—	1,128
Divestments	(706)	(577)	—	(1,283)
Reclassification	—	(32)	—	(32)
Charge/reversal provisions	877	—	—	877
Balance at 31.12.2021	**16,134**	**15,146**	**4**	**31,284**

The main corporate transactions carried out by the Company were as follows:

2021

- In March 2021, Naturgy, ENI and the Arab Republic of Egypt completed the agreement reached on 1 December 2020 to amicably resolve the disputes affecting UFG. As a result, UFG received a number of cash payments for the sale of the assets in Egypt, UFG's business activities in Spain and one of its vessels, as well as the receipt of compensation agreed with the Egyptian government. Simultaneously, Naturgy completed the acquisition of the remaining 50% holding in UFG for Euros 466 million, bringing Naturgy's holding to 100% and enabling it to obtain control. This also entailed the termination of the annual gas supply contract of around 3.5 bcm for supplying combined cycle plants in Spain that was due to end in 2029, while maintaining the contract with Oman which expires in 2025.

  In addition, the distribution of an interim dividend of Euros 218 million for 2021 was recorded as a reduction in the carrying amount of the holding.

- Cash contribution to offset losses incurred by Naturgy LNG, S.L. in the amount of Euros 82 million.

- The distribution of the share premium has been recorded as a decrease in the carrying value of the interest in Holding Negocios de Gas, S.A., in the amount of Euros 396 million.

- The distribution of an interim dividend for 2021 amounting to Euros 91 million has been recorded as a decrease in the carrying amount of the shareholding in Holding Negocios de Electricidad, S.A.

- Cash contribution to offset losses incurred by Petroleum Oil&Gas España, S.A. for Euros 1 million.

- Disposal of 60% of the shareholdings in Lean Corporate Services, S.L., Lean Customer Services, S.L, Lean Grids Services, S.L and Naturgy IT, S.L. already announced in November 2020 to provide the corresponding strategic partners in the provision of the various services involved with an equity interest without any relevant impact on results. At 31 December 2021 the Company holds a 15% interest in all these companies and therefore they have been reclassified to long-term investments (Note 8).

- As a result of the spin-off in 2021 of Naturgy Generación, S.L.U. in favour of Naturgy Ciclos Combinados, S.L.U. and Naturgy Generación Térmica, S.L., Euros 774 million of the net shareholding of Naturgy Generación, S.L.U. was reclassified, giving rise to a valuation of Euros 761 million in Naturgy Ciclos Combinados, S.L.U and Euros 13 million in Naturgy Generación Térmica, S.L.

- A provision/reversal of provisions for holdings in Group companies of Euros 877 million (expense reduction) was recorded (Note 4).

2020

- Cash contribution to offset losses incurred by Gas Natural Comercializadora, S.A. in the amount of Euros 33 million.

- Cash contribution to offset losses incurred by Comercializadora Regulada Gas&Power, S.A. for Euros 28 million.

- The distribution of the share premium was recorded as a decrease in the carrying value of the holding in the Group company Union Fenosa Mineria, S.A., in the amount of Euros 21 million. Subsequently, Union Fenosa Mineria, S.A. was wound up with no impact on income, involving a divestment of Euros 43 million. As a result of this liquidation the Company received the shareholding of Lignitos de Meirama, S.A., an investee of Union Fenosa Minería, S.A., for a carrying value of Euros 17 million, offsetting the Company's debts with the liquidated company which totalled Euros 26 million.

- Cash contribution to offset losses incurred by Lean Grids Services, S.L. in the amount of Euros 2 million. In March 2020, a 25.0% interest in Lean Corporate Services, S.L., Lean Customer Services, S.L. and Lean Grids Services, S.L. was sold to the relevant strategic partners in the provision of the various services. These transactions did not result in a loss of control and did not have a material impact on the Company's annual accounts. Subsequently, in November, the sale of an additional 60% holding was announced, together with Naturgy IT, S.L., which was completed in the first quarter of 2021.

- Cash contribution for a capital increase in Naturgy Nuevas Energías, S.L.U (formerly Naturgy Gas&Power, S.L.U) amounting to Euros 2 million.

- Liquidation of Clover Financial and Treasury Services, D.A.C. without any impact on income.

- The distribution of a supplementary dividend for 2019 amounting to Euros 64 million was recorded as a decrease in the carrying amount of the holding in the Group company Global Power Generation, S.A.

- Other movements totalling Euros 1 million.

- Provisions for holdings in Group companies amounting to Euros 1,088 million were recorded (Note 4).

- Reclassifications included the transfer to current receivables from Group companies in the amount of Euros 1,024 million.

The cumulative provision for the impairment of shareholdings in Group companies and associates totals Euros 4,153 million at 31 December 2021 (Euros 7,369 million at 31 December 2020), relating basically to the following companies (Note 4):

	2021	2020	Variation
Naturgy Generación, S.L.U.	2,186	4,678	(2,492)
Unión Fenosa Gas, S.A.	1,395	2,179	(784)
Gas Natural Exploración, S.L.	214	213	1
Naturgy Informática, S.A.	155	146	9
Petroleum, Oil & Gas España, S.A.	74	73	1
Naturgy LNG, S.L.	59	10	49
N.Engineering, S.L.	12	4	8
General de Edificios y Solares, S.L.	9	9	—
Naturgy Participaciones, S.A.U.	8	21	(13)
Naturgy Almacenamientos Andalucía, S.A.	8	3	5
Naturgy Nuevas Energías, S.L.U.	2	—	2
Other	31	33	(2)
Total	**4,153**	**7,369**	**(3,216)**

The amount of the provision for impairment of Naturgy Generación, S.L.U. considered in cost of the shares of the beneficiary companies of the spin-off Naturgy Ciclos Combinados, S.L.U and Naturgy Generación Térmica, S.L amounts to Euros 2,338 million.

Financial income for dividends received from investments in equity instruments of group companies and associates during 2021 and 2020, correspond to the following companies:

	2021	2020
Holding Negocios Electricidad, S.A.	208	183
Naturgy Iberia, S.A.	200	200
Holding Negocios Gas, S.A.	125	432
Sagane, S.A.	124	175
Global Power Generation, S.A.U.	116	—
Unión Fenosa Gas, S.A.	82	—
Naturgy Inversiones Internacionales, S.A.	70	25
Naturgy Finance, B.V.	4	—
Naturgy Engineering, S.L.	1	15
Naturgy Capital Markets, S.A.	1	3
Naturgy Distribución Latinoamérica S.A.	—	141
Naturgy Aprovisionamientos S.A	—	95
Other	1	2
Total	**932**	**1,271**

The breakdown of shareholdings in Naturgy companies is set out below:

					Data at 31 December 2021								
					% interest			Equity					
Company	Registered Office	Activity	Carrying value 2021	Carrying value 2020	Direct	Indirect	Total	Capital	Reserves (1)	Profit/(loss)	Interim dividend	Other (2)	EQUITY
Naturgy Aprovisionamientos, S.A.	Spain	Gas supply	85	85	100.0	—	100.0	1	181	(49)	—	1	134
Naturgy LNG, S.L.	Spain	Gas supply	38	5	100.0	—	100.0	2	94	(59)	—	(3)	34
Sagane, S.A.	Spain	Gas supply	42	42	100.0	—	100.0	95	22	76	—	3	196
Unión Fenosa Gas, S.A.	Spain	Gas supply	1,294	262	100.0	—	100.0	33	398	437	(300)	(341)	227
Naturgy LNG GOM, S.L.	Spain	Gas supply	—	—	100.0	—	100.0	—	—	—			—
Gas Natural Comercializadora, S.A.	Spain	Gas and electricity supply	195	195	100.0	—	100.0	3	6	(319)	—	175	(135)
Comercializadora Regulada, Gas & Power, S.A.	Spain	Gas and electricity supply	121	121	100.0	—	100.0	2	4	3	—	—	9
Naturgy Commodities Trading, S.A.	Spain	Gas and electricity supply	11	11	100.0	—	100.0	10	6	11	—	—	27
Naturgy Iberia, S.A.	Spain	Gas and electricity supply	494	494	100.0	—	100.0	3	167	140	(100)	405	615
Naturgy Clientes, S.A.	Spain	Gas and electricity supply	—	—	100.0	—	100.0	—	—	—	—	—	—
Holding Negocios Electricidad, S.A.	Spain	Electricity distribution	3,845	3,936	100.0	—	100.0	—	3,666	124	—	—	3,790
Holding de Negocios de Gas, S.A.	Spain	Gas distribution	4,720	5,115	80.0	—	80.0	—	5,958	79	—	—	6,037
Naturgy Generación, S.L.U.	Spain	Electricity generation	928	1,548	100.0	—	100.0	732	53	143	—	(113)	815
Naturgy Renovables, S.L.U.	Spain	Electricity generation	1,141	1,141	100.0	—	100.0	90	208	73	—	(228)	143
Global Power Generation, S.A.	Spain	Electricity generation	648	648	75.0	—	75.0	20	552	158	—	25	755
Toledo PV A.I.E.	Spain	Electricity generation	—	—	33.3	—	33.3	—	—	1	—	—	1
Naturgy Ciclos Combinados, S.L.U.	Spain	Electricity generation	761	—	100.0	—	100.0	320	445	42	—	(4)	803
Naturgy Generación Térmica, S.L.U.	Spain	Electricity generation	13	—	100.0	—	100.0	—	23	(4)	—	(208)	(189)
Naturgy Almacenamientos Andalucía S.A.	Spain	Gas infrastructures	—	5	100.0	—	100.0	—	5	2	—	—	7
Gas Natural Exploración, S.L.	Spain	Gas infrastructures	8	9	100.0	—	100.0	8	16	—	—	(16)	8
Petroleum, Oil & Gas España, S.A.	Spain	Gas infrastructures	—	—	32.3	67.7	100.0	4	(2)	(2)	—	—	—
Liginitos de Meirama, S.A.	Spain	Mining	17	15	100.0	—	100.0	23	(7)	1	—	—	17
Natural Re, S.A.	Luxembourg	Insurance	9	9	100.0	—	100.0	5	56	1	—	—	62
General de Edificios y Solares, S.L.	Spain	Services	54	54	100.0	—	100.0	34	20	—	—	—	54
Naturgy Capital Markets, S.A.	Spain	Financial services	—	—	100.0	—	100.0	—	—	1	—	—	1
Naturgy Finance, B.V.	Netherlands	Financial services	7	7	100.0	—	100.0	—	5	4	—	—	9
Naturgy Participaciones, S.A.	Spain	Financial services	102	89	100.0	—	100.0	—	90	13	—	(1)	102
Unión Fenosa Preferentes, S.A.U.	Spain	Financial services	—	—	100.0	—	100.0	—	1	1	(1)	110	111
Naturgy Informática, S.A.	Spain	IT services	1	10	100.0	—	100.0	20	(10)	(9)	—	—	1
Naturgy Engineering, S.L.	Spain	Engineering services	9	19	100.0	—	100.0	—	15	(3)	—	1	13
Naturgy Ingenieria Nuclear, S.L.	Spain	Engineering services	1	1	100.0	—	100.0	—	1	(1)	—	—	—
Naturgy Distribución Latinoamérica, S.A.	Spain	Holding company	557	557	100.0	—	100.0	402	221	196	—	—	819
Naturgy Nuevas Energías, S.L.U.	Spain	Holding company	—	2	100.0	—	100.0	2	—	(8)	—	—	(6)
Naturgy Infraestructuras EMEA, S.L.	Spain	Holding company	89	89	100.0	—	100.0	—	199	3	—	—	202
Naturgy Inversiones Internacionales, S.A.	Spain	Holding company	944	944	100.0	—	100.0	250	346	363	—	(142)	817
TOTAL			**16,134**	**15,413**									

(1) Includes the share premium, reserves, prior-year losses, contributions and retained earnings.

(2) Includes value change adjustments, other equity instruments and grants, donations and bequests.

Non-current loans to Group companies which at 31 December 2021 total Euros 15,146 million (15,177 million at 31 December 2020), with maturities as follows:

Maturity	At 31.12.2021
2024	7,471
2025	1,000
2026	1,000
2027	1,324
2028	1,350
2029	1,000
2030	1,000
2037	388
2040	613
Total	**15,146**

Set out below are movements during 2021 and 2020 in loans and other current financial assets:

	Loans to group companies	Other financial assets	Total
Balance at 01.01.2020	**527**	**139**	**666**
Additions	180	111	291
Divestments	(483)	(135)	(618)
Reclassifications and transfers	406	—	406
Exchange differences	(2)	—	(2)
Balance at 31.12.2020	**628**	**115**	**743**
Additions	2,127	—	2,127
Divestments	(266)	(112)	(378)
Reclassifications and transfers	(113)	—	(113)
Balance at 31.12.2021	**2,376**	**3**	**2,379**

There are no significant differences between carrying values and fair values in the balances under Loans to Group companies and other receivables.

The heading Loans to Group companies includes loans to Group companies amounting to Euros 224 million (Euros 349 million in 2020) and cash pooling balances with investee companies, as manager of Naturgy's centralised cash system amounting to Euros 2,084 million (Euros 212 million in 2020). It also includes accrued unmatured interest of Euros 68 million (Euros 67 million in 2020).

At 31 December 2021, loans to Group companies and associates have borne interest at a rate of 2.15% (2.20% in 2020) in the case of non-current loans and 1% (1% in 2020) in the case of current loans.

At 31 December 2021 there are no dividend balances receivable (110 million as at 31 December 2020 recorded under "Other current financial assets").

Note 8. Investments

Investments by class and category at 31 December 2021 and 31 December 2020 break down as follows:

At 31 December 2021	Financial assets at amortised cost	At cost	Total
Equity instruments	—	4	4
Loans to third parties	1	—	1
Other financial assets	4	—	4
Non-current investments	**5**	**4**	**9**
Other financial assets	57	—	57
Current investments	**57**	**—**	**57**
Total	**62**	**4**	**66**

At 31 December 2020	Financial assets at amortised cost	Financial assets at fair value through profit and loss	At cost	Total
Equity instruments	—	—	5	5
Other financial assets	4	—	—	4
Non-current investments	**4**	**—**	**5**	**9**
Other financial assets	51	120	—	171
Current investments	**51**	**120**	**—**	**171**
Total	**55**	**120**	**5**	**180**

Financial assets recognised at fair value at 31 December 2021 and at 31 December 2020 are classified as follows:

	31.12.2021				31.12.2020			
Financial assets	**Level 1 (quoted price in an active market)**	**Level 2 (observable variables)**	**Level 3 (unobservable variables)**	**Total**	**Level 1 (quoted price in an active market)**	**Level 2 (observable variables)**	**Level 3 (unobservable variables)**	**Total**
Fair value through profit or loss	—	—	—	—	120	—	—	120
Total	**—**	**—**	**—**	**—**	**120**	**—**	**—**	**120**

The movement in equity instruments in 2021 and 2020, based on the method applied for calculating their fair value, is as follows:

	2021				2020			
	Level 1 (quoted price in an active market)	**Level 2 (observable variables)**	**Level 3 (unobservabl e variables)**	**Total**	**Level 1 (quoted price in an active market)**	**Level 2 (observable variables)**	**Level 3 (unobservabl e variables)**	**Total**
At 1 January	120	—	—	120	—	—	—	—
Increase	—	—	—	—	120	—	—	120
Decrease	(120)	—	—	(120)	—	—	—	—
At 31 December	**—**	**—**	**—**	**—**	**120**	**—**	**—**	**120**

Financial assets at cost

All financial assets at cost relate to unlisted shareholdings at 31 December 2021 and 31 December 2020.

At 31 December 2021, this heading includes the shareholdings in Naturgy IT, S.L, Lean Customer Services, S.L, Lean Corporate Services, S.L and Lean Grids, S.L following the 60% sale described in Note 5, resulting in a percentage shareholding of 15%.

Financial assets at fair value through profit and loss

The Trading portfolio at 31 December 2020 included the valuation of deposits constituted as CO_2 emission rights amounting to Euros 120 million.

Financial assets at amortised cost

The balance at 31 December 2021 and 2020 is as follows:

	At 31.12.21	At 31.12.20
Loans to companies	1	—
Deposits and guarantee deposits	4	4
Non- current	**5**	**4**
Deposits and guarantee deposits	57	51
Current	**57**	**51**
Total	**62**	**55**

The fair values and carrying amounts of these assets do not differ significantly.

The breakdown by maturities at 31 December 2021 and 31 December 2020 is as follows:

Maturities	**31.12.2021**	31.12.2020
Before 1 year	57	51
Between 1 and 5 years	1	—
More than 5 years	4	4
Total	**62**	**55**

Note 9. Other non-current assets and Trade and other receivables

The headings "Other non-current assets" and "Trade and other receivables" at 31 December 2021 and 31 December 2020, classified by nature and category, are as follows:

At 31.12.2021	**At fair value through profit and loss**	**Amortised cost**	**Total**
Derivatives (Note 14)	231	—	231
Other non-current assets	**231**	**—**	**231**
Derivatives (Note 14)	1,865	—	1,865
Other assets	—	417	417
Trade and other receivables	**1,865**	**417**	**2,282**
Total	**2,096**	**417**	**2,513**

At 31.12.2020	**At fair value through profit and loss**	**Amortised cost**	**Total**
Derivatives (Note 14)	136	—	136
Other non-current assets	**136**	**—**	**136**
Derivatives (Note 14)	123	—	123
Other assets	—	189	189
Trade and other receivables	**123**	**189**	**312**
Total	**259**	**189**	**448**

Fair value through profit and loss

Financial assets recognised at fair value at 31 December 2021 and at 31 December 2020 are classified as follows:

	At 31.12.2021				At 31.12.2020			
Financial assets	**Level 1 (quoted price in an active market)**	**Level 2 (observable variables)**	**Level 3 (unobservable variables)**	**Total**	**Level 1 (quoted price in an active market)**	**Level 2 (observable variables)**	**Level 3 (unobservable variables)**	**Total**
Fair value through profit and loss	—	2,096	—	2,096	—	259	—	259
Total	**—**	**2,096**	**—**	**2,096**	**—**	**259**	**—**	**259**

This heading includes gas price operating hedging derivatives amounting to Euros 2,096 million (31 December 2020: Euros 259 million), of which Euros 231 million is classified as non-current (31 December 2020: Euros 136 million) (Note 14).

Amortised cost

The breakdown of this account is as follows:

	At 31.12.21	At 31.12.20
Trade receivables	83	65
Trade receivables, Group companies and associates	213	143
Sundry receivables	12	3
Provision	(27)	(28)
Current income tax asset	134	4
Other amounts receivable from Public Administrations	2	2
Total	**417**	**189**

In general, amounts billed pending collection do not bear interest, the average maturity period being less than 21 days.

Current tax assets include a reduction in the amount of the assignment of the corporate income tax receivable, as it is considered to be non-recourse factoring since the risks and rewards have been transferred.

Movements in the bad debt provision are as follows:

	2021	2020
At 1 January	**(28)**	**(30)**
Net charge for the year (Note 21)	1	2
At 31 December	**(27)**	**(28)**

Note 10. Cash and cash equivalents

Cash and cash equivalents include:

	At 31.12.2021	At 31.12.2020
Cash at banks and in hand	889	1,076
Other cash equivalents	1,319	1,542
Total	**2,208**	**2,618**

“Other cash equivalents” mainly relate to short-term investments in deposits associated with CO_2 emission allowances maturing in under three months and with assured returns.

Note 11. Equity

The main items of Equity are as follows:

Share capital and share premium

The variations during 2021 and 2020 in the number of shares and share capital and share premium accounts have been as follows:

	Number of shares	Share capital	Share premium	Total
At 1 January 2020	**984,122,146**	**984**	**3,808**	**4,792**
Capital reduction	(14,508,345)	(14)	—	(14)
At 31 December 2020	**969,613,801**	**970**	**3,808**	**4,778**
Variation	—	—	—	—
At 31 December 2021	**969,613,801**	**970**	**3,808**	**4,778**

All issued shares are fully paid up and carry equal voting and dividend rights.

On 10 August 2020, capital was reduced through the redemption of 14,508,345 treasury shares with a par value of 1 euro each, representing approximately 1.47% of the Company's share capital at the time of adoption of the relevant resolution (see paragraph on treasury shares). Following the capital reduction share capital stood at Euros 970 million and consisted of 969,613,801 shares with a par value of 1 euro each.

There were no movements in the number of shares or in the accounts "Share capital" and "Share premium" during 2021.

The Company's Board of Directors, for a maximum term of five years as from 20 April 2017, is empowered to increase share capital by Euros 500,344,670 through one or more cash payments at the time and in the amount that it deems fit, issuing ordinary, privileged or redeemable shares with or without voting rights, with or without a share premium, without requiring any further authorisation from the shareholders, with the possibility of agreeing, as appropriate, the full or partial exclusion of preferential subscription rights up to a limit of 20% of share capital at the date of this authorisation, and to alter the By-laws as required due to the capital increase or increases performed by virtue of said authorisation, with provision for an incomplete subscription, in accordance with the provisions of Article 297.1.b) of the Spanish Companies Act.

The Spanish Companies Act specifically allows the use of the Share premium balance to increase capital and imposes no specific restrictions on its use.

The most relevant holdings in the Company's share capital at 31 December 2021 and 2020, in accordance with the public information available or the communication issued by the Company itself, are as follows:

	% interest in share capital	
	2021	2020
- Fundación Bancaria Caixa d'Estalvis i Pensions de Barcelona, "la Caixa" (1)	26.71	24.8
-Global Infrastructure Partners III (2)	20.6	20.6
-CVC Capital Partners SICAV-FIS, S.A. (3)	20.7	20.7
- IFM Global Infraestructure Fund	12.2	—
- Sonatrach	4.1	4.1

(1) Holding through Criteria Caixa, S.A.U.

(2) Global Infrastructure Partners III, whose investment manager is Global Infrastructure Management LLC, holds its interest indirectly through GIP III Canary 1, S.à.r.l.

(3) Through Rioja Acquisition S.à.r.l.

All the Company's shares are traded on the four official Spanish Stock Exchanges and the "Mercado continuo" and form part of Spain's Ibex 35 stock index.

The Company's share price at 31 December 2021 was Euros 28.63 (Euros 18.96 at 31 December 2020).

Reserves

"Reserves" includes the following reserves:

	2021	2020
Legal reserve	200	200
Statutory reserve	100	100
Goodwill reserve	—	—
Voluntary reserves	10,702	10,702
Capital redemption reserve	31	31
Other reserves	271	258
Total	**11,304**	**11,291**

Legal reserve

Appropriations to the legal reserve are made in compliance with the Spanish Capital Companies Act, which stipulates that 10% of the profits must be transferred to this reserve until it represents at least 20% of share capital. The legal reserve can be used to increase capital in the part that exceeds 10% of the capital increased.

Except for the use mentioned above, and as long as it does not exceed 20% of share capital, the legal reserve can only be used to offset losses in the event of no other reserves being available.

Statutory reserve

Under the Company's Articles of Association, 2% of net profit for the year must be allocated to the statutory reserves until it reaches at least 10% of share capital.

Goodwill reserve

Law 22/2015 on Auditing eliminated the requirement to record annually the restricted reserve for at least 5% of the goodwill figuring under assets on the balance sheet, stipulating that in periods commencing as from 1 January 2016, the goodwill reserve is to be reclassified to voluntary reserves and will be available in the amount that exceeds the goodwill recognised under assets on the balance sheet.

At the annual general meeting held on 26 May 2020, the shareholders agreed to the transfer to Voluntary reserves of Euros 27 million from the Goodwill reserve. At 31 December 2020 the entire goodwill reserve has been reclassified to voluntary reserves.

Capital redemption reserve

Following approval at the ordinary general meeting of shareholders held on 26 May 2020, a capital reduction was made during the year through the redemption of treasury shares with a reduction of Euros 14 million and 284 million in Voluntary reserves.

In addition, pursuant to Article 335 c) of the Spanish Companies Act a restricted Capital redemption reserve was created for an amount equal to the par value of the redeemed shares. The total accumulated capital redemption reserve amounts to Euros 31 million at 31 December 2021 and 2020.

Voluntary reserve and other reserves

Relates basically to voluntary reserves for undistributed profits, also including the effects of the measurement of shareholdings in group companies as a result of transactions between group companies recognised in the same amounts stated in Naturgy's consolidated annual accounts.

Share-based payments

On 31 July 2018, within the framework of the Strategic Plan 2018-2022 the Board of Directors approved a long term variable incentive plan (ILP) involving the Executive Chairman and 25 other executives. The main characteristics of the plan were approved by the general meeting of shareholders on 5 March 2019.

The incentive covers the duration of the Strategic Plan 2018-2022, and scheduled to expire in July 2023. It is directly related to the total yield obtained by the Company's shareholders in the period concerned.

It is arranged through the acquisition of shares in Naturgy Energy Group S.A. through an investee company that can generate a surplus. This surplus, if any, is the incentive that will be given to the participants. At the expiration of the plan, this company will obtain a profit derived from the collection of dividends on its shares, changes in the share price and other income and expenses, mainly financial in character. At that time it will sell the shares required to return all the resources received for the acquisition of the shares and after settling its obligations it will distribute any surplus among its members in the form of shares.

The surplus will be received only if a minimum profitability threshold has been surpassed, which implies a share price of Euros 19.15 when the LTI expires and assuming that all the dividends provided for in the Strategic Plan 2018-2022 are paid.

If they leave the Company, the beneficiaries will only be entitled, in certain cases, to receive a part of the final incentive calculated in proportion to their length of service in the Company with respect to the duration of the plan.

The fair value of the equity instruments granted has been determined at the grant date using a Monte Carlo simulation valuation model based on share Price at the date of the concession with the following assumptions:

Forecast share price volatility (1)	17.73 %
Plan duration (years)	5
Expected dividends	6.26 %
Risk-free interest rate	0.34 %

(1) Forecast volatility has been determined based on the historical volatility of the daily share price in the last year.

As a result of the time apportionment of the fair value estimate of the equity instruments granted over the term of the plan, an amount of Euros 3 million (Euros 2 million in 2020) has been recorded in the income statement for 2021 under Personnel expenses, credited to “Other equity instruments” in the balance sheet.

On the other hand, given the new objectives set out in the 2021-2025 Strategic Plan approved on 28 July 2021, the Naturgy Board of Directors has decided, at the proposal of the Appointments, Remuneration and Corporate Governance Committee, the temporary extension of the current ILP, in order to contribute to the achievement of the aforementioned Strategic Plan. The entry into force of the temporary extension of the ILP is subject to the approval of the Naturgy Shareholders' Meeting.

Treasury shares

Movements during 2021 and 2020 involving the treasury shares of the Company are as follows:

	Number of shares	In million euro	% Capital
At 1 January 2020	**5,183,890**	**121**	**0.5**
Share Acquisition Plan	470,000	8	—
Delivered to employees	(455,797)	(8)	—
2019 buyback programme	9,346,025	178	0.9
Capital reduction	(14,508,345)	(298)	(1.4)
At 31 December 2020	**35,773**	**1**	**—**
Share Acquisition Plan	127,453	3	—
At 31 December 2021	**163,226**	**4**	**—**

In 2021 and 2020, no gains or losses were made on transactions involving the Company’s treasury shares.

On 5 March 2019, the shareholders in general meeting authorised the Board of Directors to purchase, within five years, in one or more operations, fully paid Company shares; the nominal value of the shares directly or indirectly acquired, added to those already held by the Company and its subsidiaries, must not exceed 10% of share capital or any other limit established by law. The price or value of the consideration may not be lower than the par value of the shares or higher than their quoted price.

The minimum and maximum acquisition price will be the share price on the continuous market of the Spanish stock exchanges, within an upper or lower fluctuation of 5%.

Transactions with the Company’s Treasury shares relate to:

2021

– Share acquisition plan: In accordance with the resolutions adopted by the shareholders of Naturgy Energy Group, S.A. at the general meeting held on 5 March 2019, within the Share Acquisition Plan 2020-2023, the one relating to 2021 addressed to Naturgy employees in Spain who decide voluntarily to take part in the Plan was set in motion. The Plan enables participants to receive part of their remuneration in the form of shares in Naturgy Energy Group, S.A., subject to an annual limit of Euros 12,000. In December 2021, 127,453 of the Company's own shares were acquired for Euros 3 million to be handed over to the employees taking part in the Plan. The shares will be delivered in January 2022.

2020

– Share acquisition plan: In accordance with the resolutions adopted by the shareholders of Naturgy Energy Group, S.A. at the general meeting held on 5 March 2019, within the Share Acquisition Plan 2020-2023, the one relating to 2020 addressed to Naturgy employees in Spain who decide voluntarily to take part in the Plan was set in motion. The Plan enables participants to receive part of their remuneration in the form of shares in Naturgy Energy Group, S.A., subject to an annual limit of Euros 12,000. During 2020, 470,000 treasury shares were acquired for Euros 8 million to be handed over to the employees taking part in the Plan and 455,797 shares were delivered, leaving a surplus of 14,203 shares.

– 2019 share buyback programme: The Board of Directors of Naturgy Energy Group, S.A. approved a treasury share buyback programme, which was published on 24 July 2019, with a maximum investment of Euros 400 million to 30 June 2020 representing approximately 2.1% of share capital on the date of notification, the redemption of which was ratified by the shareholders at the annual general meeting held on 26 May 2020. At 30 June 2020, a total of 14,508,345 treasury shares had been acquired under this programme at an average price of 20.6 euros per share, representing a total cost of Euros 299 million (5,162,320 treasury shares at an average price of 23.3 euros per share with a total cost of Euros 121 million at 31 December 2019), which were applied to reduce capital.

– Capital reduction: At a meeting held on 21 July 2020, the Board of Directors of Naturgy Energy Group, S.A. resolved to implement the capital reduction resolution approved at the annual general meeting of shareholders held on 26 May 2020, whereby it approved a reduction in the share capital of Naturgy Energy Group, S.A. to a maximum of Euros 21,465,000, relating to:

  (a) the 465,000 treasury shares held by the Company at close of trading on 24 July 2019.

  (b) the 21,000,000 additional shares with a par value of one euro each which were acquired and may continue to be acquired for redemption by the Company under the treasury share buyback programme (the "Buyback Programme") approved by the Company under Regulation (EU) No. 596/2014 on market abuse and disclosed as price-sensitive information on 24 July 2019 (registration number 280517). The time limit for acquiring these shares was 30 June 2020.

  In this respect, as Naturgy Energy Group, S.A. had acquired a total of 14,043,345 shares at 30 June 2020 under the approved buyback programme referred to in paragraph (b) above, the Board of Directors set the figure for the capital reduction at Euros 14 million (the "Capital Reduction") and agreed to implement this reduction. The Capital Reduction was carried out through the redemption of 14,508,345 treasury shares with a par value of 1 euro each, representing approximately 1.47% of the Company's share capital at the time of adoption of the resolution in question. Following the Capital Reduction share capital stood at Euros 970 million, made up 969,613,801 shares with a par value of 1 euro each.

Dividends

Set out below is a breakdown of the payments of dividends made in 2021 and 2020:

	2021			2020		
	% of Nominal	Euros per share	Amount	% sobre Nominal	Euros per share	Amount
Ordinary shares	**133**	**1.33**	**1,290**	**141**	**1.41**	**1,370**
Other shares (without voting rights, redeemable, etc.)	—	—	—	— %	—	—
Total dividens paid	**133 %**	**1.33**	**1,290**	**141 %**	**1.41**	**1,370**
a) Dividends charged to income statement or retained earnings	133	1.33	1,290	141	1.41	1,370
b) Dividends charged to reserves or share premium account	—	—	—	—	—	—
c) Dividends in kind	—	—	—	—	—	—

2021

On 2 February 2021, the Board of Directors approved the following proposal for the distribution of the Company's net profit for 2020 and retained earnings, for submission to the annual general meeting:

AVAILABLE FOR DISTRIBUTION

Profit.. 98
Retained earnings... 3,076
Distribution base... 3,174

DISTRIBUTION:

TO DIVIDENDS: the gross aggregate amount will be equal to the sum of the following quantities (the “Dividend”):

i. Euros 785 million ("the Total Interim Dividend"), corresponding to the two interim dividends for 2020 paid by Naturgy Energy Group,S.A., jointly equivalent to 0.810 euros per share for the number of shares that were not direct treasury shares on the relevant dates as approved by the Board of Directors in accordance with the interim accounting statements prepared and in accordance with the relevant legal requirements, which revealed the existence of sufficient liquidity for the distribution of these interim dividends out of the profit for 2020, and

ii. The amount obtained by multiplying 0.63 euros per share by the number of shares that are not direct treasury shares on the date on which the registered shareholders entitled to receive the supplementary dividend (the “Supplementary Dividend”) are determined.

The supplementary dividend proposal has been made in line with the commitments of the previous Strategic Plan, reaffirmed in market disclosures during 2020. However, by suspending the share buyback programme, the company has shown caution in view of the uncertainties during 2020.

Euros 785 million of said dividend had already been paid on 29 July and 11 November 2020. The Supplementary Dividend will be paid in the amount per share indicated above through the entities that are members of Sociedad de Gestión de los Sistemas de Registro, Compensación y Liquidación de Valores, S.A.U. (Iberclear). The dividend will be paid to shareholders as from 16 March 2021.

TO RETAINED EARNINGS: Determinable amount obtained by subtracting the dividend amount from the distribution base.

TOTAL DISTRIBUTED 3,174

This proposal for the distribution of profits and retained earnings prepared by the Board for approval by the annual general meeting included a supplementary payment of Euros 0.63 per share for each qualifying share outstanding at the proposed date of payment, 16 March 2021.

Finally, the general meeting of shareholders held on 09 March 2021 approved a supplementary dividend of 0.63 euros per share for shares not directly held as treasury stock on the payment date, which was fully paid in cash on 17 March 2021.

Following payment of the supplementary dividend, the amount allocated to Retained earnings was Euros 1,778 million.

On 27 July 2021, the Company's Board of Directors resolved to pay an interim dividend of 0.30 euros per share out of 2021 results, for shares not classified as direct treasury shares on the date on which the dividend was paid. The dividend was paid in full in cash on 4 August 2021.

The Company had sufficient liquidity to pay out the dividend at the approval date, with the necessary liquidity to proceed to payment pursuant to the Spanish Companies Act. The provisional liquidity statement at 30 June 2021 drawn up by the Directors on 27 July 2021 was as follows:

Profit after tax		468
Reserves to be replenished		—
Maximum amount distributable		468
Forecast maximum interim dividend payment (1)		291
Cash resources	2,341	
Undrawn credit facilities	5,460	
Total liquidity		7,801

(1) Amount considering total shares issued

On 3 November 2021, the Board of Directors of Naturgy Energy Group, S.A. resolved to pay a second interim dividend of 0.40 euros per share out of 2021 results, paid on 15 November 2021, for shares not classified as direct treasury shares on the date on which the dividend was paid.

The Company had sufficient liquidity to pay the dividend at the approval date, in accordance with the provisions of the Spanish Companies Act. The provisional liquidity statement at 30 September 2021 drawn up by the Directors on 2 November 2021 is as follows:

Profit after tax		705
Reserves to be replenished		—
Maximum amount distributable		705
Interim dividend 2020 profits		291
Forecast maximum interim dividend payment (1)		388
Cash resources	1,942	
Undrawn credit facilities	5,465	
Total liquidity		7,407

(1) Amount considering total shares issued

On 3 February 2022, the Board of Directors approved the following proposal for the distribution of the Company's net profit for 2021 and retained earnings, for submission to the annual general meeting:

AVAILABLE FOR DISTRIBUTION

Profit.. 1,706
Retained earnings.. 1,778
Distribution base... 3,484

DISTRIBUTION:

TO DIVIDENDS: the gross aggregate amount will be equal to the sum of the following quantities (the "Dividend"):

i. Euros 679 million ("the Total Interim Dividend"), corresponding to the two interim dividends for 2021 paid by Naturgy Energy Group,S.A., jointly equivalent to 0.70 euros per share for the number of shares that were not direct treasury shares on the relevant dates as approved by the Board of Directors in accordance with the interim accounting statements prepared and in accordance with the legal requirements, which revealed the existence of sufficient liquidity for the distribution of these interim dividends out of the profit for 2021, and

ii. The amount obtained by multiplying 0.50 euros per share by the number of shares that are not direct treasury shares on the date on which the registered shareholders entitled to receive the supplementary dividend (the "Supplementary Dividend") are determined.

Euros 679 million of said dividend had already been paid on 4 August and 15 November 2021. The Supplementary Dividend will be paid in the amount per share indicated above through the entities that are members of Sociedad de Gestión de los Sistemas de Registro, Compensación y Liquidación de Valores, S.A.U. (Iberclear). (Iberclear). The dividend will be paid to shareholders as from 22 March 2022.

The Board of Directors is expressly empowered to delegate its powers to the director(s) it deems fit so that they may perform all the actions required to carry out the distribution and, in particular, without limitation, so that they may designate the entity that is to act as payment agent.

TO RETAINED EARNINGS: Determinable amount obtained by subtracting the dividend amount from the distribution base.

TOTAL DISTRIBUTED 3,484

This proposal for the distribution of profits and retained earnings prepared by the Board for approval by the annual general meeting includes a supplementary payment of Euros 0.50 per share for each qualifying share outstanding at the proposed date of payment, 22 March 2022. In this respect, in the event that at the time of distribution of the third and last payment of the proposed 2021 dividend (Euros 0.50 per share) the same number of treasury shares is maintained as at the 2021 year end (163,226 treasury shares, see section on Treasury shares), the amount applied to retained earnings would be Euros 2,320 million.

2020

At a meeting held on 4 February 2020, the Board of Directors of Naturgy Energy Group, S.A. agreed to the proposed distribution of profits described in Note 11 to the annual accounts for the year ended 31 December 2019. Following the declaration of a "state of alarm" and with the aim of safeguarding the health and safety of all shareholders, employees and collaborators, the company decided to postpone the Annual General Meeting scheduled for 17 March 2020.

To prevent this deferral having a detrimental effect on its shareholders and particularly on the over 70,000 minority shareholders, on 16 March 2020 the Board of Directors of Naturgy Energy Group, S.A. resolved to pay a third interim dividend of 0.593 euros per share out of 2019 profits, for shares not classified as direct treasury shares on the date on which the dividend was paid, this being 25 March 2020.

Subsequently, the general meeting of shareholders held on 26 May 2020 approved a supplementary dividend of 0.010 euros per share for shares not directly held as treasury stock on the payment date, which was fully paid in cash on 03 June 2020. Following payment of the supplementary dividend, the amount allocated to Retained earnings was Euros 3,076 million.

On 21 July 2020, the Company's Board of Directors resolved to pay a first interim dividend of 0.31 euros per share out of 2020 results, for shares not classified as direct treasury shares on the date on which the dividend was paid, this being 29 July 2020.

Finally, on 27 October 2020, the Company's Board of Directors resolved to pay a second interim dividend of 0.50 euros per share out of 2020 results, for shares not classified as direct treasury shares on the date on which the dividend was paid, this being 11 November 2020.

The trend in the Company's profits in the last quarter of the year, basically due to the impairment of holdings in Group companies, meant that at year end profits were insufficient to be able to pay an interim dividend. At the annual general meeting, therefore, the Board of Directors proposed that they should be taken to retained earnings.

Note 12. Provisions

The breakdown of provisions at 31 December 2021 and 2020 is as follows:

	At 31.12.2021	At 31.12.2020
Provisions for employee obligations	242	258
Other provisions	67	115
Non-current provisions	**309**	**373**

Provisions for employee obligations

A breakdown of the provisions related to employee obligations is as follows:

	2021			2020		
	Pensions and other similar obligations	**Other obligations with personnel**	**Total**	**Pensions and other similar obligations**	**Other obligations with personnel**	**Total**
At 1 January	**253**	**5**	**258**	**267**	**5**	**272**
Appropriations/reversals charged to income	3	1	4	4	2	6
Payments during the year	(10)	—	(10)	(15)	(2)	(17)
Changes recognised directly in equity	(19)	—	(19)	(2)	—	(2)
Transfers and other applications	9	—	9	(1)	—	(1)
At 31 December	**236**	**6**	**242**	**253**	**5**	**258**

Pensions and other similar liabilities

Most of the Company's post-employment obligations consist of the contribution of defined amounts to occupational pension plan systems. Nevertheless, at 31 December 2021 and 31 December 2020, the Company held the following defined benefit obligations for certain groups of workers:

- Pensions to retired workers, the disabled, widows and orphans and other related groups.
- Defined benefit supplement obligations with retired personnel of the legacy Unión Fenosa group who retired before November 2002 and a residual part of current personnel.
- Coverage of retirement and death for certain employees.
- Gas subsidy for current and retired personnel.
- Electricity for current and retired personnel.
- Obligations with employees that took early retirement until they reach official retirement age and early retirement plans.
- Salary supplements and contributions to social security for a group of employees taking early retirement until they can access ordinary retirement.
- Health care and other benefits.

The amounts recognised in the Balance sheet for pensions and similar obligations, as well as the movement in the current value of the obligations and the fair value of the plan assets are determined as follows:

Present value of obligations	**2021**	2020
At 1 January	**917**	**969**
Service cost for the year	1	1
Interest cost	4	8
Changes recognised directly in equity	(34)	3
Benefits paid	(56)	(63)
Transfers and other	10	(1)
At 31 December	**842**	**917**

Fair value of plan assets		
At 1 January	**664**	**702**
Expected yield	2	5
Contributions	—	4
Changes recognised directly in equity	(15)	5
Benefits paid	(46)	(52)
Transfers and other	1	—
At 31 December	**606**	**664**
Provisions for pensions and similar obligations	**236**	**253**

The amounts recognised in the income statement for all the above-mentioned defined benefit plans are as follows:

	2021	2020
Service cost for the year	1	1
Interest cost	2	3
Total charge to the income statement	**3**	**4**

Benefits for pensions and similar obligations, depending on the duration of the above commitments, are as follows:

	2021	2020
1 to 5 years	—	—
5 to 10 years	23	26
More than 10 years	213	227
Provisions for pensions and similar obligations	**236**	**253**

The plan assets expressed as a percentage of total assets are as follows:

% of total	**2021**	2020
Bonds	100%	100%

Cumulative actuarial gains and losses, net of the tax effect, recognised directly in equity are negative in the amount of Euros 6 million at 31 December 2021 (negative in the amount of Euros 20 million at 31 December 2020).

The change recognised in equity relates to actuarial losses and gains derived basically from adjustments to:

	2021	2020
Financial assumptions	(43)	37
Demographic assumptions	39	(6)
Experience	(15)	(33)
At 31 December	**(19)**	**(2)**

Actuarial assumptions applied are as follows:

	At 31.12.2021	At 31.12.2020
Discount rate (p.a.)	0.0 to 1.38%	0.0 to 0.78%
Expected return on plan assets (p.a.)	0.0 to 1.38%	0.0 to 0.78%
Future salary increases (p.a.)	2.00%	2.00%
Future pension increases (p.a.)	2.00%	2.00%
Inflation rate (annual)	2.00%	2.00%
Mortality table	PER2020 Col 1st order	PERMF 2020
Life expectancy:		
Men		
Retired during the year	24.64	23.5
Retiring within 20 years	45.59	43.8
Women		
Retired during the year	28.37	27.3
Retiring within 20 years	49.82	48.3

These assumptions are equally applicable to all the obligations, irrespective of the origin of their collective bargaining agreements.

The interest rates used to discount post-employment commitments are applied based on the period of each commitment and the reference curve is calculated applying observable rates for high-credit-quality corporate bonds (AA) issued in the Eurozone.

The costs of health care have been measured on the basis of the expected costs of the premiums of the different medical care policies taken out. A 1% variation in the increase in the cost of these premiums would not have a significant impact on the liability recorded at 31 December 2021 and 31 December 2020, nor would it cause a relevant variation in the ordinary financial costs for future years in relation to that recorded in 2021 and 2020.

Other obligations with personnel

Within the framework of the new Strategic Plan 2018-2022, a new long-term incentive plan was implemented for Naturgy executives not included in the plan referred to in Note 11, the aim of which is to align the shareholders' interests, the materialization of the Strategic Plan and the executives' multi-year variable remuneration. This programme replaces the previous scheme, called PREMP, and is linked to the total return earned by the shareholders over the duration of the Strategic Plan, generating a collection right once the annual accounts for 2022 have been approved by the General Meeting, which will be collected in cash. The provision for this commitment at 31 December 2021 totals Euros 6 million (Euros 5 million in 2020).

Other non-current provisions

The movement in other non-current provisions is as follows:

	2021	2020
At 1 January	**115**	**187**
– Appropriations (1)	9	11
– Reversals	(6)	(27)
Transfers and other	(51)	(56)
At 31 December	**67**	**115**

(1) Includes Euros 1 million in 2020, relating to the financial update of provisions.

"Non-current provisions" mainly includes provisions posted to cover obligations deriving mainly from tax claims (Note 17), litigation and arbitration, and other liabilities.

No provision for business contracts was deemed necessary at 31 December 2021 or 2020.

At 31 December 2021, the estimated payment dates for these obligations are Euros 67 million between one and five years (2020: Euros 109 million between one and five years, Euros 6 million between five and ten years and 0 in more than ten years).

Note 13. Borrowings

Set out below is a breakdown of financial liabilities, excluding "Trade and other payables", at 31 December 2021 and 31 December 2020, by nature and category:

At 31.12.2021	Amortised cost	Hedging derivatives	Total
Borrowings from financial institutions	2,372	—	2,372
Derivatives (Note 14)	—	61	61
Other financial liabilities	1	—	1
Non-current borrowings	**2,373**	**61**	**2,434**
Borrowings from financial institutions	402	—	402
Derivatives (Note 14)	—	19	19
Other financial liabilities	—	—	—
Current borrowings	**402**	**19**	**421**
Total	**2,775**	**80**	**2,855**

At 31.12.2020	Amortised cost	Hedging derivatives	Total
Borrowings from financial institutions	2,720	—	2,720
Derivatives	—	108	108
Other financial liabilities	1	—	1
Non-current borrowings	**2,721**	**108**	**2,829**
Borrowings from financial institutions	257	—	257
Derivatives	—	21	21
Other financial liabilities	121	—	121
Current borrowings	**378**	**21**	**399**
Total	**3,099**	**129**	**3,228**

Financial liabilities recognised at fair value at 31 December 2021 and at 31 December 2020 are classified as follows:

	At 31.12.2021				At 31.12.2020			
Financial liabilities	Level 1 (quoted price in an active market)	Level 2 (observable variables)	Level 3 (unobservable variables)	Total	Level 1 (quoted price in an active market)	Level 2 (observable variables)	Level 3 (unobservable variables)	Total
Headging derivatives	—	80	—	80	—	129	—	129
Total	**—**	**80**	**—**	**80**	**—**	**129**	**—**	**129**

The carrying amounts and fair value of the non-current borrowings are as follows:

	Carrying amount		Fair value	
	At 31.12.2021	At 31.12.2020	At 31.12.2021	At 31.12.2020
Bank borrowings, derivatives and other financial liabilities	2,434	2,829	2,439	2,831

The fair value of loans with fixed interest rates is estimated on the basis of the discounted cash flows over the remaining terms of such debt. The discount rates were determined based on market rates available at 31 December 2021 and 31 December 2020 on borrowings with similar credit and maturity characteristics. These valuations are based on the quotation price of similar financial instruments in an official market or on observable information in an official market (Level 2).

The movement in borrowings is as follows:

	Bank borrowings	Derivatives	Other financial liabilities	Total
At 01.01.2020	**1,997**	**106**	**3**	**2,106**
Increase	1,227	24	121	1,372
Decrease	(247)	(1)	(2)	(250)
At 31.12.2020	**2,977**	**129**	**122**	**3,228**
Increase	50	—	—	50
Decrease	(253)	(49)	(121)	(423)
At 31.12.2021	**2,774**	**80**	**1**	**2,855**

The following tables describe borrowings and maturities at 31 December 2021 and 2020, taking into account the impact of derivatives.

	2022	2023	2024	2025	2026	2027 and beyond	Total
At 31 December 2021:							
Fixed	151	280	91	191	91	870	1,674
Floating	270	304	565	40	1	1	1,181
Total	**421**	**584**	**656**	**231**	**92**	**871**	**2,855**

	2021	2022	2023	2024	2025	2026 and beyond	Total
At 31 December 2020:							
Fixed	237	167	291	91	191	961	1,938
Floating	162	785	287	15	40	1	1,290
Total	**399**	**952**	**578**	**106**	**231**	**962**	**3,228**

Setting aside the impact of derivatives on borrowings, fixed-rate debt would amount to Euros 169 million of total borrowings at 31 December 2021 (Euros 321 million at 31 December 2020) and variable-rate debt would amount to Euros 2,606 million at 31 December 2021 (Euros 2,778 million at 31 December 2020).

The following tables describe the gross borrowings denominated in foreign currencies at 31 December 2021 and 31 December 2020 and their maturities, taking into account the impact of the derivative hedges:

	2022	2023	2024	2025	2026	2027 and beyond	Total
At 31 December 2021:							
Euro debt	421	584	656	231	92	871	2,855
Total	**421**	**584**	**656**	**231**	**92**	**871**	**2,855**

	2021	2022	2023	2024	2025	2026 and beyond	Total
At 31 December 2020:							
Euro debt	399	952	578	106	231	962	3,228
Total	**399**	**952**	**578**	**106**	**231**	**962**	**3,228**

Borrowings bore an average effective interest rate in 2021 of 1.05% (1.03% in 2020) including the derivatives assigned to each transaction.

At 31 December 2021, Bank borrowings includes Euros 8 million in interest pending payment (Euros 9 million at 31 December 2020).

Most of the outstanding financial debt carries a change-of-control clause referring to acquisition of over 50% of the voting stock or of the right to appoint a majority of members of the Board of Directors of Naturgy Energy Group, S.A. Those clauses carry additional conditions so that triggering them depends on some of the following events occurring simultaneously: a significant downgrade of the credit rating due to a change of control, or loss of an investment grade rating; inability to fulfil the financial obligations under the contract; material impairment for the creditor, or a material adverse change in solvency. These clauses would entail repayment of the outstanding debt, although the time period would normally be longer than in the event of early termination.

At the preparation date of these annual accounts, the Company is not in breach of its financial obligations or of any type of obligation that could give rise to the early maturity of its financial commitments.

The most relevant financial instruments are as follows:

Other bank borrowings

The group continues to work on enhancing its financial profile; in this respect, the most relevant financing operations with credit institutions arranged during 2021 have been the refinancing of credit lines in Spain for Euros 3,483 million, which basically includes:

- Refinancing of the undrawn syndicated credit line, increasing the limit from Euros 1,750 million to Euros 2,000 million, with a 3-year maturity (with an option to extend to 2026) at Euribor +0.30% and with ESG metrics in the calculation of the price. In addition, credit lines and bilateral loans were renegotiated for an amount of Euros 1,483 million.

Naturgy also enjoys a comfortable debt maturity profile and balance sheet position, as well as flexibility in its capital expenditure and operating expenses for coping with the current economic scenario.

Institutional financing

The Company records a loan from the Official Credit Institute (ICO) relating to instruments maturing in 2029 at maximum, for a total amount of Euros 160 million (Euros 180 million in 2020).

The European Investment Bank (EIB) has granted financing to Naturgy which at 31 December 2021 is fully drawn down, in the amount of Euros 1,336 million maturing between 2022 and 2037 (Euros 1,564 million drawn down at 31 December 2020). This loan could be subject to early repayment in the event of a change in control, additionally requiring a rating downgrade, and has special debt repayment terms that are longer than those in the event of early termination. In addition, Euros 1,215 million (Euros 1,359 million at 31 December 2020) is subject to compliance with certain financial ratios.

Note 14. Risk management and derivative financial instruments

Risk management

Naturgy has a number of standards, procedures and systems for identifying, measuring and managing different types of risk which are made up of the following basic action principles:

- Guaranteeing that the most relevant risks are correctly identified, evaluated and managed.
- Segregation at the operating level of the risk management functions.
- Assuring that the level of its risk exposure for Naturgy in its business is in line with the objective risk profile.
- Ensuring the appropriate determination and review of the risk profile by the Risk Committee, proposing global limits by risk category, and assigning them to the Business Units.

Interest rate risk

The fluctuations in interest rates modify the fair value of the assets and liabilities that accrue a fixed interest rate and the cash flows from assets and liabilities pegged to a floating interest rate, and, accordingly, affect equity and profit, respectively.

The purpose of interest rate risk management is to balance floating and fixed borrowings in order to reduce borrowing costs within the established risk parameters.

The Company employs financial swaps to manage exposure to interest rate fluctuations, swapping floating rates for fixed rates.

The debt structure at 31 December 2021 and 2020 (Note 13), after taking into account the hedges arranged through derivatives, is as follows:

	At 31.12.2021	At 31.12.2020
Fixed interest rate	1,674	1,938
Floating interest rate	1,181	1,290
Total	**2,855**	**3,228**

The floating interest rate is mainly subject to the fluctuations of the Euribor and the Libor.

The sensitivity of results and equity (measurement adjustments) to interest rate fluctuations is as follows:

	Increase/decrease in interest rates (basis points)	**Effect on profit before tax**	**Effect on equity before tax**
44561	50	(6)	(31)
	-50	6	31
44196	50	(6)	(41)
	-50	6	41

Exchange rate risk

The variations in the exchange rates can affect the fair value of:

- Counter value of cash flows related to the purchase-sale of raw materials denominated in currencies other than local or functional currencies
- Debt denominated in currencies other than local or functional currencies.
- Operations and investments in non-Euro currencies, and, accordingly, the counter value of equity contributed and results.

In order to mitigate these risks the Company finances, to the extent possible, its investments in local currency. Furthermore, it tries to match, whenever possible, costs and revenues indexed in the same currency, as well as amounts and maturities of assets and liabilities arising from operations denominated in non-Euro currencies.

For open positions, the risks in investments in non-functional currencies are managed through financial swaps and foreign exchange fluctuation insurance when its marginal contribution to the risk is relevant and can exceed the risk limits established.

The non-Euro currency with which the Company operates most is the US Dollar. The sensitivity of the Company's profits and equity ("Adjustments for changes in value") to a 5% variation (increase or decrease) in the US dollar/euro exchange rate is as follows:

		2021	2020
Effect on profit before tax	+5%	—	—
	-5%	—	—
Effect on equity before tax	+5%	—	—
	-5%	—	—

Commodity price risk

The Company purchases gas to be supplied to other Naturgy companies.

A large portion of Naturgy's operating expenses are linked to gas purchased to supply customers.

These gas supply contracts are typically signed on a long-term basis with purchase prices based on a combination of different commodity prices, basically crude oil and its derivatives, and natural gas hub prices.

However, sales prices to final customers are usually signed on a short/medium term basis and sales prices are conditioned by the supply-demand balance that exists at any given time in the gas market. This may imply a decoupling with gas supply prices, e.g. in periods of gas oversupply.

Therefore, Naturgy is exposed to the risk of variation in the price of gas with respect to the selling price of end customers. Exposure to these risks is managed and mitigated by natural hedging through the monitoring of the position with respect to these commodities, trying to balance the prices of purchase and supply obligations and sales prices. In addition, some supply contracts allow this exposure to be managed through volume flexibility and price review mechanisms.

When it is not possible to achieve natural hedging, the position is managed, within reasonable risk parameters, by contracting derivatives to reduce exposure to price decoupling risk, generally designated as hedging instruments.

In the integrated electricity businesses, the company's aggregate exposure is determined by the strategic positioning of generation/commercialisation and by the final sales pricing policies in electricity commercialisation.

Finally, the company is exposed to the evolution of the price of CO_2 emission rights, intended for generation in its combined cycle plants. Conjuncturally, Naturgy invests part of its cash surpluses in CO_2-linked notes.

Naturgy has no relevant investments in upstream businesses or commodities production.

Business segment sensitivity to the prices of oil, gas, coal and electricity is explained below:

- Gas and electricity distribution. It is a regulated activity with revenue and profit margins are linked to distribution infrastructure management services rendered, irrespective of the prices of the commodities distributed. In any event, a fall in the price of gas could increase consumption, having a favourable impact on revenue and thus contributing to the stability of Naturgy's results.

- Gas and electricity. Profit margins on gas and electricity supply activities are directly affected by commodity prices. In this regard, Naturgy has a risk policy that stipulates the tolerance range, based on applicable risk limits, among other aspects. Measures employed to keep risk within the stipulated limits include active supply management, balanced acquisitions and sales formulae, and specific hedging so as to maximise the risk-profit relationship. Additionally to that policy, a large portion of Naturgy’s supply portfolio has mechanics, through clauses, to review prices both ordinary and extraordinary. In the medium-term, those clauses allow to modulate the potential impacts of imbalances between sale prices in Naturgy’s markets and prices of the supply portfolio.

Credit risk

Credit risk is defined as the potential loss resulting from the possible nonfulfillment of the contractual obligations of counterparties with which Naturgy does business.

Naturgy performs solvency analyses on the basis of which credit limits are assigned and any necessary provisions are determined. Based on these models, the probability of customer default can be measured and the expected commercial loss can be kept under control. In addition, credit quality and portfolio exposure are monitored on a recurring basis to ensure that potential losses are within the limits provided for by internal regulations. This allows a certain capacity to anticipate events in credit risk management.

Credit risk relating to trade receivables is reflected in the balance sheet net of provisions for bad debts (Note 9), estimated by the Company on the basis of the ageing of the debt and past experience in accordance with the prior segregation of customer portfolios and the current economic environment.

Credit risk relating to trade accounts receivable is historically limited given the short collection periods of customers that do not individually accumulate significant amounts before supply can be suspended due to non-payment, in accordance with applicable regulations.

With respect to other exposures to counterparties in transactions involving financial derivatives and the investment of cash surpluses, credit risk is mitigated by carrying out such operations with reputable financial institutions in line with internal requirements. No significant defaults or losses arose in 2021 or 2020.

The ageing analysis of financial assets concluded that there were no unimpaired, past due financial assets at 31 December 2021 and 2020.

The aging analysis of financial assets and their expected loss as of 31 December 2021 and 31 December 2020 is as follows:

31.12.2021	**Total**	**Current**	**0 to 180 days**	**180 to 360 days**	**Over 360 days**
Expected loss ratio	32.5 %	—	—	—	100.0 %
Trade receivables for sales and services	83	56	—	—	27
Expected loss	27	—	—	—	27

31.12.2020	**Total**	**Current**	**0 to 180 days**	**180 to 360 days**	**Over 360 days**
Expected loss ratio	43.1 %	—	—	—	100.0 %
Trade receivables for sales and services	65	37	—	—	28
Expected loss	28	—	—	—	28

The impaired financial assets are broken down in Note 9.

Concerning supplier credit risk, the solvency of each supplier of products and services is guaranteed through the recurring analysis of their financial information, particularly prior to new engagements. To this end, the relevant assessment criteria are applied depending on the supplier's criticality in terms of service or concentration. This procedure is supported by control mechanisms and systems and supplier management.

At 31 December 2021 and 2020 the Company did not have significant concentrations of credit risk.

Liquidity risk

The Company has liquidity policies that ensure compliance with its payment commitments, diversifying the coverage of financing needs and debt maturities. A prudent management of the liquidity risk includes maintaining sufficient cash and realisable assets and the availability of sufficient funds to cover credit obligations.

At 31 December 2021, available cash totalled Euros 7,484 million (Euros 7,930 million in 2020), considering cash and cash equivalents of Euros 2,208 million (Euros 2,618 million in 2020) together with bank borrowings and undrawn credit facilities amounting to Euros 5,276 million (Euros 5,312 million in 2020).

Capital management

The main purpose of the Company’s capital management is to ensure a financial structure that can optimise capital cost and maintain a solid financial position, in order to combine value creation for the shareholder with the access to the financial markets at a competitive cost to cover financing needs.

Naturgy considers a long-term leverage level of approximately 50% as an indicator of the capital management objectives.

The Company's long-term credit rating is as follows:

	2021	2020
Standard & Poor’s	BBB	BBB
Fitch	BBB	BBB

Other considerations

On 23 June 2016 UK voters supported the departure of their country from the European Union in a national referendum (“Brexit”). On 31 January 2020 the United Kingdom left the European Union and a transitional period began until 31 December of that same year. On 30 December 2020 the European Union and the United Kingdom signed a Trade and Cooperation Agreement with provisional entry into force on 1 January 2021.

The Brexit process has had and is likely to continue to have adverse effects on the economic and political situation of the EU and the stability of international financial markets. Without considering the aforementioned impact at international level, Naturgy's exposure to the risk derived from the Brexit is not considered significant.

Derivative financial instruments

The breakdown of derivative financial instruments by category and maturity is as follows:

	At 31.12.2021		At 31.12.2020	
	Assets	**Liabilities**	**Assets**	**Liabilities**
Hedging derivative financial instruments	**—**	**61**	**—**	**108**
Cash flow hedge				
- Interest rate		38		81
- Interest rate and foreign exchange rate		23		27
Other financial instruments	**231**	**232**	**136**	**136**
- Price of commodities	231	232	136	136
Derivative financial instruments – non current	**231**	**293**	**136**	**244**
Hedging derivative financial instruments	**—**	**19**	**—**	**142**
Cash flow hedge				
- Interest rate	—	19	—	21
- Exchange rate	—	—	—	—
- Price of commodities	—	—	—	121
Other financial instruments	**1,865**	**1,873**	**123**	**123**
- Price of commodities	1,865	1,873	123	123
- Exchange rate	—	—	—	—
Derivative financial instruments - current	**1,865**	**1,892**	**123**	**265**
Total	**2,096**	**2,185**	**259**	**509**

Other financial instruments include the derivatives not qualifying for hedge accounting.

The impact on the Income statement of derivative financial instruments is as follows:

	2021		2020	
	Operating profit	**Net financial income/ (expense)**	**Operating profit**	**Net financial income/ (expense)**
Cash flow hedge	—	(19)	—	(17)
Other financial instruments	(6)	—	1	(1)
Total	**(6)**	**(19)**	**1**	**(18)**

The breakdown of derivatives at 31 December 2021 and 2020, their fair value and maturities of their notional values is as follows:

	At 31.12.2021							
	Fair value	Notional value						
		2022	2023	2024	2025	2026	Subsequent years	Total
INTEREST RATE HEDGES:								
Cash flow hedges:								
Financial swaps (EUR)	(57)	91	191	70	498	48	527	1,425
INTEREST RATE AND FOREIGN EXCHANGE RATE HEDGES:								
Cash flow hedges:								
Financial swaps (NOK)	(23)	—	101	—	—	—	—	101
EXCHANGE RATE HEDGES:								
Cash flow hedges:								
Foreign exchange insurance (USD)	—	—	—	—	—	—	—	—
Fair value hedges:								
Foreign exchange insurance (USD)	—	9	—	—	—	—	—	9
PRICE OF COMMODITIES HEDGES:								
Cash flow hedges:								
Price of commodities Derivatives (EUR)	—	—	—	—	—	—	—	—
OTHER:								
Foreign exchange insurance (USD)	(9)	—	—	—	—	—	—	—
	(89)	**100**	**292**	**70**	**498**	**48**	**527**	**1,535**

	At 31.12.2020							
	Fair value	Notional value						
		2021	2022	2023	2024	2025	Subsequent years	Total
INTEREST RATE HEDGES:								
Cash flow hedges:								
Financial swaps (EUR)	(102)	63	91	191	70	498	576	1,489
INTEREST RATE AND FOREIGN EXCHANGE RATE HEDGES:								
Cash flow hedges:								
Financial swaps (NOK)	(27)	—	—	101	—	—	—	101
EXCHANGE RATE HEDGES:								
Cash flow hedges:								
Foreign exchange insurance (USD)	—	33	—	—	—	—	—	33
Fair value hedges:								
Foreign exchange insurance (USD)	—	—	—	—	—	—	—	—
PRICE OF COMMODITIES HEDGES:								
Cash flow hedges:								
Price of commodities Derivatives (EUR)	(121)	1,228	—	—	—	—	—	1,228
OTHER:								
Foreign exchange insurance (USD)	—	—	—	—	—	—	—	—
	(250)	**1,324**	**91**	**292**	**70**	**498**	**576**	**2,851**

Note 15. Payables to Group companies and associates

The breakdown by maturity of payables to Group companies is as follows:

Maturity	At 31.12.2021	At 31.12.2020
2021	—	2,560
2022	4,823	1,451
2023	629	625
2024	1,619	1,604
2025	1,197	1,196
2026	1,591	1,589
2027	1,488	989
Subsequent years	2,586	2,076
Total	**13,933**	**12,090**

Payables to Group companies mainly relate to issuances carried out by Naturgy Capital Markets, S.A. and Naturgy Finance, B.V. under the European Medium-Term Notes (EMTN) programme. The balances payable to Naturgy Finance, B.V. in respect of perpetual subordinated debentures amounting to Euros 1,500 million (Euros 1,500 million 2019) and to Unión Fenosa Preferentes, S.A. relating to preference shares totalling Euros 110 million (Euros 110 million in 2019) are also included.

It also includes accrued unmatured interest of Euros 135 million (Euros 145 million in 2020) and cash-pooling balances with Group companies amounting to Euros 3,429 million are also included (Euros 1,268 million in 2020).

A breakdown of amounts owed to Group companies due to bond issues of Naturgy Finance, B.V. and Naturgy Capital Markets, S.A. is as follows:

At 31 December 2021

Programme/Company	Country	Year formalised	Currency	Programme limit	Drawn-down nominal amount	Available	Issuances per year
Euro Commercial Paper (ECP) programme							
Naturgy Finance B.V.	Netherlands	2010	Euro	1,000	—	1,000	280
European Medium Term Notes (EMTN) programme							
Naturgy Capital Markets, S.A. and Naturgy Finance, B.V.	Netherlands /Spain	1999	Euro	12,000	8,110	3,890	—

At 31 December 2020

Programme/Company	Country	Year formalised	Currency	Programme limit	Drawn-down nominal amount	Available	Issuances per year
Euro Commercial Paper (ECP) programme							
Naturgy Finance B.V.	Netherlands	2010	Euro	1,000	—	1,000	900
European Medium Term Notes (EMTN) programme							
Naturgy Capital Markets, S.A. and Naturgy Finance, B.V.	Netherlands /Spain	1999	Euro	12,000	8,941	3,059	1,150

The bonds issued, in a volume of Euros 8,110 million (Euros 8,941 million at 31 December 2020), as usual in the Euromarket, could be redeemed in advance provided that such a change in control triggers a downgrade of more than two full notches in at least two of the three ratings that it had obtained, and all the ratings fall below investment grade, and provided that the rating agency states that the rating downgrade results from the change in control.

The main movements for the years 2021 and 2020 are:

2021

In 2021 two bonds have matured for a total amount of Euros 831 million and with an average coupon of 4.58%.

In 2021, issues under the Euro Commercial Paper (ECP) programme totalling Euros 280 million were carried out. There were no outstanding issues at 31 December 2021 or 31 December 2020.

In November 2021, Naturgy issued a subordinated perpetual bond for an amount of Euros 500 million, redeemable at the issuer's option from February 2027 and with an annual return of 2.374%. As part of the transaction, a repurchase of Euros 500 million of the amortized subordinated perpetual bonds was repurchased from November 2022. The repurchase price was 104.211% and was determined on the basis of the purchase yield up to the first optional purchase date based on a settlement date of 24 November 2021.

Consequence of the cancellation of the Company's debt with Naturgy Finance B.V. for said repurchase, Euros 22 million have been recorded under the heading “Other financial expenses” of the Net financial income (Note 23).

2020

Issuances in 2020 under this programme were as follows:

Issue	Par value	Maturity	Coupon (%)
April 2020	1,000	2026	1.250
May 2020(*)	150	2029	0.750

(*) Increase issue November 2019

In 2020 two bonds matured for a total amount of Euros 934 million with an average coupon of 5.07%.

In 2020, issues under the Euro Commercial Paper (ECP) programme totalling Euros 900 million were carried out. At 31 December 2020 there were no outstanding issues under the ECP.

Borrowings from group companies and associates accrued an average interest rate of 2.15% in 2021 (2.20% in 2020).

There are no significant differences between the carrying amounts and fair values of Payables to Group companies and associates.

Note 16. Other non-current liabilities and Trade and other payables

The headings “Other non-current liabilities” and “Trade and other payables” at 31 December 2021 and 31 December 2020, classified by nature and category, are as follows:

At 31.12.2021	**At fair value through profit and loss**	**Amortised cost**	**Total**
Derivatives (Note 14)	232	—	232
Other non-current liabilities	**232**	**—**	**232**
Derivatives (Note 14)	1,873	—	1,873
Other liabilities	—	425	425
Trade and other payables	**1,873**	**425**	**2,298**
Total	**2,105**	**425**	**2,530**

At 31.12.2020	At fair value through profit and loss	Amortised cost	**Total**
Derivatives (Note 14)	136	—	136
Other non-current liabilities	**136**	**—**	**136**
Derivatives (Note 14)	123	—	123
Other liabilities	—	338	338
Trade and other payables	**123**	**338**	**461**
Total	**259**	**338**	**597**

Fair value through profit and loss

Financial liabilities recognised at fair value at 31 December 2021 and at 31 December 2020 are classified as follows:

	At 31.12.2021				At 31.12.2020			
Financial liabilities	**Level 1 (quoted price in an active market)**	**Level 2 (observable variables)**	**Level 3 (unobservable variables)**	**Total**	**Level 1 (quoted price in an active market)**	**Level 2 (observable variables)**	**Level 3 (unobservable variables)**	**Total**
Fair value through profit and loss	—	2,105	—	2,105	—	259	—	259
Total	**—**	**2,105**	**—**	**2,105**	**—**	**259**	**—**	**259**

This heading includes gas price operating hedging derivatives amounting to Euros 2,105 million (31 December 2020: Euros 259 million), of which Euros 232 million is classified as non-current (31 December 2020: Euros 136 million) (Note 14).

Amortised cost

The breakdown of this account is as follows:

	At 31.12.2021	At 31.12.2020
Trade payables	259	141
Trade payables, Group companies and associates	103	59
Other payables	12	10
Personnel (outstanding remuneration)	33	18
Public Administrations	18	17
Current tax liabilities (Note 17)	—	93
Total	**425**	**338**

Most payables do not accrue interest and have contractual maturity dates of less than 30 days, in the case of gas purchases and within the legal limits, for other suppliers.

Information on average supplier payment period. Additional Provision 3 "Duty of disclosure" of Law 15/2010/5 July

The average payment period is in accordance with Law 15/2010 on measures to combat late payment in business operations.

Information disclosed under the Resolution of 29 January 2016 of the Institute of Accountants and Auditors concerning the details to be included in the notes to the annual accounts concerning the average supplier payment period is as follows:

	2021	2020
	Amount	**Amount**
Total payments (thousand euro)	615,883	458,021
Total outstanding payments (thousand euro)	13,528	18,284
Average supplier payment period (days) (1)	38	32
Transactions paid ratio (days) (2)	38	32
Transactions pending payment ratio (days) (3)	40	38

(1) Calculated on the basis of amounts paid and pending payment.

(2) Average payment period in transactions paid during the year.

(3) Average age, suppliers pending payment balance.

The accompanying ratios do not include situations that could distort calculations, such as Trade payables, Group companies and associates.

Note 17. Tax situation

Naturgy Energy Group, S.A. is the parent of tax group 59/93, which includes all the companies resident in Spain that are at least 75% directly or indirectly owned by the parent company and that fulfil certain requirements, entailing the overall calculation of the group's taxable income, deductions and tax credits. The tax group for 2021 is analysed in Appendix I.

Corporate income tax is calculated on the basis of economic or accounting profit obtained by application of generally accepted accounting principles, which do not necessarily coincide with taxable profit, understood as taxable income for corporate income tax purposes.

The reconciliation of accounting profit for 2021 and 2020 to taxable income is as follows:

	At 31.12.2021	At 31.12.2020
Accounting profit before tax	**1,635**	**60**
Permanent differences	**(1,772)**	**(184)**
Temporary differences:		
Arising during current year	55	51
Arising in prior years	(46)	(139)
Taxable income	**(128)**	**(212)**

Permanent differences mainly relate to the application of the tax consolidation system and the double taxation exemption for dividends and income derived from the transfer of shares under Article 21 of Law 27/2014 on Corporate Income Tax, which has led to negative permanent differences of Euros 908 million resulting mainly from negative adjustments for dividends accruing during the year (Euros 1,271 million in 2020), the impairment of shareholdings in Group companies and associates amounting to Euros 868 million (Euros 1,080 million in 2020) and the upward adjustment for donations and other minor adjustments amounting to Euros 4 million.

In 2021 the Company recorded a tax loss of Euros 128 million (Euros 212 million in 2020), which is recovered from the tax group companies due to the taxable income generated by them during the year.

Income tax expense is as follows:

	2021	2020
Current-year tax	58	60
Deferred tax	13	(22)
Total	**71**	**38**

Current corporate income tax is the result of applying a 25% tax rate to taxable income. In the tax group, tax credits applied in 2021 amounted to Euros 26 million (Euros 4 million in 2020) and no tax losses were offset.

In 2021 there were no adjustments for tax differences from the previous year (Euros 4 million negative adjustment in 2020).

Likewise, other adjustments for provisions for future risks, tax on profits abroad and reversal for final inspection records for a total of 7 million euros are included as a lower expense for current tax in 2020.

On 3 December 2016 Royal Decree-Law 3/2016 was published, adopting tax measures for the consolidation of public finances, which introduced relevant changes in the corporate income tax area. Among other matters, with effect from 1 January 2016 the obligation is laid down to reverse provisions for the impairment of shareholdings that would have been deductible before 2013 in a maximum term of five years, the offsetting of tax losses for large companies is limited to 25% of the preliminary tax base and the application of the tax credit for domestic or international double taxation generated or pending application is restricted to 50% of preliminary gross tax payable. Additionally, effective from 1 January 2017, losses on the transfer of shares will not be deductible. In 2021 and 2020 these measures did not have a significant impact on the Company's financial statements.

On 31 December 2020, Law 11/2020 on the General State Budget for 2021 was published in the Official State Gazette, under which, among other measures, certain articles of Law 27/2014 on Corporate Income Tax were amended. The most relevant amendments relate to the limitation of the exemption of dividends and capital gains such that, with effect from 1 January 2021, only those derived from holdings of more than 5% of share capital will be exempt at 95%, thus eliminating those relating to holdings with an acquisition cost exceeding Euros 20 million (although a transitional regime is established for such holdings).

At the same time, the tax consolidation regime was modified by establishing the non-elimination of dividends distributed between companies in the same Tax Consolidation Group, which entails an effective tax rate of 1.25% for dividends received or capital gains generated in Spanish companies receiving dividends from companies in which a percentage of 5% or more is held, without prejudice to whether the distributing company and the receiving company belong to the same Tax Consolidation Group.

Related to this measure, and for the purposes of calculating the limitation on the deductibility of financial expenses in the case of holding companies in which dividends form part of operating profit, only dividends from entities in which the holding is equal to or greater than 5% will be considered, eliminating from the calculation those dividends from holdings in which the acquisition value of the holding was greater than Euros 20 million.

The General State Budget Law for 2022 approved the modification of Law 27/2014 on Corporation Tax, establishing a minimum taxation of 15% of the tax base. Naturgy does not anticipate that this modification will have an impact on the Group as the deductions applied do not imply a reduction in the effective rate below this percentage.

Income qualifying for the tax scheme for transfers of assets made in compliance with competition law (Additional Provision 4 of the Revised CIT Act) is explained below:

Year of sale	Amount obtained on the sale	Amount reinvested	Capital gain	Capital gain included in tax base	Capital gain pending inclusion in tax base
2002	917	917	462	20	442
2003	39	39	20	—	20
2004	292	292	177	9	168
2005	432	432	300	2	298
2006	310	310	226	—	226
2009	161	161	87	—	87
2010	752	752	551	—	551
2011	468	468	394	1	393
2012	38	38	32	—	32
Total	**3,409**	**3,409**	**2,249**	**32**	**2,217**

The reinvestment has been made in fixed assets used in business activities both by the Company and by the other companies in the tax group, pursuant to Article 75 of the Revised CIT Act.

A breakdown of the tax effect of each item on the Statement of Recognised Income and Expenses is as follows:

	At 31.12.2021			At 31.12.2020		
	Gross	**Tax effect**	**Net**	**Gross**	**Tax effect**	**Net**
Cash flow hedges	(46)	11	(35)	21	(5)	16
Actuarial gains and losses and other adjustments	(22)	5	(17)	(2)	1	(1)
	(68)	**16**	**(52)**	**19**	**(4)**	**15**

A breakdown of deferred taxes is as follows:

	At 31.12.2021	At 31.12.2020
Deferred tax assets:	173	193
- Non-current	162	180
- Current	11	13
Deferred tax liabilities:	(250)	(211)
- Non-current	(250)	(211)
Net deferred tax	**(77)**	**(18)**

Movements and breakdown of deferred asset accounts are as follows:

Deferred tax assets	**Provisions**	**Tax credits**	**Valuation of assets and financial instruments**	**Goodwill**	**Other**	**Total**
At 1.1.2020	**121**	**4**	**21**	**12**	**19**	**177**
Creation (reversal)	(4)	—	—	(1)	(17)	(22)
Movements linked to equity adjustments	(1)	—	5	—	—	4
Transfers and other	—	34	—	—	—	34
At 31.12.2020	**116**	**38**	**26**	**11**	**2**	**193**
Creation (reversal)	3	—	—	(1)		2
Movements linked to equity adjustments	(5)	—	(11)	—	—	(16)
Transfers and other	(5)	—	—	—	(1)	(6)
At 31.12.2021	**109**	**38**	**15**	**10**	**1**	**173**

Deferred tax liabilities	**Differences Depreciation**	**Deferred gains**	**Other**	**Total**
At 1.1.2020	**2**	**207**	**2**	**211**
Creation (reversal)	—	—	—	—
Movements linked to equity adjustments	—	—	—	—
Transfers and other	—	—	—	—
At 31.12.2020	**2**	**207**	**2**	**211**
Creation (reversal)	—	—	(11)	(11)
Movements linked to equity adjustments	—	—	—	—
Transfers and other	—	—	50	50
At 31.12.2021	**2**	**207**	**41**	**250**

In 2015, the demerger of the thermal and hydraulic power generation business from the Company to Naturgy Generación, S.L.U. was completed. Pursuant to Article 76.3 of Law 27/2014 on corporate income tax in force in 2015, this operation was defined as a non-cash contribution of a line of business and was thus subject to the special scheme provided by Title VII, Chapter VIII of that law. The information requirements stipulated in the special tax scheme are fulfilled in the notes to the Company's 2015 annual accounts.

In 2014, the demerger of the thermal and hydraulic power generation business from the Company to Naturgy Generación, S.L.U. was completed. Pursuant to Article 83.3 of Royal Decree-Law 4/2004 whereby the Revised CIT Act was approved, this operation is defined as a non-cash contribution of a line of business and is thus subject to the special scheme provided for in Title VII, Chapter VIII of said Act. The information requirements stipulated in the special tax scheme are fulfilled in the notes to the Company's 2014 annual accounts.

In 2009, the companies Unión Fenosa, S.A. and Unión Fenosa Generación S.A. were merged into the Company under the special tax scheme for mergers, spin-offs, asset contributions, share exchanges and changes of registered address of European companies or European cooperatives from one European Union Member State to another, provided by Title VII, Chapter VIII of the Revised CIT Act. The information requirements stipulated in the special tax scheme are fulfilled in the notes to the Company's 2009 annual accounts.

In July 2021 tax inspection proceedings were instigated against the Company as the parent company of Group 59/93 in relation to corporate income tax and as the parent company of Group 273/08 with respect to VAT. These proceedings are partial in nature in both taxes, the object of the verification being limited to certain aspects of the tax obligation. The periods under inspection for corporate income tax purposes (tax consolidation regime) are 2016 to 2019 and for VAT purposes (corporate group regime) from September 2017 to December 2020.

This notification interrupts the limitation period for assessing the taxes for the periods mentioned above with respect to the entire tax group for corporate income tax purposes and the VAT Group for VAT purposes.

In addition, within the framework of the same inspection procedure the Company was notified of the commencement of verification proceedings, also of a partial nature, in respect of personal income tax, withholdings and payments on account on earned income. The inspection covers periods from September 2017 to December 2020.

The tax inspection proceedings initiated against the Company in July 2018 as the parent company of Group 59/93 in relation to corporate income tax and as the parent company of Group 273/08 with respect to VAT concluded at the end of 2020. The periods under inspection for corporate income tax purposes (tax consolidation regime) were from 2011 to 2015 and for VAT purposes (corporate group regime) from June 2014 to December 2015.

The assessments raised on the conclusion of the proceedings have not had a material impact on the Naturgy companies as the resulting liability had already been provisioned.

As a result of the agreed tax assessments a current tax liability was recognised in 2020 under "Trade and other payables" (Note 16), which has been reversed following the settlements paid in 2021.

The assessments relating to the adjustment to the international double taxation credit were contested, as the company considers that its approach is supported by legal doctrine and case law on this matter. This amount continues to be recognised under "Provisions" (Note 12) and has been restated during 2021 for the late payment interest incurred.

In accordance with Spanish tax legislation, at the date of preparation of these annual accounts, the Company's returns for the last four year for the principal taxes to which it is subject and which are not involved in the above-mentioned tax inspection are open to inspection.

Concerning tax-related appeals, on 30 September 2020 the Spanish National Court handed down a ruling on an appeal against the tax assessments resulting from an inspection on corporate income tax for the periods 2006-2008, which were contested and which basically regularised the tax deduction for export activities. This resolution has been executed during 2021 and the debt provided for under "Provisions" (Note 12) at 31 December 2020 has been repaid during this year.

In addition, the Central Economic-Administrative Court has yet to rule on the appeal filed against the settlements derived from the contested tax assessments relating to the regularisation of the deduction for international double taxation mentioned in previous paragraphs, which is fully provisioned as indicated therein.

As a result, among other things, of the different interpretations to which current tax legislation lends itself, additional liabilities could arise as a result of an inspection. The Company considers, however, that any liabilities that might arise would not significantly affect these annual accounts.

Naturgy has recorded provisions for obligations deriving from a number of tax claims. There are no lawsuits or uncertain tax treatments which are individually significant (Note 12).

Note 18. Revenue

Revenue breaks down as follows:

	2021	2020
Electricity sales	1	—
Natural gas sales and other	801	667
Provision of services	—	1
Income from equity instruments of Group companies and associates (Note 7)	932	1,271
Income from marketable securities and other financial instruments of Group companies and associates	348	353
Total	**2,082**	**2,292**

	2021	2020
Export market:	1,442	1,770
- European Union	640	522
- OECD countries	639	521
- Other countries	1	1
Total	**2,082**	**2,292**

Gas sales are made basically in the domestic market and relate to gas sales to other Naturgy companies.

Note 19. Raw materials and consumables

Includes gas purchases related to the activity of selling gas to other Naturgy companies.

Note 20. Personnel expenses

A breakdown of this heading in the income statement for 2021 and 2020 is as follows:

	2021	2020
Wages and salaries	58	66
Termination benefits	54	32
Social security costs	6	8
Defined contribution plans	1	2
Defined benefit plans (Note 12)	1	1
Share-based payments (Note 11)	3	2
Other	3	4
Total	**126**	**115**

In May 2021, the workers' union representatives and the representatives of Company management adopted a Voluntary Redundancy Plan for the Naturgy Group to be implemented before 31 December 2021. Compensation for termination includes the costs associated with said Voluntary Redundancy Plan corresponding to effective terminations and the agreements confirmed between the parties until 31 December 2021 and which make the commitment irrevocable.

The average number of Company employees in 2021 and 2020 is as follows:

	2021	2020
Executives	34	48
Middle management	105	214
Specialists	172	191
Operational staff	44	74
Total	**355**	**527**

The average number of Company employees during 2021 and 2020 with a disability equal to or greater than 33% is as follows:

	2021		2020	
	Men	**Women**	**Men**	**Women**
Executives	—	—	—	—
Middle management	—	—	1	2
Specialists	3	3	3	1
Operational staff	1	1	1	—
Total	**4**	**4**	**5**	**3**

The number of Company employees at the end of 2021 and 2020 broken down by category and gender is as follows:

	2021		2020	
	Men	**Women**	**Men**	**Women**
Executives	26	6	29	8
Middle management	42	39	96	68
Specialists	68	73	65	82
Operational staff	4	25	8	49
Total	**140**	**143**	**198**	**207**

Note 21. Other operating expenses

A breakdown of this heading in the income statement for 2021 and 2020 is as follows:

	2021	2020
Leases, royalties, operation and maintenance	23	27
Professional services and insurance	17	19
Advertising and other commercial services	12	14
Contribution Naturgy Foundation	5	6
Banking services	6	6
Supplies	7	20
Taxes	2	1
Impairment losses and changes in trade provisions (Note 9)	(1)	(2)
Other	39	79
Total	**110**	**170**

The Company makes contributions to the Naturgy Foundation to enable it to carry out its energy and environmental projects, basically in the community area, as well to fund international initiatives.

In the community area, the Naturgy Foundation has broadened its activities to place greater emphasis on its community initiatives, defining new strategic lines for actions aimed at palliating energy vulnerability.

Note 22. Other operating income

This account includes Euros 71 million in transactions with group companies and associates in 2021 (Euros 149 million in 2020), and basically corresponds to the repercussion of costs incurred.

Note 23. Net financial income/(expense)

The breakdown of this account in the Income statement for 2021 and 2020 is as follows:

	2021	2020
Income from marketable securities and other financial instruments	3	5
Total financial income	**3**	**5**
Cost of borrowings	(313)	(326)
Interest expense on pensions (Note 12)	(2)	(3)
Other financial expense	(34)	(10)
Total financial expense	**(349)**	**(339)**
Variation in fair value of financial instruments	—	1
Net exchange differences	—	(2)
Impairment and gains/(losses) on disposals of financial instruments	(1)	—
Net financial income/(expense)	**(347)**	**(335)**

Other financial expenses include the expenses for the cancellation of the debt associated with the repurchase of bonds from Naturgy Finance, B.V. for an amount of Euros 22 million (Note 15).

Note 24. Foreign currency transactions

Transactions effected in foreign currencies are analysed below, the main currency being the US dollar:

	2021	2020
Sales	401	257
Other operating income	8	—
Income from marketable securities and other financial instruments of Group	16	7
Purchases	(396)	(257)
Services received	(6)	(5)
Financial expenses by borrowings from group companies and associates	(5)	—
Total	**18**	**2**

Note 25. Information on transactions with related parties

The following are related parties for the purposes of this Note:

- Significant Company shareholders, i.e. those directly or indirectly owning an interest of 5% or more, and those who, though not significant, have exercised the power to propose the appointment of a member of the Board of Directors.

  Based on this definition, the significant shareholders of Naturgy are Fundación Bancaria Caixa d'Estalvis i Pensions de Barcelona ("la Caixa"), Global Infrastructure Partners III (GIP) and related companies, CVC Capital Partners SICAV-FIS, S.A. (through Rioja Acquisitions, S.à.r.l.) and IFM Global Infrastructure Fund (IFM) (through IFM Global InfraCo O (2), S.à.r.l.).

- Directors and executives of the Company and their close relatives. The term "director" means a member of the Board of Directors and the term "senior management personnel" refers to personnel reporting directly to the Executive President and the Internal Audit Manager. Operations with directors and senior management personnel are disclosed in Note 26.

- Transactions between Naturgy companies form part of ordinary activities and are effected at arm's length.

The aggregated amounts of operations with significant shareholders are as follows (in thousand Euros):

	2021				2020		
Income and expense (in thousand Euros)	**"la Caixa" group**	**CVC group**	**GIP group**	**IFM Group**	**"la Caixa" group**	**CVC group**	**GIP group**
Receipt of services	1	—	—	—	1	—	—
Total expenses	**1**	**—**	**—**	**—**	**1**	**—**	**—**
Total income	**—**	**—**	**—**	**—**	**—**	**—**	**—**
Other transactions (in thousand Euros)	**"la Caixa" group**	**CVC group**	**GIP group**	**IFM Group**	**"la Caixa" group**	**CVC group**	**GIP group**
Dividends and other profits distributed	319,676	267,142	266,183	42,743	339,625	283,813	282,795

The aggregated amounts of operations with group companies and associates are as follows (in million Euros):

	2021		2020	
Expenses, income and other transactions	**Group companies**	**Jointly-controlled entities and associates**	**Group companies**	**Jointly-controlled entities and associates**
Financial expenses	(303)	—	(292)	—
Lease expenses	(1)	—	(1)	—
Receipt of services	(12)	—	(24)	(1)
Purchases of goods	(419)	—	(353)	—
Total expenses	**(735)**	**—**	**(670)**	**(1)**
Financial income	343	5	350	4
Dividends received	1,639	—	1,355	1
Sale of goods	1,046	—	516	—
Other income	71	—	148	1
Total income	**3,099**	**5**	**2,369**	**6**

In 2021 and 2020, "Purchases of goods" relates mainly to purchases of natural gas from Group companies.

The heading "Dividends received" includes the supplementary dividend payments made against the share premium account and reserves, recorded as a Euros 707 million decrease in investments in group companies (Euros 85 million in 2020) (Note 7).

The heading "Sales of goods" includes sales of natural gas derived from supply contracts, as well as gas commodity settlements passed on to group companies.

The heading "Other income" includes income from services rendered in accordance with the nature and extent thereof (Note 22).

Costs shared between the Company and other Naturgy companies are allocated on the basis of business or cost generation parameters.

Detailed definitions are prepared of services to be provided and of related activities or tasks in order to determine the measurement indicators used to calculate costs allocated. Transactions between companies are objective, transparent, non-discriminatory and always effected at arm's length.

Note 26. Information on Board members and management Committee

Remuneration of the members of the Board of Directors

The remuneration policy for the members of the Board of Directors was approved at the General Shareholders' Meeting held on 9 March 2021 and is periodically revised by the Board of Directors following a report from the Appointments and Remuneration Committee, in order to keep it aligned with the best practices in the reference market and with the objectives indicated in the By-laws.

The amount accrued by the members the Board of Directors of Naturgy Energy Group, S.A., for belonging to the Board of Directors, Audit and Control Committee (ACC), Appointments, Remuneration and Corporate Governance Committee (ARGC) and Sustainability Committee (SC), totalled Euros 3,955 thousand. There is no increase compared to 2020, as the creation of the Sustainability Committee has been compensated by a reduction in the unit amounts of the different committees. The amount for 2021 is detailed below (expressed in euros):

	Office	Board	AC	ARC	SC	Total
Mr. Francisco Reynés Massanet	Executive Chairman	1,100,000	—	—	—	1,100,000
Mr. Ramón Adell Ramón	Coordinating Director	205,000	44,000	66,000	—	315,000
Mr. Enrique Alcántara-García Irazoqui (1)	Director	111,022	—	27,914	—	138,936
Mr. Marcelino Armenter Vidal (2)	Director	62,567	—	15,731	—	78,298
Mr. Francisco Belil Creixell	Director	175,000	66,000	44,000	—	285,000
Ms. Lucy Chadwick	Director	175,000	44,000	—	44,000	263,000
Ms. Helena Herrero Starkie	Director	175,000	44,000	—	66,000	285,000
Ms. Isabel Estapé Tous	Director	175,000	44,000	—	44,000	263,000
Mr. Rajaram Rao	Director	175,000	—	44,000	—	219,000
Rioja S.à.r.l, Mr. Javier de Jaime Guijarro	Director	175,000	—	44,000	—	219,000
Mr. Pedro Sainz de Baranda Riva	Director	175,000	44,000	44,000	—	263,000
Mr. Claudi Santiago Ponsa	Director	175,000	—	44,000	44,000	263,000
Theatre Directorship Services Beta, S.à.r.l., Mr. José Antonio Torre de Silva López de Letona	Director	175,000	44,000	—	44,000	263,000
		3,053,589	**330,000**	**329,645**	**242,000**	**3,955,234**

(1) Since 13 May 2021
(2) From 9 May 2021

In 2021, as in 2020, no amounts were received for other items.

At 31 December 2021, the Board of Directors comprised 12 members, the Audit and Control Committee had 7 members, the Appointments, Remuneration and Corporate Governance Committee had 7 members and the Sustainability Committee had 5 members.

The members of the Board of Directors of Naturgy Energy Group, S.A., excluding the Executive Chairman, have not received remuneration from profit sharing, bonuses or indemnities, and have not been granted any loans or advances. Neither have they received shares or share options during the year, nor have they exercised options or have options to be exercised.

The members of the Board of Directors are covered with the same liability policy that insures all managers and directors of Naturgy. The premium paid in 2021 by Naturgy Energy Group, S.A. amounted to Euros 614 thousand (Euros 316 thousand in 2020).

Management Committee Remuneration

For the sole purposes of the information contained in this section, the Management Committee is considered to be the Executive Chairman in relation to his executive functions, the directors reporting directly to the Executive Chairman and the Internal Audit Director.

At 31 December 2021, 9 persons make up this group, excluding the Executive Chairman and the Internal Audit Director (9 persons at 31 December 2020). During 2021 there have been no movements in the Management Committee.

Amounts accrued by the Management Committee in respect of fixed remuneration, annual variable remuneration and other items totalled Euros 10,311 thousand in 2021 (Euros 5,106 thousand, Euros 4,997 thousand and Euros 208 thousand, respectively) and Euros 11,408 thousand in 2020 (Euros 6,130 thousand, Euros 4,752 thousand and Euros 526 thousand, respectively). As in 2020, the amount corresponding to the annual variable remuneration of the Executive Chairman will be paid as a voluntary contribution to the social security plan of which he is the beneficiary, in accordance with the provisions of the contract.

At 31 December 2021, the Management Committee has received for the extension of the current ILP, described in Note 11, the amount of Euros 831 thousand (as of 31 December 2020, the Committee did not receive any amount for this concept).

Contributions to pension plans and group insurance policies, together with life insurance premiums paid, totalled Euros 1,458 thousand in 2021 (Euros 1,601 thousand in 2020). The funds accrued for these contributions, including in the case of the Executive Chairman the amounts contributed voluntarily since 2018 together with the annual variable remuneration accrued in 2021 which will be settled as a contribution to a pension plan, amount to Euros 16,916 thousand at 31 December 2021 (Euros 13,112 thousand at 31 December 2020).

In 2021, as in 2020, Naturgy has not provided any new guarantees for loans to senior management personnel. No indemnities were received for departures from the Management Committee in 2021 (Euros 14,261 thousand in 2020).

The Chairman's contract was approved by the Board of Directors on 6 February 2018 and provides for a fixed remuneration component, an annual variable component and a long-term incentive plan, as well as other welfare benefits.

At a meeting held on 31 July 2018 the Board of Directors approved a long-term variable incentive plan (LTI) in which the Executive Chairman and other senior executives take part, the main characteristics of which are described in Note 11.

The Chairman's contract provides for an indemnity in the event of the termination or non-renewal of his directorship amounting to two years' total remuneration: total fixed remuneration, annual variable remuneration and the annualised part of long-term remuneration (equivalent to 1.25 times the total fixed remuneration). The indemnity will not be payable in the event of the serious and culpable nonfulfillment of his professional obligations causing significant harm to Naturgy's interests. In addition, as consideration for a post-contractual no-competition agreement with a duration of one year, an indemnity equivalent to one year's full fixed remuneration is provided for.

The contracts concluded with the members of the Management Committee (9) contain a clause providing for termination benefits equivalent to the legally established severance payment, which varies, depending on seniority, between two and three and a half years' salary. This clause applies to cases of unfair dismissal, as well as those referred to in Articles 40, 41 or 50 of the Workers' Statute and in one of the contracts for certain situations of change of control . In addition, the 9 contracts contain a clause providing for compensation equivalent to one year's fixed remuneration for a post-contractual non-competition commitment lasting up to two years.

Transactions with members of the Board of Directors and the Management Committee

The Directors have the obligation to avoid conflicts of interest as established by the Board Regulations of Naturgy Energy Group, S.A. and Articles 228 and 229 of the Spanish Companies Law. Additionally, these articles require that conflicts of interest incurred by the board shall be reported in the annual accounts.

In 2021 the Directors of Naturgy Energy Group, S.A. have not notified the Board of Directors of any general situation of conflict of interest.

During 2020, at two meetings of the Board of Directors, two directors abstained from taking part as certain inorganic investments where there was a conflict of interest with Naturgy were discussed. Apart from these cases, in 2021 the Directors of Naturgy Energy Group, S.A. have not notified the Board of Directors of any general situation of conflict of interest.

In transactions with related parties (significant shareholders) that have been submitted for approval by the Board, subject to a favourable report of the Audit Committee, any directors linked to the related party involved have abstained.

During 2021 and 2020, the members of the Board of Directors and the Management Committee have not carried out related-party transactions outside the ordinary course of business or transactions that have not been conducted under normal market conditions with Naturgy Energy Group, S.A. or Group companies.

Note 27. Contingent liabilities and commitments

Guarantees

Guarantees furnished by Naturgy at 31 December 2021 and 2020 are as follows:

- Guarantees provided to third parties, basically for investment commitments of Group companies, amounting to Euros 23 million (Euros 34 million at 31 December 2020).
- Guarantees to group companies Naturgy Capital Markets, S.A., Naturgy Finance, B.V. and Unión Fenosa Preferentes, S.A.U., for debt issuances carried out by them totalling Euros 9,720 million (Euros 10,551 million at 31 December 2020).
- Guarantees to group companies Naturgy Aprovisionamientos, S.A. and Gas Natural Europe, S.A.S for obligations under the gas purchase and transport contracts and gas tanker chartering agreements.

In 2020 the following guarantees provided by the Company were cancelled:

- Guarantees relating to the economic obligations resulting from its participation in the Spanish electricity system (MEFF and OMIE) for Euros 19 million.
- Guarantee for compliance with obligations under the administrative concession granted for USD 7 million (Euros 6 million) and guarantees for compliance with loan obligations relating to investee companies amounting to USD 78 million (Euros 69 million), cancelled as the obligation ceased to exist due to the assignment to other Naturgy Group companies.

As the above guarantees are basically granted in order to guarantee the fulfilment of contractual obligations or investment commitments, the events that would lead to their execution, and therefore a cash disbursement, would be the nonfulfillment by Naturgy of its obligations in the ordinary course of its business, the probability of which is considered remote. Naturgy estimates that the liabilities not foreseen at 31 December 2021 if any, that could arise from guarantees furnished would not be significant.

Contractual commitments

At 31 December 2020, the Company was party to several gas supply contracts with “take or pay” clauses negotiated for “own use” (Note 3.5), by virtue of which it had gas purchase rights for the period 2021 - 2024 in the amount of Euros 547 million, calculated on the basis of natural gas prices at 31 December 2020. These commitments have been cancelled during 2021.

Operating lease commitments break down as follows:

	2021	2020
Up to one year	18	17
Between 1 and 5 years	68	69
Between 5 and 10 years	28	42
	114	**128**

In 2021 this mainly includes operating leases without purchase options on six properties, as detailed below:

Property	**Situation**	**Maturity contract**	**Extension contract**
Avda San Luis, 77	Madrid	2026	5 years
Acanto, 11-13	Madrid	2026	5 years
Calle Lérida	Madrid	2027	5 years
Avda América,38	Madrid	2030	2 periods of 5 years
Can Ametller	Sant Cugat del Valles (Barcelona)	2022	—
Diagonal, 525	Barcelona	2031	2 periods of 5 years

Contingent liabilities for litigation and arbitration

The Company is involved in certain judicial and extrajudicial disputes within the ordinary course of its activities. At the date of preparation of these annual accounts, the main litigation or arbitration in which the Company is involved are the following:

Qatar Gas arbitration

In 2021, the arbitration on prices for gas supplies for the 2015-2017 period was resolved and an agreement was reached on the arbitration procedure that had been initiated for the 2018-2020 period.

Unión Fenosa Gas

In 2014, Egyptian Natural Gas Holding (EGAS), an Egyptian public company, ceased to supply gas to Unión Fenosa Gas, a company 50% owned by Naturgy at the time, and stopped paying the utilisation fee for the Damietta liquefaction plant. This led to Unión Fenosa Gas instigating arbitration proceedings at various locations (Madrid, El Cairo and the ICSID) against this supplier, which requested the nullity of the contract, and against the Arab Republic of Egypt. In December 2017 the arbitration proceedings against EGAS conducted in Cairo concluded with a decision that confirmed the position of Unión Fenosa Gas concerning the nonfulfillment of the relevant obligations. In August 2018 a decision was made in the investment protection arbitration proceedings (ICSID) against the Arab Republic of Egypt, ordering it to pay USD 2,013 million after taxes and before interest, pending resolution of the arbitration based in Madrid. On 21 December 2018, the Arab Republic of Egypt submitted an appeal to the ICSID against the award and requested its suspension while the appeal proceedings last. In January 2020, as Egypt had not provided the guarantees established by ICSID, the suspension that had been provisionally decreed was lifted and enforcement actions were resumed, with the award having been approved in the United Kingdom and the Netherlands.

In December 2020, Naturgy announced an agreement with ENI and the Arab Republic of Egypt to amicably resolve disputes affecting Unión Fenosa Gas, with the execution of the arbitration award suspended while said conditions were met.

As described in Note 7, in March 2021, Naturgy, ENI and the Arab Republic of Egypt completed the agreement reached on 1 December 2020 to amicably resolve the disputes affecting UFG. As a result, UFG received a number of cash payments and the majority of assets outside Egypt, excluding UFG's commercial activities in Spain. This also entailed the end of the gas supply contract for approximately 3.5 bcm per year to supply combined cycle plants in Spain, which was due to end in 2029 while maintaining its contract with Oman that expires in 2025. As a result of the agreement, Naturgy acquired an additional 50% stake in UFG, with the result that it now owns 100%, having gained control and fully consolidated that company. Additionally, impairment recognised on this holding, corresponding to the valuation of the pre-existing 50% stake in Unión Fenosa Gas, S.A., was reversed.

Energy subsidy (“bono social”)

The Supreme Court ordered reimbursement of the amounts contributed by Naturgy Energy Group, S.A. to the energy subsidy for 2014 to 2016 (Euros 74 million) in accordance with Royal Decree-Law 9/2013. However, this decision was appealed against by the government before the Constitutional Court. After a sentence of the Constitutional Court of 2020 and another of the Court of Justice of the European Union of 2021, the Supreme Court has confirmed its initial sentence.

At 31 December 2021, the balance sheet includes provisions for litigation based on the best estimate made using the information available at the date of preparation of these annual accounts on their progress and ongoing negotiations, which cover the estimated risks. The Company therefore considers that no significant liabilities will be derived from the risks described in the relevant section of this Note.

Note 28. Auditors’ fees

The Company’s auditor until 31 December 2020 was Ernst & Young, S.L. Since 1 January 2021, the Company's auditor has been KPMG. The fees payable to these companies in 2021 and 2020 were as follows:

	2021			2020		
	KPMG Auditores, S.L	**Rest KPMG network**	**Total**	**Ernst & Young, S.L.**	**Rest EY network**	**Total**
Auditing services	565	—	**565**	696	—	696
Assurance services and services related to the audit (1)	131	—	**131**	55	—	55
Tax services (2)	—	92	**92**	—	—	—
Other services (2)	15	127	**142**	127	—	127
Total fees	**711**	**219**	**930**	**878**	**—**	**878**

(1) Includes in 2021 the limited reviews of interim financial statements and fees related to the issuance of securities provided by KPMG Auditores, S.L. and Rest KPMG network.

(2) Fiscal year 2020 tax services have been reclassified for comparative purposes.

Note 29. Environment

Environmental actions

Naturgy is aware of its activities' environmental impacts and therefore the company pays particular attention to the protection of the environment and the efficient use of natural resources to meet energy demand.

As established in the Corporate Responsibility Policy, Naturgy is committed to promoting the sustainable development of society by ensuring the supply of competitive, safe energy with the maximum respect for the environment.

Naturgy only understands its business in the context of a commitment to sustainability, materialized in the company's Sustainability Plan in the form of specific, ambitious and measurable targets. This plan, whose main lines contribute to the SDGs established by the United Nations, is the backbone of the new Strategic Plan 2021-2025.

Climate change is the great global challenge of the 21st century; to face it, it is vital to transform the energy sector. Naturgy views the energy transition as a real opportunity, as reflected in the new Strategic Plan. This is evident in the company's commitment to achieving carbon neutrality by 2050, at the latest, by reducing total scope 1, 2 and 3 GHG emissions in accordance with the 1.5ºC - 2ºC pathways under the Paris Agreement, in line with the principles of a just transition. To this end, the bulk of investments will be concentrated in activities that are eligible under the EU Taxonomy:

- New renewable generation facilities, with the objective of reaching close to 60% of installed capacity by 2025.
- Carbon-neutral renewable gases, driving new projects with a target of injecting at least 1 TWh into the gas grids by 2025.
- Smart adapted energy grids to play a key role in the energy transition.

Protecting biodiversity, as part of the climate change problem, is another strategic priority of the new Plan

Although the "The Opportunity of Environmental Challenges" chapter in the Sustainability Report and Non-Financial Information Statement 2021 contains detailed information on the company's environmental management performance and results, the main milestones are summarized below.

Governance and environmental management

- Approval of a new Sustainability Plan 2021-2025 that reinforces the company's ambition in the transformation towards sustainability and contains more ambitious environmental targets.

- Continuous improvement and environmental performance metrics are based on concrete, ambitious targets that are measured and audited within the framework of the ISO 14001-certified environmental management system and are made public to meet the organisation's commitment to transparency. In 2021, 93.1% of EBITDA came from industrial activities whose environmental management is certified under the ISO 14001 standard, which involves passing external audits each year.

- Naturgy was recognized by CDP as part of its A-list for water management, and received an A- rating for its climate management, in 2021, placing it in the top range in both indexes.

- "Ejemplos Empresariales de Acciones #PorElClima2020" diploma from the #PorElClima Community for the company's initiative on Biomethane, circular energy for the climate and demographic challenge.

- The renewable gas project at the Butarque WWTP was a finalist in the 'Green Generation' category in the first edition of the Retina ECO Awards, organized by El País and Capgemini.

Climate change and energy transition

- In the new Strategic Plan through 2025, Naturgy announced a commitment to achieve climate neutrality by 2050 (net zero emissions).

- In 2021, 562 MW of new renewable plant (wind and photovoltaic) were commissioned worldwide, increasing renewable installed capacity to 33%. These new facilities contribute to the decarbonization of Naturgy's generation mix.

- Renewable gases (biomethane and hydrogen) are the key lever for decarbonizing Naturgy's gas business. In 2021, the company participated in biomethane projects and attained a production or grid injection capacity of 0.14 TW.

- Improved gas grid management (better monitoring, maintenance, improved materials, etc.) resulted in a 2% reduction in the methane leakage rate compared to the previous year.

- Commercialization of ECO tariffs and products in Spain, based on guarantees of origin, to provide customers with energy from renewable sources. In 2021, this represented 34% of the electricity supplied in the free market. Additionally, in 2021, the Gas Neutro product, i.e. natural gas whose CO_2 emissions have been offset, was applied to all new gas customers.

Circular economy

- The process of replacing hazardous chemicals with others that are more environmentally friendly is ongoing. An example is the replacement, at Spanish hydroelectric power plants, of mineral oils with other biodegradable and environmentally friendly oils.

- Encouragement to customers to opt for electronic invoicing to eliminate paper consumption and the pollution associated with its life cycle. Naturgy's online invoicing expanded considerably; at the end of 2021, 4.2 million contracts in Spain had online invoicing, i.e. 41% of the total, which represents an estimated saving of more than 390 tons of paper per year. The measure is also being implemented in Chile, where more than 200,000 paper invoices were eliminated between January and October.

- Worldwide water consumption was reduced by 24% in 2021. The largest reduction (75%) was in the use of inland fresh water, mainly because the coal-fired power plants that were decommissioned in 2020 used mostly river water. This improvement means a reduction of negative environmental impacts, due to reduced use of the most sensitive resource (fresh water). This trend is replicated in areas of high water stress, where there is greater competition for fresh water and where fresh water uptake was cut by 67%.

- Total waste production was cut by 38% year-on-year, mainly in the category of non-hazardous waste due to the non-operation of the coal-fired power plants (which produce ash and slag). Hazardous waste production was reduced by 7%. As for the final destination of the waste, 57% was reused or recycled.

Biodiversity and natural capital

- In 2021, Naturgy undertook numerous actions in the area of natural capital and biodiversity, all with the aim of preventing, reducing or offsetting our impacts so as to advance with our commitment to no net loss of biodiversity and the enhancement of the value of the natural surroundings. Specifically, 302 biodiversity initiatives were implemented worldwide, 25% of them voluntary.

- A total of 145 surveys of the natural environment were carried out, especially in the area of generation (thermal, hydroelectric and wind farms) and electricity distribution facilities, in order to ascertain and monitor the environmental and ecological status of the surroundings. Sampling campaigns were conducted in the environs of thermal and hydroelectric power plants to determine the physicochemical and biological quality of the aquatic environment (rivers, reservoirs, etc.). The most recent surveys confirm that the situation is normal, as it has been over the time series, and conclude that the environmental impact of the facilities that were surveyed is acceptable.

- Environmental restoration actions were taken on 635 hectares of land in 2021. 29% of that area relates to protected areas, habitats or species.

Environmental investment and expenditure

The environmental activities undertaken by the Company in 2021 totalled Euros 1.3 million (Euros 3.9 million in 2020), comprising Euros 0.2 million relating to environmental investment and Euros 1.1 million relating to the costs of environmental management at facilities excluding those derived from the carbon market (Euros 2 million for environmental investments and Euros 1.9 million related to expenses incurred in environmental management at facilities in 2020). Of the investments made, those in new renewable projects stand out, which will contribute to the energy transition and to reducing specific emissions of CO_2 and other atmospheric pollutants.

Finally, referring to possible contingencies, indemnities and other environmental risks that may be incurred by the company, third-party liability insurance policies are in place to cover any damage that might arise.

Emissions

In 2021, total consolidated CO_2 emissions from Naturgy's combined cycle plants and cogeneration subject to regulations governing the European emission trading system totalled 4.9 million tonnes of CO_2 (6 million tonnes of CO_2 in 2020).

Naturgy devises a strategy each year for managing transfers to its CO_2 emission allowance coverage portfolio, acquiring them through its active participation in both the primary and secondary markets.

Note 30. Events after the reporting date

On 3 February 2022, the Board of Directors approved the proposal for the distribution of the Company's net profit for 2021 and retained earnings, which will be submitted to the General Shareholders' Meeting, as described in Note 11.

Apart from this, there have been no significant post-closing events.

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APPENDIX I. NATURGY TAX GROUP COMPANIES

The companies in the Naturgy tax group are as follows:

Naturgy Energy Group, S.A.	Naturgy Future, S.L.U.
Boreas Eólica 2, S.A.	Naturgy Generación Térmica, S.L.U.
Comercializadora Regulada, Gas & Power, S.A.	Naturgy Generación, S.L.U.
Energías Ambientales De Somozas, S.A.	Naturgy Iberia, S.A.
Eòlica Tramuntana, S.L.	Naturgy Informática, S.A.
Europe Mahgreb Pipeline Limited	Naturgy Infraestructuras EMEA, S.L.
Explotaciones Eólicas Sierra De Utrera, S.L.	Naturgy Ingeniería Nuclear, S.L.
Fenosa, S.L.U.	Naturgy Inversiones Internacionales, S.A.
Gas Natural Comercializadora, S.A.	Naturgy LNG GOM, S.L.
Gas Natural Exploración, S.L.	Naturgy LNG, S.L.
Gas Natural Redes GLP, S.A.	Naturgy Nuevas Energías, S.L.U.
Gas Natural Transporte SDG, S.L.	Naturgy Participaciones, S.A.
General de Edificios y Solares, S.L.	Naturgy Renovables Canarias, S.L.U.
Global Power Generation, S.A.	Naturgy Renovables Ruralia, S.L.U.
GPG Ingeniería y Desarrollo de Generación, S.L.U.	Naturgy Renovables, S.L.U.
GPG México Wind, S.L.U.	Naturgy Wind, S.L.
GPG México, S.L.U.	Nedgia Andalucía, S.A.
Holding de Negocios de Gas, S.A.U.	Nedgia Aragón, S.A.
Holding Negocios Electricidad, S.A.	Nedgia Balears, S.A.
Infraestructures Elèctriques de la Terra Alta, S.L.U.	Nedgia Castilla La Mancha, S.A.
JGC Cogeneración Daimiel, S.L.	Nedgia Catalunya, S.A.
La Propagadora del Gas, S.A.	Nedgia Cegas, S.A.
Lignitos de Meirama, S.A.	Nedgia Madrid, S.A.
Naturgy Acciones, S.L.U.	Nedgia Navarra, S.A.
Naturgy Alfa Investments, S.A.U.	Nedgia, S.A.
Naturgy Almacenamientos Andalucía, S.A.	Operación y Mantenimiento Energy, S.A.
Naturgy Aprovisionamientos, S.A.	Parque Eólico Nerea, S.L.
Naturgy Capital Markets, S.A.	Parque Eólico Peñarroldana, S.L.
Naturgy Ciclos Combinados, S.L.U.	Petroleum, Oil & Gas España, S.A.
Naturgy Clientes, S.A.U.	Sagane, S.A.
Naturgy Commodities Trading, S.A.	Societat Eòlica de L'Enderrocada, S.A.
Naturgy Distribución Latinoamérica, S.A.	Tratamiento Cinca Medio, S.L.
Naturgy Electricidad Colombia, S.L.	UFD Distribución Electricidad, S.A.
Naturgy Engineering, S.L.	Unión Fenosa Preferentes, S.A.U.

Naturgy Energy Group. S.A.
2021 Report

DIRECTORS' REPORT

Directors' Report for the year ended 31 December 2021

Contents

1. Main aggregate performances

The main financial aggregates of Naturgy Energy Group, S.A. and their performance are as follows:

	2021	**2020**	**%**
Net turnover	2,082	2,292	(9.2)
Operating profit	1,982	395	401.8
Profit of the year	1,706	98	1,640.8
Shareholders' equity	18,901	18,471	2.3
Net equity	18,858	18,393	2.5
Current liabilities	2,855	3,228	(11.6)

Naturgy Energy Group, S.A., is a company that develops its activity basically through the tendency of other group and associated companies shares, so information bellow refers to Consolidated group of Naturgy (hereinafter, Naturgy).

1.1. Business performance and results

Notes on financial disclosures

– Naturgy's financial disclosures contain magnitudes drafted in accordance with International Financial Reporting Standards (IFRS), and Alternative Performance Metrics (APM), which are viewed as adjusted figures with respect to those presented in accordance with IFRS. The attached appendix in Consolidated Directors' Report contains a definition of the APMs.

Main financial aggregates

	2021	2020	**%**
Net sales	22,140	15,345	44.3
Ebitda	3,529	3,449	2.3
Ebit	2,101	466	350.9
Income attributable to equity holders of the parent	1,214	(347)	(449.9)
Investments	1,484	1,279	16.1
Net borrowings (at 31/12)	12,831	13,612	(5.7)
Free cash flow after non-controlling interests	2,113	1,626	30.0

Key financials & metrics

	2021	2020
Leverage	59.10%	54.70%
Ebitda / Cost of net borrowings	7,2x	6,9x
Net borrowings / Ebitda	3,6x	3,9x

Main stock market ratios and shareholder remuneration

	2021	2020
Total no. of shares ('000)	969,614	969,614
Average no. of shares ('000)[1]	960,935	962,555
Share price at 31/12 (Euros)	28.63	18.9
Market capitalisation at 31/12 (Euros million)	27,760	18,384
Earnings per share (Euros)[1]	1.26	(0.36)
Dividend paid	1,290	1,370

[1] Calculated using the weighted average number of outstanding shares in the year (weighted average number of ordinary shares minus weighted average number of treasury shares).

Main operating aggregates

Distribution	**2021**	2020
Gas distribution (GWh)	459,878	403,910
Electricity distribution (GWh)	36,411	35,536
Gas supply points ('000)	11,037	11,052
Electricity supply points ('000)	4,776	4,727
Gas distribution network (km)	135,640	134,802
Length of electricity transmission and distribution network (km)	153,981	151,495

Gas	**2021**	2020
Supply (GWh)	239,780	181,738
International LNG (GWh)	141,748	133,979
Total gas supply (GWh)	**381,528**	**315,717**

Electricity	**2021**	2020
Thermal installed capacity (MW)	10,674	10,674
Renewable installed capacity (MW)	5,221	4,659
Total installed capacity (MW)	**15,895**	**15,333**
Thermal net production (GWh)	30,891	31,501
Renewable net production (GWh)	10,862	9,513
Total net production (GWh)	**41,753**	**41,014**

Environmental and social performance

Environment	2021	2020
Power generation emission factor (t CO2/GWh)	261	297
Greenhouse gas (GHG) emissions (M tCO2 eq)[1]	14	16
Emissions-free installed capacity (%)	33	29
Emissions-free net production (%)	35	32

Interest in people	2021	2020
No. of employees at year-end[2]	7,366	9,335
Training hours per employee	28.8	26.6
Men/women (%)[3]	68/32	67/33

Health and safety	2021	2020
No. of accidents leading to time lost	8	4
Frequency of accidents with time lost	0.1	0.04

Commitment to society and integrity	2021	2020
Economic value distributed (Euros million)	22,494	16,235
No. of complaints received by the Ethics Committee	61	80

[1] GHG: greenhouse gases, measured as tCO_2 equivalent (scope 1).
[2] Does not include the number of employees at discontinued operations (1 person in 2021 and 1,392 persons in 2020).
[3] Including employees at discontinued operations.

1.2. Executive summary

- The year 2021 has been marked by the gradual recovery of energy demand and the significant rise of commodity prices, impacting both gas and electricity. This trend has intensified during the second half of the year as we approached the winter season.

- Naturgy ordinary EBITDA reached Euros 3,983 million in the full year 2021, up 7% vs. previous year, and above its guidance, mainly supported by the gradual recovery of energy demand and the rising commodity prices, particularly gas.

- Ordinary Net Income reached Euros 1,231 million in 2021, up 41% vs. 2020. On a reported basis, Net income reached €1,204m. The restructuring costs linked to the employee voluntary departure plan in Spain, and the breakup penalties associated to the cease of certain gas contracts in the last quarter of the year, were almost fully compensated by the net gains from the disposal of CGE Chile, the agreement in UFG, and the 2013-2020 hydro canon provision reverted during the last quarter of 2021

- Total capex amounted to Euros 1,484 million in 2021, up 16% vs. the previous year. This increase was mainly explained by greater investments in renewable developments in Australia, Spain & the USA, as well as by higher investments in supply (commercial efforts and digitization).

- Net debt at the end of 2021 stood at Euros 12,831 million, implying a Net debt / LTM reported EBITDA of 3.6x compared to 3.9x as of 31 December 2020. The significant net debt reduction and deleveraging was mainly driven by the disposal of Naturgy's Chilean electricity networks subsidiary in Chile and the cash payments resulting from the agreement to exit UFG. On the other hand, the surge and volatility in gas prices had a temporary negative impact on working capital consumption, notably in 4Q21, which has partially offset the expected reduction in net debt. Such impact however is deemed as transitory and WC consumption is expected to normalize in the forthcoming quarters.

- During 2021, the company paid out a total dividend of 1.33 €/share in cash, including the final dividend of 2020 (0.63 €/share) paid in March as well as the first and second interim dividends for 2021 corresponding to 0.3 €/share and 0.4 €/share, paid in August and November 2021, respectively. The company will be proposing a 2021 complementary dividend of €0.5/share in its upcoming AGM, in line with its dividend policy of €1.2/share per year.

Macroeconomic growth and energy demand

Energy demand experienced a gradual recovery during the year in the regions where the Group operates. Electricity and gas demand in Spain compared on average 2.4% and 5.4% above 2020 respectively. Similarly, electricity and gas demand across the Latin American regions where the Group operates experienced an increase on average of 4.8% and 22.5% respectively during 2021 and compared to 2020.

During 2021, LatAm currencies depreciated against EUR with a negative effect of €-42m and €-8m on the Group's ordinary EBITDA and Net Income respectively. The depreciation pace has moderated in 2021compared to prior years, albeit Brazil and Argentina continued to show a notable depreciation in the year.

Evolution of commodity prices

The year 2021 has been marked by the volatile energy scenario and the surge of gas and electricity prices, most notably during the second half of the year.

Brent prices increased by 69.5% on average when compared to 2020 while gas prices on major gas hubs show as well significant increases vs. 2020 (HH increased by 71.4% and NBP multiplied by 4.9x on average). Wholesale electricity prices for their part multiplied by 3.3x on average vs. 2020, exceeding all- time highs Said increases resulted in significant regulatory changes and uncertainty in Spain during the year.

Corporate activity

During 2021 Naturgy continued to progress on its business simplification and de-risking, reducing risk concentration in Chile and reaching a solution to its lingering disputes in Egypt, reinforcing the company's balance sheet and strength to pursue more ambitious renewable growth.

On 10 March 2021, Naturgy, ENI and The Arab Republic of Egypt completed the agreement to amicably resolve the disputes affecting Union Fenosa Gas (UFG), the 50%/50% partnership between Naturgy and ENI. Naturgy received a series of cash payments adding up to approximately US$0.6bn, as well as most of the assets outside of Egypt, excluding UFG's commercial activities in Spain.

Furthermore during 2021, Naturgy completed the disposal of its 96.04% equity shareholding in its Chilean electricity networks subsidiary, Compañía General de Electricidad S.A in Chile (CGE), to State Grid International Development Limited (SGID) for a total purchase price (equity value) of €2,570m.

COVID-19 update

Naturgy continues to support and protect the interests of all its stakeholders, including measures to preserve employee health, safety and wellbeing, resources to guarantee effective remote work, or individual protection and support by Naturgy's medical services.

Relevant measures remain in place to support society as well as customers and suppliers, including the reinforcement of key infrastructures to ensure the stability and quality of electricity and gas supply. Moreover, and in light of the significant rise in electricity prices and the impact it might have on its industrial and SME/retail clients, Naturgy announced at the beginning of September, its Commitment Initiative, consisting on offering a fixed price of €60/MWh for electricity in Spain for 2 years without conditions. Further to this, Naturgy extended its offering with a fixed price of 65 euros / MWh for three years, which allows clients to get a stable price not linked to the volatility of the pool for a longer horizon.

Naturgy reiterates the importance and value of its commitment to society and reaffirms its willingness to maintain its support for its clients with measures within the company's reach.

2. Main risks and opportunities

2.1. Risk management model

Naturgy's risk management model seeks to ensure that the company's performance is predictable within an acceptable bounded range. The model quantifies the variability of performance and ensures that it is in line with strategically defined target levels in all aspects that are of importance to its stakeholders.

Core goals of the risk measurement and management model include ensuring that material risk factors are correctly identified, assessed and managed. The final objective is to ensure that the level of risk exposure assumed by Naturgy in the course of its business is consistent with the company's defined overall risk profile and the attainment of annual and strategic objectives.

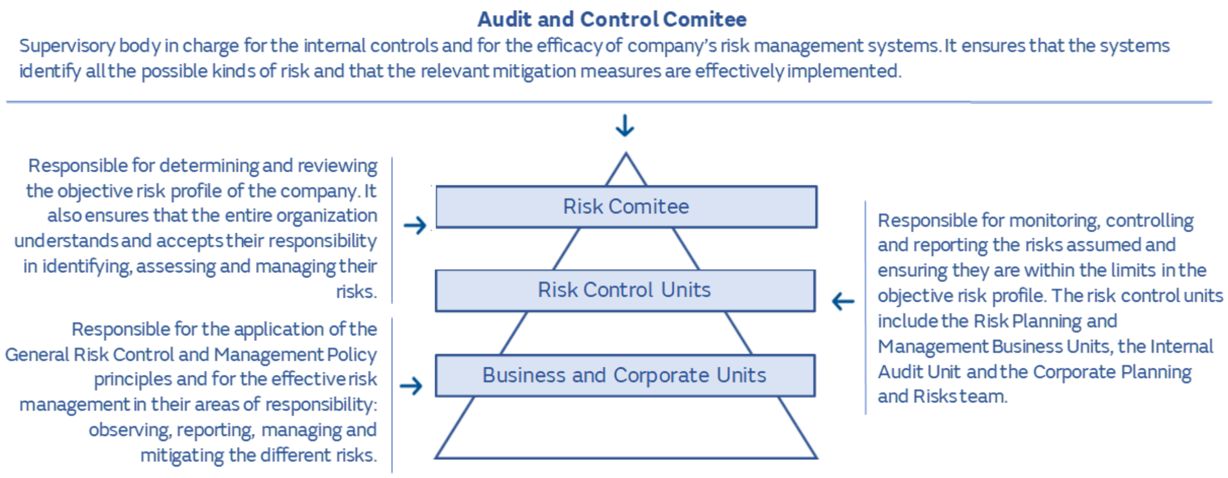
The Integrated Risk Management and Control System is structured as follows:

- *Risk Appetite*: definition of risk tolerance by setting limits for the main risk categories, by risk and by business, as a function of the targets.
- *Risk Assessment*: methodology, procedure and process for identifying, assessing and measuring risks.
- *Risk Governance & Management*: risk governance and management mechanism for all risk classes and all businesses.
- *Risk Reporting*: regular systematic reporting and monitoring of risk at the various levels of management: Business, Business Units, Chairman's Office and Board of Directors.

Risk management bodies

Naturgy has a framework integrating the vision of governance, risks and compliance so as to provide a 360º view of the group's processes, existing controls and the associated risks.

To this end, it has a number of bodies with clearly identified areas of responsibility, making it possible to ensure the predictability and sustainability of the company's operational and financial performance.



The Risk Control units exercise oversight to ensure that results are recurrent and sustainable. A key task is modelling the annual accounts to identify their main sensitivities and anticipate possible impacts and mitigating actions.

Additionally, each business unit has specific information on the main types of risk that may affect it. The goal is to facilitate decision-making, which is positive for the company since it enhances profitability, predictability and efficiency.

Comprehensive management

Naturgy analyses its overall risk profile on the basis of the potential impact on its annual accounts. In this way, it determines the maximum accepted level of risk exposure and the admissible limits.

The tools that enable the company to achieve continuous improvement in the process of identifying, characterising and determining Naturgy's risk profile are:

- Global Risk Control and Management Policy: updated and approved by the Board of Directors of Naturgy in November 2020. Its purpose is to establish the general principles and standards of behaviour required to ensure proper identification, reporting, assessment and management of Naturgy's exposure to risk.

- Corporate Risk Map: identifies and quantifies the risks which might affect Naturgy's performance, considering the characteristics of the risk position (impact variables, potential severity in quantitative and qualitative terms, likelihood of occurrence, and degree of management and control). It is updated and submitted to the Audit and Control Committee every year.

- Other risk maps: these are developed by Naturgy's Business and Corporate units following a common methodology and serve as the basis for the Corporate Risk Map.
- Risk Measurement System: serves to quantify, on a recurring probabilistic basis, the risk position assumed overall in each risk category. To this end, it analyses correlated risks, analyses sensitivity and performs stress tests for the main identified risk.

Risk categories

In the 2021 Risk Map, Naturgy defined four risk types: Economic, Financial, Operational, and Reputational/ Sustainability.

Types of economic and financial risk

For the types of economic and financial risk, a risk assessment is applied through quantitative modelling.

Categories of economic risk

Risk factors with an impact on the businesses' EBITDA.

- **Market/commodity risk**, the uncertainty caused by price variability of energy and other commodities that the company uses.
- **Exchange rate risk**, the uncertainty associated with changes in the exchange rates of the currencies in which Naturgy's businesses are denominated during the year.
- **Regulatory risk**, the risk associated with reviews of the remuneration frameworks for the regulated businesses and/or updates to the specific remuneration parameters under which Naturgy businesses operate.
- **Volume risk**, risk associated with the variation of volumes produced, distributed and/or supplied due to variations in temperature and the macroeconomic or competitive environment with respect to the base scenario considered in the projections.
- **Margin/Price Risk**, understood as the price risk not contemplated under market/commodity risk created by changes in competitive pressure or unachieved margin optimisation scenarios.
- **Legal risk,** related to the eventual outcome of litigation, arbitration or legal claims against Naturgy in the year of analysis.
- **Operational risk**, associated with events of force majeure or accidents affecting persons, and with accidents, damage or non-availability of the company's operating assets, after coverage by Naturgy's insurance programme.

Financial risk categories

Risk factors impacting the company's cash flow and balance sheet.

- **Credit risk**, unexpected loss due to uncertainty associated with the probability of non-payment of monetary obligations and/or deterioration of the credit quality of the end customers and counterparties with which Naturgy operates.
- **Interest rate risk**, variability of the company's financial expenses caused by interest rate movements in the currencies in which Naturgy's debt is denominated.
- **Tax risk**, associated with the proper application of tax regulations, the complexity of their interpretation, and possible amendments, with a potential economic impact on the company's accounts.
- **Liquidity,** risk associated with a potential increase in the financing needs required to maintain the company's target rating.
- **Rating**, risk of a downgrade of the company's credit rating, considering that the company targets an anchor BBB rating.
- **Provisions**, risk of maintaining an excessive volume of provisions on the balance sheet, resulting in the risk that they may materialize and their effect on cash outflows.

Types of operational and reputational/sustainability risk

For the operational and reputational/sustainability risk typologies, an assessment of the risk position using heat maps is generally applied.

Operational risk categories

Risk factors derived from operating the company's human and material assets.

- **Security risk**, understood as the residual risk associated with personal injury or material damage to critical facilities caused intentionally by a third party.
- **Process risk**, understood as a loss resulting from a shortcoming or failure in processes, systems or personnel performance with an impact on the company's efficiency or other risks.
- **Fraud risk**, derived from any intentional breach of the law by an employee or a third party to benefit themselves or the company, directly or indirectly, through the improper use of Naturgy resources or assets.
- **Cybersecurity risk**, arising from malicious attacks or accidental events with an operational impact that affect data, computer networks or technology.
- **Data protection risk**, understood as the risk associated with breach of data protection obligations that may result in an administrative sanction or civil judgement.
- **Environmental risk**, associated with the possibility that natural phenomena or human action may result in regulatory environmental limits being exceeded or in damage to ecosystems and biodiversity.
- **Customer satisfaction risk**, understood as the risk of not offering the customer a distinctive value proposition that places the company in a privileged position to define new relationship models and address the digital transformation by maximising the value of new technologies.
- **Health and safety risk,** understood as the risk of injury and health impairment for professionals of Naturgy or partner companies in connection with the business.

Sustainability and Reputational risk categories

Risk factors associated with behaviours that constitute a departure from good practices in the area of reputation, ESG commitment, compliance, people and climate change.

- **Reputational and ESG risk,** uncertainty in the evolution of stakeholders' perception of the company's reputation and its capacity to engage in business sustainably from an environmental, social and governance point of view.
- **Compliance risk,** understood as the risk of sanctions, financial losses or loss of reputation that Naturgy could suffer as a result of non-compliance with both legal obligations and standards, policies and other internal regulations applicable to its activities.
- **Energy transition and climate change risk**, arising from the energy transition (regulation, markets, technologies, etc.) and the physical impacts of climate change (acute and chronic).

2.2. Main risks

There are horizontal risks, such as the uncertainty in the macroeconomic context and geopolitical exposure, which materialize and have an impact on many of the risk types described in the previous section.

Uncertainty in the macroeconomic context

During the last decade the global economy has been growing at moderate rates marked by the stagnation of economic activity in Europe and the economic contraction of various emerging countries. As of 2020, the macroeconomic scenario was profoundly altered by the lockdowns derived from the outbreak of the COVID-19 pandemic and, specifically in the energy sector, this translated into lower demands for gas and electricity and a significant depreciation of the currencies in key regions of Latin America.

In 2021, the effects of the pandemic have continued to generate strong uncertainty in the economy which, as of the third quarter of 2021, has implied instability between supply and demand in the international markets for energy commodities. At the date of publication of this report, the final extent and timing of the definitive recovery from the COVID-19 health crisis, and the final extent and evolution of geopolitical tensions in Europe, are not known with certainty.

In any case, the Group continuously monitors the evolution of the economic cycle in the short, medium and long term, with the aim of minimizing the negative effects that the context could generate.

External geopolitical exposure

Naturgy has interests in countries with varied political, economic and social environments. It is exposed to two main geographies outside the European Union:

- Latin America
  Among the risk factors linked to investment and business in Latin America, it is worth mentioning the influence on the economy by local governments, the fluctuation in the rate of economic growth, high levels of inflation and devaluation, depreciation or overvaluation of currencies. local, changing environment of interest rates, as well as social tensions and political instability.

– Middle East and Maghreb
  Naturgy has assets and major gas procurement contracts in several countries of the Maghreb and the Middle East. Political instability in the zone may result in physical damage to the assets of Naturgy's investee companies or the obstruction of the operations of those or other companies, interrupting the Group's gas supply.

Table of main risks and trends

Risk type		Description	Management approach	Metric		Trend
Market/commodity risk						
Commodity prices	Gas	Volatility in the international markets that determine the gas price.	Physical and financial hedges. Portfolio management	Stochastic	↑	Mismatch between long-term contracts and hub prices.
	Electricity	Volatility in electricity markets.	Physical and financial hedges. Optimisation of the generation fleet.	Stochastic	↑	Penetration by renewables with zero marginal cost and intermittent production.
Exchange rate risk						
Exchange rate		Volatility in international currency markets.	Geographic diversification. Hedging via local-currency funding and derivatives. Monitoring the net position.	Stochastic	↑	Uncertainty about growth prospects in Latin America.
Regulatory risk						
Regulatory		Exposure to reviews of criteria and returns recognised for regulated activities.	Step up communication with regulators. Adjust efficiency and capital expenditure to recognised rates.	Scenarios	↑	Pressure from regulators, as a function of the situation of the country/industry.
Volume risks						
Volume	Gas	Mismatch between gas supply and demand.	Optimisation of contracts and assets worldwide.	Deterministic / Stochastic	↑	Aggregate demand pressure.
	Electricity	Reduction of the available thermal gap. Uncertainty as to renewable production volume.	Optimisation of the supply-generation balance.	Stochastic	↑	Aggregate demand pressure.
Margin/price risk						
Margin/price		Risk created by changes in competitive pressure or unachieved margin optimisation scenarios.	Portfolio management by adapting long-term purchase and sale formulas.	Scenarios	↑	Reviews of long-term gas contracts
Legal risk						

Legal	Uncertainty as to the eventual outcome of litigation, arbitration or legal claims.	Analysis and mitigation of legal risk affecting the company's operations and corporate governance. Engagement of top-level law firms. Recognition of provisions on a prudential basis.	Scenarios	⇆	Different business units are affected by different laws in each country.
Operational risk					
Insurable risks	Accidents, damage or non-availability of Naturgy assets.	Continuous improvement plans. Optimisation of the total cost of risk and hedges.	Stochastic	↑	Growing tension in the insurance market in the face of the rising frequency of extreme weather events.
Credit risk					
Credit	Uncertainty associated with the probability of non-payment of monetary obligations and/or deterioration of the credit quality of the end customers and counterparties with which Naturgy operates.	Analysis of customer solvency in order to define specific contractual conditions. Debt collection process.	Stochastic	↑	Transitory effect of the post-COVID-19 recovery.
Interest rate risk					
Interest rates and credit spreads.	Volatility in funding rates.	Financial hedges. Diversification of funding sources.	Stochastic	⇆	Uncertainty about interest rate scenarios.
Tax risk					
Tax	Ambiguity or subjectivity in the interpretation of current tax regulations, or material amendments to same.	Queries to independent expert bodies. Engagement of top-level advisory firms. Adoption of the Code of Good Tax Practices. Recognition of provisions on a prudential basis.	Scenarios	⇆	Different business units are affected by different taxes.
Liquidity, rating and provision risks					

Liquidity, rating and provision risks	Financial risks associated with maintaining the company's rating, derived from liquidity conditions or other causes. Risks associated with excessive use of resources due to maintaining provisions.	Establishment of a target rating and ensuring sufficient liquidity to maintain it in the event of a potential adverse scenario.	Scenarios	⇆	Ratification of the target of an investment grade rating in the Business Plan 2021-2025
Security risk					
Security	Residual risk associated with personal injury or material damage to critical facilities caused intentionally by a third party.	Corporate positioning through the Security Policy, defining a specific protection model for Critical Infrastructures (CI). Engagement with the businesses, Centro Nacional para la Protección de Infraestructuras Críticas (CNPIC), Instituto Nacional de Ciberseguridad (INCIBE-CERT) and other public- and private-sector bodies involved in CI security.	Heatmap/ Scenarios	⇆	Certification audits by the regulator (CNPIC) of critical operators, in which technology is of great importance.
Process risk					
Processes	Uncertainty resulting from a shortcoming or failure in processes, systems or personnel performance with an impact on the company's efficiency or other risks.	Annual internal audit plan Weakness detection. Implementation of improvement actions (recommendations). Audit and Control Committee.	Heatmap/ Scenarios	⇆	Increase in the percentage of material recommendations that are implemented.
Fraud risk					
Fraud	Risk derived from any intentional breach of the law by an employee or a third party to benefit themselves or the company, directly or indirectly, through the improper use of Naturgy resources or assets.	Control mechanisms through the Global Policy of the Internal Control System for Financial Information. Arrangement of hedges in the insurance market	Scenarios	⇆	Maintain low levels of fraud at Naturgy
Cybersecurity risk:					

Cybersecurity	Malicious attacks or accidental events that affect data, computer networks or technology.	Implementation of security measures; Event analysis and remediation measures; Training.	Scenarios/ Heatmaps	↑	The cybernetic situation is becoming more demanding.Threat protection plan to mitigate the likelihood of these risks and their associated impact.
Data protection risk					
Data protection	Uncertainty associated with breaches of data protection obligations that may result in an administrative sanction or civil judgement.	Action Plan by business area to mitigate the risk associated with each obligation based on priority and criticality. The company conforms to the requirements of the General Data Protection Regulation (GDPR).Internal audit plan for periodic review of compliance.	Heatmap/ Scenarios	↑	Uncertainty and tightening regulatory requirements.
Environmental risk					
Environment	Possibility that natural phenomena or human action may result in regulatory environmental limits being exceeded or in damage to ecosystems or biodiversity.	Emergency plans at facilities with risk of environmental accident. Specific insurance policies. End-to-end environmental management.	Scenarios/ Heatmaps	⇆	Implementation of an Integrated Management System certified and audited each year by AENOR.
Health and safety risk					
Health and safety	Risk of injury and health impairment for professionals of Naturgy or partner companies in connection with the business.	Health and safety management system. Safety plan aimed at controlling the six most critical risk factors in terms of accident frequency and severity: confined spaces, work at heights, electrical risk, tree felling and pruning, cargo handling, and road safety.	Heatmap/ Scenarios	⇆	Accident rates at partner firms.
Reputation and ESG risk					
Image and reputation	Impairment of stakeholders' perception of Naturgy.	Identification and tracking of potential reputation events. Transparency.	Scenarios/ Heatmaps	⇆	Stabilisation of MERCO index score.
Compliance risk					

Reputational and criminal risk	Administrative and criminal sanctions. Deterioration of Naturgy's reputational image.	Criminal prevention model, Code of Ethics and Anticorruption Policy.	Heatmap/ Scenarios	↑	Commission of criminal offenses, sanctions, financial, reputational, contract and client losses.
Counterparty risk	Administrative and criminal sanctions. Damage arising from breach of contract.	Counterparty Due Diligence Procedure.			
Climate change risk					
Climate change and energy transition	Uncertainty arising from the energy transition (regulation, markets, technologies, etc.) and the physical impacts of climate change.	Corporate positioning via the Global Environmental Policy and Environment Plan, which strengthen governance in climate issues and set emission reduction targets.	Stochastic/ Scenarios/ Heatmaps	↑	Regulatory uncertainty.

Metrics used:

- Stochastic: production of trend lines for the main magnitudes, taking the maximum deviation from the benchmark scenario to be the risk, within a pre-set confidence interval. Those magnitudes are generally EBITDA, earnings after taxes, cash flow and value.
- Scenarios: analysis of the impact, with respect to the benchmark scenario, of a limited number of possible incidents.
- Heatmap: the main risk factors for each risk category are assessed to quantify the impact and probability of the identified risks.

Market/commodity risk

Electricity and gas price volatility

An important part of Naturgy's operating results is linked to the purchase of gas to supply a diversified portfolio of customers.

Most of these gas supply contracts are signed in the long term with purchase prices based on a combination of different commodity prices, basically prices of crude oil and its derivatives, and natural gas hubs.

However, sales prices to end customers are generally agreed in the short/medium term and are conditioned by the supply-demand balance that exists at any given time in the gas market. This may imply a decoupling with gas supply prices.

Therefore, Naturgy is exposed to the risk of variations in the price of gas supply with respect to the sale price of end customers. The exposure to this risk is managed and mitigated by natural coverage, trying to balance the exposures to commodities of both prices. Additionally, some supply contracts allow this exposure to be managed through volume flexibility and price review mechanisms.

When it is not possible to achieve a natural hedge, the position is managed, within reasonable risk parameters, contracting derivatives to reduce exposure to price decoupling risk, generally designated as hedging instruments.

In the integrated electricity businesses, the company's aggregate exposure is determined by the generation/ commercial strategic positioning and by the final sales pricing policies in electricity commercialization.

Finally, the company is exposed to the evolution of the price of CO_2 emission rights, destined for generation in its combined cycles. Conjuncturally, Naturgy invests part of its cash surpluses in notes linked to CO_2.

Exchange rate risks

Naturgy has interests in various countries and is exposed to the exchange rate in each of its currencies, as well as to the dollar currency.

Exchange rate risk is largely mitigated by financing investments in local currency. Likewise, efforts are made to match the costs and revenues of the activities referenced to the same currency, as well as the amounts and maturities of assets and liabilities arising from operations denominated in currencies other than the euro.

Additionally, the exchange rate risk is managed by contracting financial derivatives, within the limits approved for hedging instruments, the level of exposure and the risk appetite approved in each year.

Margin/price risk

The liberalization processes both in Spain and in other relevant markets have had a significant impact in terms of competitive pressure on the final prices of the markets and on the definition of market shares.

In the electricity industry, liberalization in the European Union has increased competition with the entry of new agents, affecting the Spanish market, and may have an impact on the development of electricity generation and marketing businesses.

Naturgy monitors and quantifies the sales margins of all its businesses, identifies the relevant deviations in the margin spread assumptions and mitigates its risk by adapting sales and purchase formulas to all terms.

Gas and electricity volume risk

Part of the purchases of natural gas and liquefied natural gas (LNG) is made through long-term contracts, which include take-or-pay clauses under which Naturgy is obliged to purchase certain volumes of gas annually. Any downward deviation in gas demand may contractually obligate the payment of the minimum amount committed in accordance with said clauses.

On the other hand, in a scenario of gas shortage or excess demand, short-term supply extra costs may have a material adverse effect on the group's operating costs.

All volume risks are measured, monitored and quantified annually, evaluating the suitability of coverage for those linked to the weather (temperature, hydraulicity, etc.) whose management follows the policies and the approved risk appetite.

In the field of electricity generation, Naturgy's results are exposed to the variability of volumes, conditioned by the evolution of electricity demand and the generation mix in the market, which is being particularly affected by the growing weight relative to generation with renewable energies.

Naturgy manages its contracts and assets in an integrated manner, optimizing the energy balance.

Regulatory risk

Regulated and unregulated activities coexist in the gas and electricity distribution businesses. The legal regulations applicable to the gas and electricity sectors are typically subject to periodic reviews by the competent authorities, which may have an impact on the current remuneration scheme for regulated activities, affecting the operation of the business, as well as the economic situation of Naturgy.

All the specific legislation governing the establishment of the methodological frameworks for setting the remuneration for gas and electricity distribution and transportation/transmission in each of the countries and sectors is set out in the Regulatory Framework appendix 4 to the consolidated annual accounts.

As a consequence of the COVID-19 crisis, most of the authorities in the countries where Naturgy operates have established temporary regulatory measures that may affect regulated businesses.

Naturgy manages regulatory risk on the basis of regular communication with the regulators. In addition, in its regulated activities, Naturgy adjusts its costs and investments to the allowed rates of return for each business.

Operational risk

Naturgy's activities are exposed to various operational risks, such as breakdowns in the distribution network, accidents in power generation facilities LNG tankers accidents, explosions, pollutant emissions, toxic spills, fires, adverse weather conditions, contractual breaches, among others.

Additionally, claims might be brought against Naturgy for personal injury and/or other damage arising in the ordinary course of its operations. Such claims could result in the payment of indemnities under the legislation applicable in the countries in which Naturgy operates.

Naturgy has an extensive insurance programme that covers its operational exposure.

Cybersecurity risk

Naturgy is exposed to threats in connection with the availability, confidentiality, integrity and privacy of the information and technology that support business processes as well as the risk of non-compliance with regulations related to cybersecurity.

Such threats include, unauthorised access and the use, disruption, modification or destruction of information as a result of terrorist acts, malicious attacks, sabotage and other intentional acts.

Naturgy has contingency and security plans and insurance policies that cover such exposure.

Environmental risk

Risk associated with the possibility that, naturally or by human action, environmental limits set by the regulator are exceeded, ecosystems or biodiversity are damaged. Naturgy pays special attention to the protection of the environment and the efficient use of natural resources, acting beyond compliance with legal requirements and involving suppliers, interest groups and promoting the responsible use of energy both in its own facilities and on clients.

Naturgy has identified the environmental risks at its facilities using the reference standard –UNE 150008 in Spain– as a basis. For its prevention, it has implemented an integrated management system that includes the operational control and environmental management procedures. Additionally, Naturgy has implemented emergency plans in facilities and warehouses at risk of environmental accidents, including an action plan, means of containment and regular drills. Naturgy takes out specific insurance policies to cover this type of risk.

The environmental risk is developed in detail in chapter 5 “The opportunity of environmental challenges” of the Sustainability Report and Statement of Non-Financial Information.

Reputational and ESG risk

Naturgy has identified its stakeholder groups and subgroups and defines reputational risk as the gap between those groups' expectations and the Company's performance in the environmental, social and governance dimensions.

Naturgy has drawn up a Sustainability Plan that determines the 2021-2025 commitments and lines of action, which accompanies the company's transformation process and is aligned with the 2021-2025 Strategic Plan, with the commitments of the Corporate Responsibility Policy and the Sustainable Development Goals (SDG).

In environmental aspects, the commitments under the Corporate Responsibility Policy are expanded upon the Global Environment Policy, which applies to all geographies and businesses, which establishes four strategic environmental axes:

1. Environmental governance and management
2. Climate change and energy transition
3. Circular economy and eco-efficiency
4. Natural capital and biodiversity

Climate change and energy transition risk

With the aim of integrating the climate variable into Naturgy's strategic planning, the identification, measurement and management of climate change risks and opportunities is carried out in accordance with the recommendations of the Task Force on Climate-related Financial Disclosure (TCFD). The most outstanding result of this process in 2021 is the incorporation of the risks and opportunities of climate change in the new Strategic Plan 2021-2025, aligned with the international climate agenda.

Following the taxonomy of the TCFD, climate risk derives from two risk factors: from the energy transition, in regulation, market and technology risks and from the physical impacts of climate change, in acute climate risks (increase in extreme weather events) and chronic risks (sustained increase in average temperatures and rise in sea level).

Additionally, Naturgy is a member of a number of working groups at European level, which will enable it to adapt its strategy to new regulatory developments in advance. It is involved in clean development projects aimed at reducing CO_2 emissions.

The risk of climate change and energy transition is developed in detail in chapter 5 "The opportunity of environmental challenges" of the Sustainability Report and Statement of Non-Financial Information.

Other risks

Financial risks (interest rate, credit risk, liquidity risk and rating) and Legal are developed in Notes 18 and 36 of the Consolidated Annual Report, respectively.

The Tax, Compliance, Data Protection, Processes, Security and Fraud risks are developed in chapter 4 “Integrity and Trust” of the Sustainability Report and Non-Financial Information Statement. Likewise, the Health and Safety and Customer Satisfaction risks are developed in chapter 7 “Commitment and Talent” and chapter 6 “Customer Experience” of the same report, respectively.

2.3. Main opportunities

At Naturgy, the energy transition is seen as an opportunity to transform the business and promote the necessary changes to achieve a low-carbon economy. Naturgy's main opportunities are as follows:

- **Focus on stable geographical areas**, with low risk and strong currency, which allowcapture energy demand growth and maximise business opportunities in new markets.
- **Renewable generation**: increase renewable generation capacity aligned with the global energy transition.
- **Operation and growth in Networks,** based on solid regulatory frameworks with long-term visibility and focused on continuous improvement, digitization and automation.
- **Technological developments and innovation**: development of innovation projects in hydrogen and its blending in gas networks, renewable gas, energy efficiency, sustainable mobility and fair transition.
- **Natural gas and LNG supply portfolio**: continuous review and optimization of supply contracts, transition in the indexation of oil prices to hub, continuous risk management to guarantee predictable cash flows and adequacy of the fleet of LNG ships putting value its flexibility.

3. Corporate governance

Attached as an Appendix and forming an integral part of this Directors' Report is the Annual Report on Corporate Governance 2021 and the Annual Report on Director Remuneration 2021, as required by article 538 of the Capital Companies Act.

Corporate governance model

Naturgy is governed in accordance with the principles of efficiency and transparency in line with the main international recommendations and standards in this area.

The corporate governance terms of reference comprise basically:

- Articles of Association (adopted in 2018, updated in 2021).
- Regulations of the Board of Directors and its committees (updated in 2021).
- Regulations of the General Meeting of Shareholders (adopted in 2018, updated in 2020).

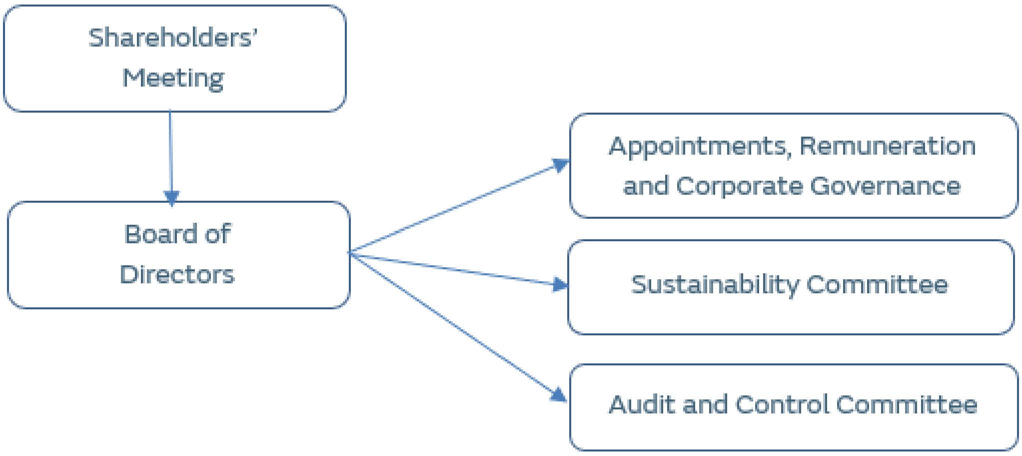
- Human Rights Policy (updated in 2019).
- Code of Ethics (updated in 2021)

The main shareholders of Naturgy as of 31 December 2021 and 2020 are as follows:

	% interest in share capital	
	2021	2020
- Fundación Bancaria Caixa d'Estalvis i Pensions de Barcelona, "la Caixa" (1)	26.71	24.8
-Global Infrastructure Partners III (2)	20.6	20.6
-CVC Capital Partners SICAV-FIS, S.A. (3)	20.7	20.7
- IFM Global Infraestructure Fund	12.2	—
- Sonatrach	4.1	4.1

(1) Holding through Criteria Caixa, S.A.U.
(2) Global Infrastructure Partners III, whose investment manager is Global Infrastructure Management LLC, holds its interest indirectly through GIP III Canary 1, S.à.r.l.
(3) Through Rioja Acquisition S.à.r.l.

Naturgy's governance structure is as follows:



Shareholders' Meeting

Any person who is a shareholder of record five days before the Shareholders' Meeting is entitled to attend the Meeting.

Board of Directors

The Board of Directors of Naturgy operates via plenary meetings and committees, in accordance with the requirements of the Capital Companies Act. For this reason, the Board of Directors of Naturgy has an Audit and Control Committee, an Appointments, Remuneration and Corporate Governance Committee, and a Sustainability Committee, which, in addition to the functions entrusted to them by law, also discharge the duties assigned to them by the Board of Directors. Independent directors comprise a majority of both the Audit and Control Committee and the Appointments, Remuneration and Corporate Governance Committee, and all committees are chaired by independent directors.

Risk prevention and corporate responsibility are within the remit of the Board of Directors and its committees. The Board of Directors is the most senior body with responsibility for approving corporate governance and corporate responsibility policies. Each year, by drafting the respective reports, it reviews and approves disclosures of the risks and opportunities in those areas.

The main issues addressed by the Board of Directors in 2021 are as follows:

- Approval of a new Strategic Plan 2021-2025.

- Production of the mandatory report in connection with the voluntary tender offer by Global InfraCo O (2) S.à.r.l.
- Amendment of the Regulations of the Board of Directors and its committees.
- Amendment of the Code of Ethics.s
- Review of the powers of the Audit Committee.
- Grant of powers to the Executive Chairman to approve related-party transactions in the terms set out in the Capital Companies Act.
- Approval of the internal procedure for reporting and regular oversight of related-party transactions that are approved by the Chairman in exercise of his delegated powers.
- External audit of the separate and consolidated annual accounts.
- Oversight of the production of the financial reporting.
- Tax and litigation situation.
- Auditor independence.
- Related-party transactions.
- Verification of the crime prevention system.
- Oversight of the risk control system and analysis of specific risks.
- Oversight of the internal control and internal audit systems.
- Naturgy insurance programme.
- Oversight of transactions with own shares.
- Compliance action plan.

The Board of Directors of Naturgy has 12 members, the Audit and Control Committee has 7 members, the Appointments, Remuneration and Corporate Governance Committee has 7 members, and the Sustainability Committee has 5 members.

The composition of the Board of Directors and its sub-committees on 31 December 2021 is as follows:

Board of Directors		Audit and Control Committee	Appointments, Remuneration and Corporate Governance Committee	Sustainability Committee	Category of director	Seniority on Board
Executive Chairman	Mr. Francisco Reynés Massanet				Executive	6/02/2018
Lead director	Mr. Ramón Adell Ramón	Director	Chairman		Independent	18/06/2010
Director	Mr. Enrique Alcántara-García Irazoqui		Director		Proprietary	13/05/2021
Director	Mr. Francisco Belil Creixell	Chairman	Director		Independent	14/05/2015
Director	Ms. Lucy Chadwick	Director		Director	Proprietary	16/03/2020
Director	Ms. Isabel Estapé Tous	Director		Director	Proprietary	16/03/2020
Director	Ms. Helena Herrero Starkie	Director		Chairman	Independent	04/05/2016
Director	Mr. Rajaram Rao		Director		Proprietary	21/09/2016
Director	Rioja S.à.r.l, Mr. Javier de Jaime Guijarro		Director		Proprietary	01/08/2019
Director	Mr. Pedro Sáinz de Baranda Riva	Director	Director		Independent	27/06/2018
Director	Mr. Claudio Santiago Ponsa		Director	Director	Independent	27/06/2018
Director	Theatre Directorship Services Beta, S.à.r.l., Mr. José Antonio Torre de Silva López de Letona	Director		Director	Proprietary	18/05/2018
Secretary (not a director)	Mr. Manuel García Cobaleda	Secretary (not a director)	Secretary (not a director)	Secretary (not a director)	N/A	29/10/2010

Management structure

Naturgy's management structure consists of three business units (Energy and Networks, Renewables and New Businesses, and Supply) as well as corporate units to ensure centralised control.

The Executive Committee is deemed to comprise the Executive Chairman, Mr. Francisco Reynés Massanet, in connection with his executive functions, and the executives who report directly to him. As of 31 December 2021, it comprised the following departments:

Business units

Energy and Networks, managed by Mr. Pedro Larrea Paguaga
Renewables and New Businesses, managed by Mr. Jorge Barredo López
Supply, managed by Mr. Carlos Francisco Vecino Montalvo

Corporate Units

Information Systems, managed by Mr. Rafael Blesa Martínez
Capital Markets, managed by Mr. Steven Fernández Fernández
Planning, Control and Administration, managed by Mr. Jon Ganuza Fernández de Arroyabe
Company and Board Secretariat, managed by Mr. Manuel García Cobaleda
Sustainability, Reputation and Institutional Relations, managed by Mr. Jordi García Tabernero
People and Organisation, managed by Mr. Enrique Tapia López

4. Forecast Group Performance

4.1. Vision

Strategic pillars

On July 28, 2021, Naturgy presented the **2021-2025 Strategic Plan**, which addresses a new stage that aims to promote our industrial growth while maintaining financial discipline and taking advantage of the opportunities of the energy transition; and to become a best-in-class reference operator through the digitization of processes.

The new plan is based on five solid pillars to promote Naturgy's transformation:

1. Growth
2. Focus
3. *Best-in-class*
4. ESG (environment, society and governance)
5. Culture

Growth

Our growth aims to be mainly organic, consistent with the energy transition and capable of taking advantage of asset rotation to accelerate the transformation.

- Mainly organic, maintaining capital discipline.
- Consistent with the energy transition.
- Opportunistic asset rotation to accelerate transformation.

Focus

We focus on renewable projects in early stages of development and stable geographies; also in network projects, with a prominent role of digitization and a stable regulatory framework.

- Renewables and networks.
- Stable geographies and regulatory frameworks.
- Volatility reduction in procurement commitments.

Best-in-class

We are committed to continuous improvement, increasing the digital footprint and reinventing relationships with our customers.

- Continuous improvement.
- Increasing digital footprint.
- Reinventing customer relationships.

ESG

We have a firm commitment to environmental and social matters. Our roadmap includes a Sustainability Plan with solid objectives in the environmental, social and governance fields, thus integrating ESG into the core of the company.

- Embedded at the core
- Aligned with SDG.
- Tangible targets to meet commitments.

Culture

Our corporate culture must intensify the passion of our professionals, allow us to establish our values and be aligned with our stakeholders.

- Fueling passion on our employees.
- Solidifaying core values.
- Aligned with stakeholders.

Key investment objectives

In economic matters, our Strategic Plan pursues ambitious investment objectives, setting an estimated investment for this period of **14,000 million euros.**

This investment is established by maintaining financial discipline as a pillar and focusing on projects with predictable returns. On the other hand, 80% of the planned investment will be eligible according to the EU taxonomy of sustainable finance, thus being aligned with the energy transition.

The investment is distributed as follows:

Renewables

Euros 8,700 million

- Proven generation technologies.
- Focus on attractive geographies.
- Commitment to innovation.
  - Distributed generation.
  - Biogas and hydrogen.
  - Sustainable mobility.

Networks

Euros 4,100 million

- Focus on solid frameworks with proactive regulatory management.
- Ongoing projects to achieve full automation and remote operation.
- Adapting existing infrastructures to play a key role in energy transition.

ESG at the core of our vision

The Strategic Plan is part of Naturgy's commitments to the environment, society and governance (ESG). Placing sustainability as the backbone of our strategy on our roadmap allows us to reduce our environmental impact, increase the involvement and commitment of all our stakeholders and endorse ourselves as a responsible company with the energy transition.

Our 2025 objectives in ESG are the following:

Environment

Net Zero by 2050

- Reduce total CO2 emissions by 24% (2025 vs 2017).
- Protect Biodiversity, reaching a figure of more than 350 projects to preserve ecosystems.

Social

Gender parity by 2030

- Enhace diversity, reaching more than 40% of women in management positions.
- Extending ESG throughout supply chain up to 95%.

Governance

Management compensation aligned with ESG

- Variable pay of 10% linked with ESG objectives.
- Implement climate change risk reporting and taxonomy to maintain leadership positions in the sustainability indices.

4.2. Roadmap

Based on these strategic pillars, a roadmap is developed that is specified in economic objectives for each of the businesses.

Renewables

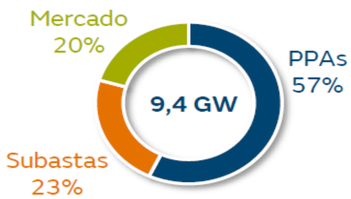
It is defined for the renewable business a growth strategy based on:

1. 1. Stable geographies
- Low risk and hard currency
- Solid regulatory frameworks
- Long-term visibility

2. 2. Proven technologies
- Solar PV, onshore wind and storage
- 14 GW in operation by 2025
- Tangible pipeline with visibility

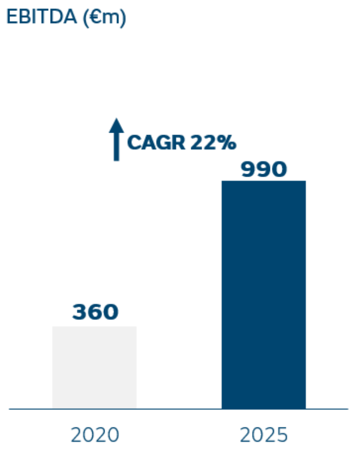
3. Customer base as a natural hedge

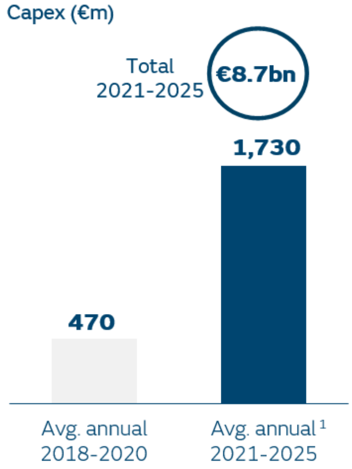
Balancing risks with new capacity (4.6 GW in 2020 to 14.0 GW in 2025)



New installed capacity

Financial estimates





Networks

The following key transformation initiatives are defined for the network business:

1. Spain Electricity networks

- At the forefront of electricity networks digitalization
- Increasing investment commitments in line with sector requirements

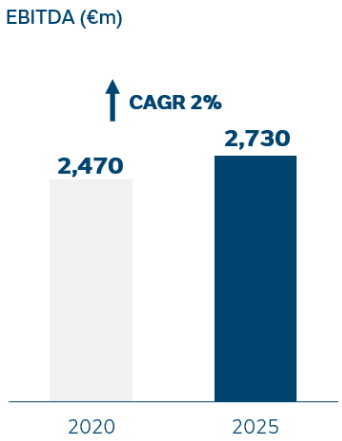
2. Spain gas networks

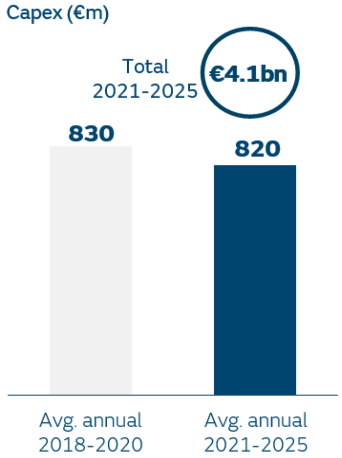
- Networks digital transition to ensure bes-in-class operations
- Commercial repositioning
- Accelerating contribution to decarbonization

3. LatAm networks

- portfolio management
- Investments to guarantee maintenance and safety standards

Financial estimates





Energy management

The following key transformation initiatives are defined for the energy management business:

1. Markets and procurements

- Progressive downsizing of procurements commitments
- Ongoing review and optimization of procurement contracts (oil to hub indexation transition)

2. International LNG

- Risk management to ensure predictable cash flows
- Downsizing of LNG tanker fleet under time charter
- Exploring value alternatives

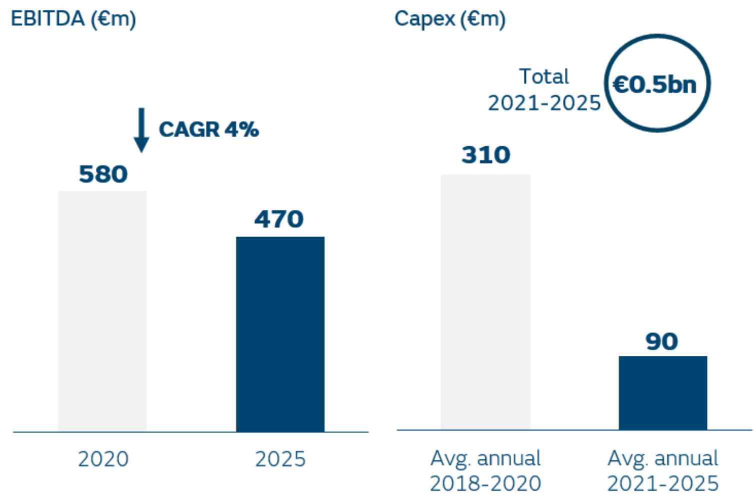
3. Spain thermal generation

- Remote operation and bottom-up process review of CCGT fleet
- Mothballing of non-performing CCGTs
- Working on hybridization alternatives
- Proactive regulatory management (system back-up)

4. LatAm thermal generation

- New opportunities for excess capacity over PPAs
- Cost and investments efficiency
- Exploring value alternatives for Mexico CCGTs

Financial estimates



Supply

The following key transformation initiatives are defined for the marketing business:

1. Boost competitiveness

- Market repositioning
- Integrated energy offering
- Refocusing of distribution channel strategy, including additional third party agreements
- Enhance profitability

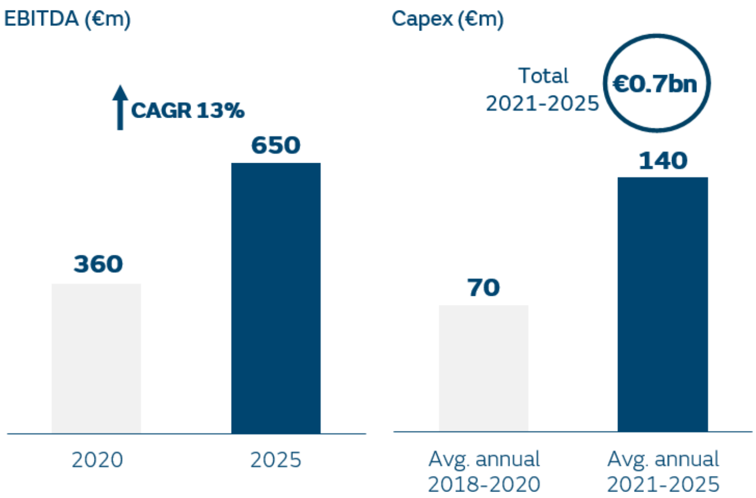
2. Reinvent customer relationships

- Redefined customer service
- Enhanced data analysis and customer segmentation
- Increased loyalty through customer value management

3. Accelerate digital transformation

- Transition to a new, simpler and integrated digital platform
- Enhanced efficiency in every single operating process

Financial estimates

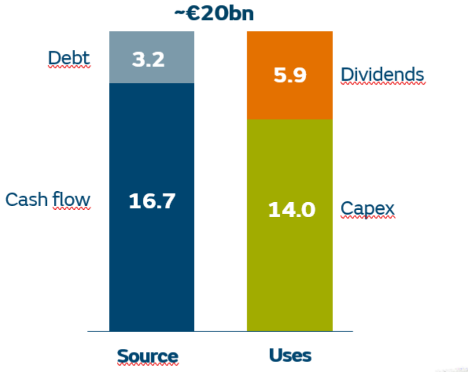


4.3. Summary

Dividend policy and capital allocation

The dividend policy is set with the aim of maintaining a solid BBB rating throughout the period. In this way, a dividend of 1.20 euros per share per year is established, which will be reassessed in 2023 depending on the performance and execution of the transformation.

The allocation of capital for the period 2021-2025 detailed between origins and uses is as follows:



Key figures

The 2025 objectives for the main economic magnitudes are detailed below:

Key figures	2020	2025	
Ordinary EBITDA	~3.700	~4.800	TACC 5,1%
Ordinary Net income	~900	~1.500	TACC 12,0%
Leverage (FFO/DN)	17.1 %	20.7 %	Rating BBB
Net debt	~13.600	~16.800	
	PE 2018-22	**PE 2021-25**	
Capex	~8.400	~14.000	x 1,7
Dividends (*Pay-out* on ordinary Net Income)	120 %	85 %	1,20 €/share

5. Sustainable innovation

Management vision and approach

The ecological transition to a carbon neutral economy is an opportunity in environmental, social and economic terms. It allows us to reduce our dependence on foreign energy, improve our trade balance and move towards a prosperous, modern economy. In this global context, meeting the challenge of climate neutrality requires a transformation of the energy system. Achieving this objective requires a horizontal vision that abandons the classic approach of analyzing and managing the main energy uses (electricity, heating, industrial heat, transportation) individually and adopts a smart sectoral integration that flexibly combines renewable generation, storage, demand-side management and the production of renewable fuels to optimize energy resources. This new energy model must be supported by:

- **Innovation**, which is a key lever for growth as it enables the adoption of new or better practices, new business models and technological solutions that contribute to process digitalization, automation and optimization, guaranteeing safety and operational improvement and facilitating access to information for better decision making, aimed at creating value and ensuring the company's competitiveness in the long term. Always to the fore, putting the customer at the center of what it does.
- **Optimization of renewable energy generation** through innovative systems because of their improved energy efficiency, their capacity for integration in the environment, in buildings or in business, their lower costs or greater reliability, and models that allow new players into the system and cover part of the energy needs of homes, SMEs and governments.
- Harnessing energy directly through new **manageable electricity demand applications that lend flexibility**, e.g. in climate control and mobility, and through storage for subsequent use as electricity or heat, in daily or seasonal storage systems.

- Production of **renewable gases**, particularly hydrogen, for end users where electrification is not technically feasible or economically viable. This is an efficient solution providing immediate decarbonization in hydrogen-intensive industries that currently use natural gas reforming and high temperature processes; also in heavy goods transport, maritime transport, rail transport and aviation. The fact that it is an energy vector gives it great potential for energy storage and integration into industry.

On this basis, Naturgy is developing an extensive programme of investment in renewable energies as a result of the Strategic Plan 2021-2025 and developing new lines of business in areas such as renewable gases (hydrogen and biomethane), storage and sustainable mobility; all of this to provide a broad range of value-added services and promote sustainable innovation as a driver of development. Examples include the additional investment opportunities under the Next Generation EU programme, focusing on renewable gases by developing projects such as La Robla and Meirama (green hydrogen plants), a network of hydrogen stations along the Spain's main heavy goods transport routes, and combining hydrogen and natural gas in turbines and cogeneration engines.

Investment in innovation (million euro)

In 2021, a total of Euros 59 million were spent on innovation (Euros 37 million in 2020), as indicated below:

	2021	2020
Investment in innovation	59	37

Main lines of innovation

The main lines of innovation on which Naturgy is working are described below:

Renewable gases

Basing decarbonization of the economy predominantly on a high level of electrification with renewable energies faces technical limitations in certain energy-intensive sectors, such as manufacturing and transportation. Since electrification cannot cover all energy demand, further integration of electricity and gas is an effective solution to achieve the decarbonization goals by taking advantage of the complementarity of renewable gases, gas infrastructure and electricity. The gas grid currently has a high storage capacity, and a level of reach and capillarity that make it possible to transport large amounts of energy to where it is to be consumed; these are essential factors for the use of renewable gases to decarbonize the end-use of energy at all points where natural gas is currently used. The development of renewable gases, biomethane and hydrogen, is part of the Just Transition Strategy and one of the areas of the energy transition that represents the greatest opportunities for job creation. They are identified as a way to decarbonize and generate employment in transportation and manufacturing while placing special emphasis on the creation of green jobs in rural areas, in line with Spain's strategy against depopulation.

As one of the main operators of basic natural gas infrastructures, Naturgy accepts its leading role as a driver of the development of the renewable gas value chain.

Biomethane

The production of biomethane, a renewable gas, from livestock, agricultural or industrial organic waste, or from landfills and wastewater plants, is an excellent example of the circular economy in the energy sector, providing significant environmental benefits and a supplementary source of income for rural areas.

Naturgy is working both on the development of projects with the integrated value chain (including waste management, biogas production and biomethane production and marketing), and on projects where biogas is available and the scope is focused on biomethane production and marketing.

Naturgy has experience in the development of renewable gas on a commercial scale, acquired in projects launched in recent years such as Methamorphosis, in Vilasana (Lleida), as well as the one located at the Bens (A Coruña) wastewater treatment plant (WWTP).

Naturgy also has 32 projects under development for biogas production and upgrading to biomethane for injection into the natural gas grid:

- 8 projects using livestock waste (1,408 GWh/year).
- 4 projects using WWTP sludge (170 GWh/year).
- 16 projects using industrial waste (595 GWh/year).
- 3 projects using the organic fraction of municipal solid waste (109 GWh/year).

- 1 project using agricultural waste (85 GWh/year).

Hydrogen

The renewable hydrogen value chain is at an incipient stage of development, with pilot projects that use hydrogen in place of fossil or other fuels.

Not all sectors of the economy will adopt hydrogen at the same pace because of differences in uses and availability, as well as the cost of the final equipment. In the short term, renewable hydrogen penetration can leverage sectors that already consume grey hydrogen, such as refineries and fertilizer plants.

Green hydrogen has a promising future provided that it receives the necessary boost from governments and the private sector to implement large-scale projects in line with the projected technology roadmap.

Spain's Hydrogen Roadmap set a target of 4 GW of installed electrolysis capacity by 2030, which is 10% of the target set by the European Union in its Hydrogen Strategy for that same year.

Naturgy has long been researching hydrogen development, because the renewable resource, the existing infrastructure and Spain's geostrategic position mean that the country has all the potential to become a hydrogen exporter in the future. This new energy could be exported through the current gas infrastructure, which would enable integration between the electricity and gas grids to create a more efficient and resilient energy system.

Also, like LNG, hydrogen can also be transported over long distances in liquid form. In a context in which there is global trading of hydrogen, this form of transport and distribution can be vital and Naturgy could play an essential role by contributing its international capacity and knowledge throughout the value chain.

During 2021, the company worked on the development of large renewable hydrogen production hubs linked to just transition zones, especially in areas affected by the closure of the group's thermal power plants. The objective of developing multi-demand hubs is to promote the development of new markets for direct consumption in industry, injection into the gas network for commercialization with guarantees of origin, mobility, and production of H2 derivatives: ammonia, methanol, etc.

Storage

Renewables penetration is growing steadily. According to Spain's National Integrated Energy and Climate Plan (PNIEC), by 2030, 74% of the energy mix will be made up of renewable energies, principally wind and photovoltaic. This presents the energy system with the challenge of equipping itself with flexible tools to manage production, match generation and consumption, avoid sudden drops in production, and provide firm capacity to the system. In this scenario, storage is key to the security and quality of supply.

During 2021, Naturgy worked on several initiatives:

- **Hybridization projects in its generation fleet**, mainly in wind and photovoltaic farms. The hybridization of storage with generation will make grid-connected renewable capacity manageable, providing flexibility and firm capacity to the system.
- Deployment of **stand-alone storage** in key areas where there is either grid congestion or loss of firm capacity due to the closure of thermal power plants. In technology terms, the challenges are similar to those of hybridization projects in wind farms — mainly managing the control system to achieve optimal operation.
- Development of a **new storage mode**l to optimize, in both economic and technical terms, the implementation of hybridized systems with storage in small generating facilities that are close to each other. Since there is currently no regulatory framework for this, it will be developed as a regulatory test case.

These projects are being developed with Spanish technology partners and research centres, with the aim of generating employment and strengthening the business fabric throughout the project value chain.

Sustainable mobility

In 2021, the company continued to focus on the nationwide roll-out of a network of natural gas filling stations open to the public.

The most notable initiatives in 2021 were as follows:

- Signature of the first **biomethane for vehicles** contract. Naturgy agreed to supply up to 2GW/year of biomethane for the last-mile delivery fleet of Aquaservice, a water distributor. This fuel substitution will contribute to reducing emissions by up to 350 tCO2/year, which is equivalent to taking 53,000 vehicles in a city off the road for one day. The biomethane is from Naturgy's production plant at the Elena landfill.
- Supply of **renewable gas to the first bus** in Zaragoza. In partnership with Consorcio de Transportes del Área de Zaragoza, Automóviles Zaragoza, Scania and Calvera, Naturgy supplied 150 MWh of biomethane from the company's plant in Vilasana (Lleida) for the purification of biogas obtained from slurry digestion. This biomethane was used to propel a city bus, which ran for three months between Zaragoza and Villamayor de Gállego.
- Alliance for the development of **hydrogen mobility**. Signature of an agreement with Enagás, through its subsidiary Scale Gas, and Exolum, to jointly study and develop infrastructures for the production, distribution and supply of green hydrogen in the mobility sector nationwide. This is the first major alliance for hydrogen in mobility corridors. The project will be called Win4H2. The agreement covers the development of a network of 50 hydrogen service stations, which will offer homogeneous penetration of this energy vector in Spain, enabling any user to choose the green hydrogen solution with guaranteed supply in 100% of mainland Spain.

6. Non-financial information statement

The non-financial information statement for the year 2021, referred to in articles 262 of the Capital Companies Law and 49 of the Commercial Code, is presented in a separate report called “Sustainability report and Non-financial information statement 2021”, in which it is indicated, expressly, that the information contained in said document is part of the Naturgy Group's consolidated directors’ report (Appendix II).

This document is subject to verification by an independent verification service provider and is subject to the same approval, deposit and publication criteria as the Naturgy Group's consolidated directors’ report.

7. Additional information

7.1 Treasury shares

Movements during 2021 and 2020 involving the treasury shares of Naturgy Energy Group, S.A. are as follows:

	Number of shares	In million euro	% Capital
At 1 January 2020	**5,183,890**	**121**	**0.5**
Share Acquisition Plan	470,000	8	—
Delivered to employees	(455,797)	(8)	—
2019 buyback programme	9,346,025	178	0.9
Capital reduction	(14,508,345)	(298)	(1.4)
At 31 December 2020	**35,773**	**1**	**—**
Share Acquisition Plan	127,453	3	—
At 31 December 2021	**163,226**	**4**	**—**

In 2021 and 2020, no gains or losses were made on transactions involving the Company’s treasury shares.

On 5 March 2019, the shareholders in general meeting authorised the Board of Directors to purchase, within five years, in one or more operations, fully paid Company shares; the nominal value of the shares directly or indirectly acquired, added to those already held by the Company and its subsidiaries, must not exceed 10% of share capital or any other limit established by law. The price or value of the consideration may not be lower than the par value of the shares or higher than their quoted price.

The minimum and maximum acquisition price will be the share price on the continuous market of the Spanish stock exchanges, within an upper or lower fluctuation of 5%.

Transactions with the Company’s Treasury shares relate to:

2021

- Share acquisition plan: In accordance with the resolutions adopted by the shareholders of Naturgy Energy Group, S.A. at the general meeting held on 5 March 2019, within the Share Acquisition Plan 2020-2023, the one relating to 2021 addressed to Naturgy employees in Spain who decide voluntarily to take part in the Plan was set in motion. The Plan enables participants to receive part of their remuneration in the form of shares in Naturgy Energy Group, S.A., subject to an annual limit of Euros 12,000. In December 2021, 127,453 of the Company's own shares were acquired for Euros 3 million to be handed over to the employees taking part in the Plan. The shares will be delivered in January 2022.

2020

- Share acquisition plan: In accordance with the resolutions adopted by the shareholders of Naturgy Energy Group, S.A. at the general meeting held on 5 March 2019, within the Share Acquisition Plan 2020-2023, the one relating to 2020 addressed to Naturgy employees in Spain who decide voluntarily to take part in the Plan was set in motion. The Plan enables participants to receive part of their remuneration in the form of shares in Naturgy Energy Group, S.A., subject to an annual limit of Euros 12,000. During 2020, 470,000 treasury shares were acquired for Euros 8 million to be handed over to the employees taking part in the Plan and 455,797 shares were delivered, leaving a surplus of 14,203 shares.

- 2019 share buyback programme: The Board of Directors of Naturgy Energy Group, S.A. approved a treasury share buyback programme, which was published on 24 July 2019, with a maximum investment of Euros 400 million to 30 June 2020 representing approximately 2.1% of share capital on the date of notification, the redemption of which was ratified by the shareholders at the annual general meeting held on 26 May 2020. At 30 June 2020, a total of 14,508,345 treasury shares had been acquired under this programme at an average price of 20.6 euros per share, representing a total cost of Euros 299 million (5,162,320 treasury shares at an average price of 23.3 euros per share with a total cost of Euros 121 million at 31 December 2019), which were applied to reduce capital.

- Capital reduction: At a meeting held on 21 July 2020, the Board of Directors of Naturgy Energy Group, S.A. resolved to implement the capital reduction resolution approved at the annual general meeting of shareholders held on 26 May 2020, whereby it approved a reduction in the share capital of Naturgy Energy Group, S.A. to a maximum of Euros 21,465,000, relating to:

  (a) the 465,000 treasury shares held by the Company at close of trading on 24 July 2019.

  (b) the 21,000,000 additional shares with a par value of one euro each which were acquired and may continue to be acquired for redemption by the Company under the treasury share buyback programme (the "Buyback Programme") approved by the Company under Regulation (EU) No. 596/2014 on market abuse and disclosed as price-sensitive information on 24 July 2019 (registration number 280517). The time limit for acquiring these shares was 30 June 2020.

  In this respect, as Naturgy Energy Group, S.A. had acquired a total of 14,043,345 shares at 30 June 2020 under the approved buyback programme referred to in paragraph (b) above, the Board of Directors set the figure for the capital reduction at Euros 14 million (the "Capital Reduction") and agreed to implement this reduction. The Capital Reduction was carried out through the redemption of 14,508,345 treasury shares with a par value of 1 euro each, representing approximately 1.47% of the Company's share capital at the time of adoption of the resolution in question. Following the Capital Reduction share capital stood at Euros 970 million, made up 969,613,801 shares with a par value of 1 euro each.

7.2. Disclosure of delays in payment to suppliers. Additional Provision 3 "Duty of disclosure" of Law 15/2010/5 July

The total amount of payments made during the year, with details of payment periods, in accordance with the maximum legal limit under Law 15/2010 of July 5, which laid down measures against late payment, is as follows:

	2021	2020
	Amount	**Amount**
Total payments (thousand euro)	615,883	458,021
Total outstanding payments (thousand euro)	13,528	18,284
Average supplier payment period (days) (1)	38	32
Transactions paid ratio (days) (2)	38	32
Transactions pending payment ratio (days) (3)	40	38

(1) Calculated on the basis of amounts paid and pending payment.

(2) Average payment period in transactions paid during the year.

(3) Average age, suppliers pending payment balance.

7.3. Subsequent events

Events subsequent to the end of the period are described in Note 30 of the Notes to the Annual Accounts.

8. Annual Corporate Governance Report

The Annual Corporate Governance Report for the year 2021 of the Company is included as an Annex to the consolidated Management Report of Naturgy, in accordance with the provisions of Article 49.4 of the Commercial Code and in accordance with Article 538 of the Capital Companies Law. Likewise, this report will be available from the publication of these accounts on the corporate website (www.naturgy.com) and on the website of the CNMV (www.cnmv.com).

9. Annual Directors' Remuneration Report

The Annual Directors' Remuneration Report for the year 2021 is included as an Annex to the consolidated Directors' Report of Naturgy, in accordance with Article 538 of the Capital Companies Law. Likewise, this report will be available from the publication of these accounts on the corporate website (www.naturgy.com) and on the website of the CNMV (www.cnmv.com).