MADRILEÑA RED DE GAS, S.A.
(Sociedad Unipersonal)

Independent Auditor's Report at December 31, 2018 pwc

INDEPENDENT AUDITOR'S REPORT

To the Directors of Madrileña Red de Gas, S.A. (Sociedad Unipersonal):

Opinion

We have audited the financial statements of Madrileña Red de Gas, S.A. (Sociedad Unipersonal) company, which comprise the balance sheet as at December 31, 2018, the income statement, the statement of comprehensive income, the total statement of changes in equity and the cash flow statement for the year then ended, and notes to the financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying financial statements of Madrileña Red de Gas, S.A. (Sociedad Unipersonal) for the year ended on December 31, 2018 are prepared, in all material respects, in accordance with the International Financial Reporting Standards adopted by the European Union.

Basis for Opinion

We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Statements* section of our report.

We are independent of the Company in accordance with the ethical requirements of the International Ethics Standards Board for Accountant (IESBA Ethic Code), and we have fulfilled our other ethical responsibilities in accordance with these requirements.

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

Emphasis of Matter

Basis of Accounting and Restriction on Distribution

We draw attention to Notes 3 and 4 to the financial statements, which describes the basis of accounting and the conciliation between the IFRS-EU and the Spanish accounting standards. The financial statements are prepared to show the financial position of the Company and its financial performance in accordance with the International Financial Reporting Standards adopted by the European Union. As a result, the financial statements may not be suitable for another purpose. Our report is intended solely for the Directors of Madrileña Red de Gas, S.A. (Sociedad Unipersonal). Our opinion is not modified in respect of this matter.

Additionally, we draw attention to Note 3.1.3 of the financial statements, which describes that the Company has modified in 2017 the period-end closing date, that in previous years ended on June 30 and, as a consequence, this fact has to be taken into consideration when comparing the figures of the year of 6 months ended on December 31, 2017 with the figures of the year of 12 months ended on December 31, 2018. Our opinion is not modified in respect of this matter.

Other matters

The present financial statements have not been prepared in accordance with any legal requirements and have been audited in accordance with International Standards on Auditing (ISAs), as a result the present report in no case could be understood as an audit report in the terms established in applicable financial statement auditing standards in Spain.

Madrileña Red de Gas, S.A. (Sociedad Unipersonal) has prepared separately the annual accounts for the year ended on December 31, 2018, in accordance with the applicable financial statement auditing standards in Spain, on which we gave our separate audit opinion on March 27, 2019, to the sole shareholder of Madrileña Red de Gas, S.A. (Sociedad Unipersonal).

Responsibilities of the Directors and the Audit for the Financial Statements

Management is responsible for the preparation of these the financial statements in accordance with the International Financial Reporting Standards adopted by the European Union and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, management is responsible for assessing the Company's ability to continue as a going concern, disclosing, as applicable, matters relating to going concern and using the going concern basis of accounting unless management either intends to liquidate the Company or to cease operations, or has no realistic alternative but to do so.

Auditor's Responsibilities for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the financial statements 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 International Standards on Auditing (ISAs) 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 financial statements.

As part of an audit in accordance with ISAs, we exercise professional judgment and maintain professional scepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the financial statements, 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 Partnership's internal control.

- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the 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 financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Company to cease to continue as a going concern.

- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.

We communicate with the Directors 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.

PricewaterhouseCoopers Auditores, S.L.

Juan Manuel Anguita Amate

March 27, 2019

MADRILEÑA RED DE GAS, S.A.U.

Financial statements under IFRS corresponding to the year ended on December 31st 2018

MADRILEÑA RED DE GAS, S.A.U.

BALANCE SHEET AT DECEMBER 31st 2018
(Expressed in thousand of euros)

ASSETS	Note	31/12/2018	31/12/2017
NON-CURRENT ASSETS		**1,191,081**	**1,209,496**
Intangible assets	7	805,773	803,853
Property, plant and equipment	8	358,522	373,091
Financial assets at amortized cost	9	1,854	5,273
Deferred income tax assets	17	24,932	27,279
CURRENT ASSETS		**118,857**	**678,874**
Inventories	11	2,651	3,508
Trade and other receivables at amortized cost	9,10	52,490	58,580
Deferred expenses		674	761
Cash and cash equivalents	12	63,042	616,025
TOTAL ASSETS		**1,309,938**	**1,888,370**

EQUITY AND LIABILITIES	Note	31/12/2018	31/12/2017
EQUITY		**233,274**	**304,800**
Capital	13	1,048	1,048
Share premium	13	100,354	222,954
Reserves	13	80,867	64,298
Profit/(loss) for the year		51,005	16,500
NON-CURRENT LIABILITIES		**1,016,969**	**1,007,518**
Non-current provisions	16	4,661	5,737
Other non-current liabilities	9,14	1,656	1,841
Payables to related parties	9,14,20	942,640	941,481
Deferred income	15	17,775	18,092
Deferred income tax liabilities	17	50,237	40,367
CURRENT LIABILITIES		**59,695**	**576,052**
Current provisions	16	2,336	2,854
Financial liabilities	9,14	84	4,460
Payables to related parties	9,14,20	12,007	517,587
Trade and other payables	9,14	45,268	51,151
TOTAL EQUITY AND LIABILITIES		**1,309,938**	**1,888,370**

Notes 1 to 24 set out in the attached report form an integral part of these financial statements.

MADRILEÑA RED DE GAS, S.A.U.

INCOME STATEMENT CORRESPONDING TO THE YEAR ENDED ON DECEMBER 31st 2018
(Expressed in thousand of euros)

CONTINUING OPERATIONS	Note	31/12/2018	31/12/2017
Revenues	18	186,278	85,627
Raw materials and consumables	18	(15,170)	(7,665)
Other income	15	1,641	798
Staff costs	18	(11,668)	(7,010)
Other operating expenses	18	(21,936)	(11,156)
Amortisation and depreciation	7,8	(27,787)	(15,597)
Provision excess		-	1,291
Other results	18	(746)	(220)
OPERATING PROFIT/(LOSS)		**110,612**	**46,068**
Financial income	18	33	699
Financial costs	18	(42,896)	(24,695)
NET FINANCIAL INCOME/(EXPENSE)		**(42,863)**	**(23,996)**
PROFIT/(LOSS) BEFORE INCOME TAX		**67,749**	**22,072**
Income tax	17	(16,744)	(5,572)
PROFIT/(LOSS) FOR THE PERIOD		**51,005**	**16,500**

Notes 1 to 24 set out in the attached report form an integral part of these financial statements.

MADRILEÑA RED DE GAS, S.A.U.

STATEMENT OF CHANGES IN EQUITY CORRESPONDING TO THE YEAR ENDED ON DECEMBER 31st 2018
(Expressed in thousand of euros)

A) STATEMENT OF COMPREHENSIVE INCOME

	Note	31/12/2018	31/12/2017
Profit for the period		**51,005**	**16,500**
Items that will not be reclassified to profit or loss:			
On actuarial gains and losses and other adjustments (net of tax)	**16**	69	(15)
Other comprehensive income for the period, net of tax		**69**	**(15)**
Total comprehensive income for the period		**51,074**	**16,485**

Notes 1 to 24 set out in the attached report form an integral part of these financial statements.

MADRILEÑA RED DE GAS, S.A.U.

STATEMENT OF CHANGES IN EQUITY CORRESPONDING TO THE YEAR ENDED ON DECEMBER 31st 2018
(Expressed in thousand of euros)

B) TOTAL STATEMENT OF CHANGES IN EQUITY

	Capital (Note 13)	Share premium (Note 13) (Note 13)	Reserves (Note 13)	Profit/(loss) for the period Note	Total
BALANCE AT 30 JUNE 2017	**1,048**	**224,797**	**48,533**	**48,937**	**323,315**
Profit for the period	-	-	-	16,500	**16,500**
Other comprehensive income	-	-	(15)	-	**(15)**
Operations with shareholders or owners					
Dividends	-	(1,843)	(33,157)	-	**(35,000)**
Other changes in equity	-	-	48,937	(48,937)	-
BALANCE AT 31 DECEMBER 2017	**1,048**	**222,954**	**64,298**	**16,500**	**304,800**
Profit for the period	-	-	69	51,005	51,074
Other comprehensive income	-	-	-	-	-
Operations with shareholders or owners					-
Dividends	-	(122,600)	-	-	(122,600)
Other changes in equity	-	-	16,500	(16,500)	-
BALANCE AT 31 DECEMBER 2018	**1,048**	**100,354**	**80,867**	**51,005**	**233,274**

Notes 1 to 24 set out in the attached report form an integral part of these financial statements.

MADRILEÑA RED DE GAS, S.A.U.

CASH FLOW STATEMENT CORRESPONDING TO THE YEAR ENDED ON DECEMBER 31st 2018
(Expressed in thousand of euros)

A) CASH FLOW FROM OPERATING ACTIVITIES	Notes	31/12/2018	31/12/2017
1. Profit/(loss) for the period before income tax		**67,749**	**22,072**
2. Adjustments for:		**69,949**	**40,124**
Amortisation and depreciation (+)	7,8	27,787	15,597
Impairment adjustments (+/-)		940	1,479
Change in provisions (+/-)		-	1,142
Release of grants (-)	15	(1,641)	(798)
Financial income (-)		(33)	(699)
Financial expenses (+)	18	42,896	24,695
Other income and expenses (+/-)		-	(1,292)
3. Changes in working capital		**(111)**	**27,528**
Inventories (+/-)		746	76
Trade and other receivables (+/-)	10	5,061	14,945
Other current assets (+/-)		87	175
Creditors and other payables (+/-)	14	(4,333)	12,456
Other non-current liabilities (+/-)		(1,672)	(124)
4. Other cash flow from operating activities		**(53,197)**	**(32,900)**
Interest paid (-)	14	(47,356)	(32,107)
Interest received (+)		33	699
Income tax (paid)/received (+/-)	17	(5,874)	(1,544)
Other amounts paid (received) (-/+)		-	52
A) Cash flow from operating activities (+/-1+/-2+/-3+/-4)		**84,390**	**56,824**
B) CASH FLOW FROM INVESTING ACTIVITIES			
6. Amounts paid on investments (-)		**(16,330)**	**(9,304)**
Intangible assets	7	(3,022)	(1,872)
Property, plant and equipment	8	(13,308)	(7,432)
7. Amounts collected from divestments (+)		**4,609**	**3**
Other financial assets		3,418	-
Fixed assets		1,191	3
B) Cash flow from investing activities (7-6)		**(11,721)**	**(9,301)**
C) CASH FLOW FROM FINANCING ACTIVITIES			
9. Amounts collected from grants		**1,323**	**505**
Grants	14	1,323	505
10. Collections and payments financial liability instruments		**(500,000)**	**-**
Payables to related parties (+)		(500,000)	-
11. Dividend payments		**(126,975)**	**(30,625)**
C) Cash flow from financing activities		**(625,652)**	**(30,120)**
NET INCREASE/(DECREASE) IN CASH OR CASH EQUIVALENTS		**(552,983)**	**17,403**
Cash and cash equivalents at the beginning of the period		616,025	598,622
Cash and cash equivalents at the end of the period		**63,042**	**616,025**

Notes 1 to 24 set out in the attached report form an integral part of these financial statements.

MADRILEÑA RED DE GAS, S.A.U.

NOTES TO THE FINANCIAL STATEMENTS CORRESPONDING TO THE YEAR ENDED ON DECEMBER 31st 2018
(Expressed in thousand of euros)

1. General information

Madrileña Red de Gas, S.A.U. (hereinafter, the Company) is a Spanish public limited liability company, that was incorporated on July 3rd, 2009 under the registered name of GEM Servicios Comunes 2, S.L. The Company subsequently changed its registered name to Madrileña Servicios Comunes, S.L.U. on February 15th, 2010, and then to its current name as a result of the merger through absorption with Madrileña Red de Gas, S.A.U. on June 30th, 2011.

Its current registered and tax address is in "Centro Empresarial Arco, calle Virgilio n° 2-B Edificio 1, 28223 Pozuelo de Alarcón (Madrid)".

Madrileña Red de Gas, S.A.U. is the company resulting from the merger through absorption of Madrileña Red de Gas, S.A.U. (as the merging company) and Madrileña Red de Gas II, S.A.U. (as the merged company) carried out on December 17th, 2013.

The merged company was incorporated on September 13th, 2010, resulting from the merger through absorption of Nueva Madrileña de Gas, S.A.U. (as the merging Company) and Madrileña Red de Gas II, S.A.U. (as the merged company) carried out on May 31st, 2012. Under this transaction the merging company Nueva Madrileña de Gas, S.A.U. changed its corporate form and its name to Madrileña Red de Gas II, S.A.U.

On May 7th 2015, the Company Elisandra Spain V, S.L.U. acquired the 100% of the Company's shares of MSIP Violin BV, and became part of the Group, whose ultimate parent company is Elisandra Spain IV, S.L (sole shareholder of Elisandra Spain V, S.L.U.), whose shareholders turn are Realgaz, S.A.S (formerly called C41, S.A.S)., Stichting Depositary PGGM Infrastructure Funds, JCSS Mike S.A.R.L and Lancashire County Pension Fund. The consolidated annual accounts of the Group for the year ended December 31st 2017 and prepared under IFRS were adopted by the General Meeting of Shareholders of April 25th 2018 and filed with the Mercantile Registry of Madrid.

On July 25th, 2017, The General Meeting of Shareholders approved the transfer of the shareholdings held by Lancashire County Pension Fund, representing 12.50% of the share capital of Elisandra Spain IV, S.L to LPPI Insfrastructure Investment LP. By October 2017 Lancashire County Pension Fund had contributed its 12.5% stake in the company to the pooled investments vehicle, LPPI Infrastructure Investments LP, which is owned by it and the London Pension Fund Authority.

Elisandra Spain IV, S.L. has its registered office and tax address located at Calle Virgilio, 2B, edificio 1, Pozuelo de Alarcón, Madrid.

MADRILEÑA RED DE GAS, S.A.U.

NOTES TO THE FINANCIAL STATEMENTS CORRESPONDING TO THE YEAR ENDED ON DECEMBER 31st 2018
(Expressed in thousand of euros)

The Company's financial year ran from July 1st to June 30th of the following calendar year. On May 31st 2017, the Company's Board of Directors approved the change in the financial year, which will now run from January 1st to December 31st commencing from January 1st 2018. This resulted in a new interim financial period commencing on July 1st, 2017 and finishing on December 31st 2017 (Note 3.1.3).

The Company's corporate purpose is the distribution and secondary transmission of natural gas as well as the distribution and sale of piped liquefied petroleum gas (LPG). The activities included in its corporate purpose may be carried out in full or in part indirectly through the holding of shares or interests in companies having identical or analogous purposes in accordance with legislation on the hydrocarbon sector.

2. Regulatory framework

Main characteristics of the Spanish gas sector

The Spanish gas sector is regulated by Law 34/1998, of October 7th on the hydrocarbons sector, amended by Law 12/2007, of July 2nd Royal Decree-Law 13/2012 and Law 18/2015, of May 21st as well as Law 18/2014, of October 15th and by its enabling regulations, the most relevant being Royal Decree 1434/2002, of December 27th Royal Decree 949/2001, of August 3rd and Royal Decree 984/2015, of October 30th.

The Ministry of the Ecological Transition, previously denominated Ministry of Energy, Tourism and the Digital Agenda (MINETAD), is the competent organization responsible for the regulation of the gas and electricity industries, while the National Markets and Competition Commission (CNMC) is the regulatory authority in charge of maintaining and ensuring effective competition and transparent functioning of the Spanish energy industries. Prior to the publication of Law 3/2013 of June 4th, these functions were performed by the National Energy Commission (CNE), which was later integrated into the CNMC. The Ministries belonging to the Regional Governments also have competencies in legislative enactment and regulatory powers.

Royal Decree Law 1/2019, of 11 January, on urgent measures to bring the competencies of the National Commission on Markets and Competition into line with the requirements of Community Law with respect to Directives 2009/72/EC and 2009/73/EC of the European Parliament and of the Council, of 13 July 2009, on the common rules for the internal market in electricity and natural gas, amended Law 3/2013, of 4 June, on the creation of the National Commission on Markets and Competition; Law 34/1998, of 7 October, on the hydrocarbon sector; Law 24/2013, of 26 December, on the Electricity Sector; and Law 18/2014, of 15 October, approving urgent measures for growth, competition and efficiency.

With respect to the aspects subject to amendment, first of all, a mechanism is brought in to ensure consistency in the exercise of the competencies pertaining to the regulator with exclusive competence on the basis of the energy scheme that article 149.1.25.ª of the Spanish Constitution attributes to Central Government, defining for such purposes a procedure which, in any event, guarantees the independence of the regulatory authority in approving legislative circulars, while foreseeing a prior reconciliation arrangement in order to attempt to deliver a mutually agreed solution in the event of discrepancy. In this way, the rule envisages that prior to the start of processing of the National Commission on Markets and Competition's legislative circulars, the Government, through an order of the Ministry of Ecological Transition, may establish the energy policy guidelines to be taken into account in the circular that is approved by the National Commission on Markets and the Competition. In such cases, and prior to the approval of the legislative circular, the Ministry of Ecological Transition may issue a report on the consistency of the proposal with such guidelines. In the event of discrepancies between the parties, a Cooperation Committee will be formed in order to seek an understanding between the both parties.

If there are no discrepancies or if there are, an understanding has been reached between the parties, the legislative circulars approved by the National Commission on Markets and the Competition will state that they are adopted «in accordance with the energy policy guidelines of the Ministry of Ecological Transition ». Otherwise, they will indicate that they are adopted «having heard the Ministry of Ecological Transition ».

Second, with respect to the remuneration of gas and electricity transport and distribution activities and of liquefied natural gas plants (except for underground natural gas storage facilities), the rule specifies that the National Commission on Markets and Competition will approve the methodology, the remuneration parameters, the asset regulatory base and the annual remuneration of the activity. In any event, the financial remuneration rate may not exceed the threshold established by Law for the regulatory period. For electricity and natural gas network access tolls, it is established that apart from the toll methodology, the regulatory authority will approve their structure and specific values, with the Ministry of Ecological Transition being tasked with approving the structure of the charges, methodology and values.

Third, in relation to the terms of access and connection to the electricity and natural gas transport and distribution network, the National Commission on Markets and the Competition will be tasked with approving the methodology and conditions of access and connection that will comprise the economic criteria, and with assessing capacity, reasons for rejection, content of the requests, permits and contracts and the obligations of publicity and transparency regarding relevant access and connection information.

Fourth, the National Commission on Markets and Competition will be tasked with regulating the rules on the functioning of organised markets in terms of their regulated component in those aspects approval of which pertains to the national regulatory authority, in accordance with European Community law. In preparing the legislative circulars relating to the remuneration of regulated activities, network access tolls and access and connection terms and conditions and the rules on the functioning of organised markets, the National Commission on Markets and the Competition should take into account the energy policy guidelines that have been defined by the Ministry of Ecological Transition.

Fifth, the new regulation provides that the remuneration of the electricity system operator and gas system technical manager will be that established by the National Commission on Markets and the Competition, it clarifies the control function with respect to the transport network investment plans and re-defines the distribution of competencies under the disciplinary and inspection regime, in line with the function changes brought in.

Finally, it establishes a transitional regime for all the changes that are brought in, in order to ensure an orderly transfer of functions and that the legal certainty of the sector players is not affected.

Furthermore, the Technical Manager of the System, Enagás, S.A., is responsible for the appropriate functioning and coordination of the gas system. Law 12/2007 of July 2nd limits the shareholding in Enagás, S.A. to a maximum of 5% of its share capital, voting rights to 3% in general, and to 1% participants in gas activities, and in any event, the sum of the interest of the shareholders undertaking activities in the gas sector cannot exceed 40%.

In general, the Spanish gas sector has the following main characteristics:

- It is an industry in which regulated and unregulated activities coexist. The regulated activities consist of transport, regasification, storage and distribution of natural gas. The non-regulated activities comprise production, supply and retailing of natural gas.

- The natural gas sector is entirely dependent on foreign supplies of natural gas, which represent almost 99.9% of the natural gas supply in Spain.

- Under EU legislation (Directives 2003/55/CE of June 26th, and 2009/73/UE of July 13th), the supply of natural gas in Spain is totally de-regulated, and all Spanish consumers can freely choose their natural gas provider as of 1st January 2003. The deregulation procedure for the industry has been reinforced substantially by the disappearance as of 1st July 2008 of the bundled tariff of distribution companies and the subsequent right of consumers to participate in the deregulated market (although as indicated further below a tariff of last resort has been maintained for consumers of lower consumption).

Regulation of natural gas activities in Spain

The natural gas activities are divided into: regulated activities: transport, storage, regasification and natural gas distribution; and non-regulated activities: production, supply and commercialization of natural gas.

2.1 Regulated activities

Regulated activities are characterized by:

- *Need for prior government authorization:* The undertaking of regulated activities requires prior regulated administrative authorization. In order to obtain this authorization, the applicant must demonstrate its legal, technical and economic capacity to exercise this activity. This authorization creates a legal monopoly for the regulated activity in a predetermined territory.

- *Remuneration established by legislation:* The general directives that set the remuneration for these activities are governed by Law 18/2014 of October 15th and Royal Decree 949/2001 of August 3rd while the specific remuneration to be received is updated annually by ministerial order.

  Thus, the remuneration framework incentivises the further development of the network infrastructure while allowing companies to recover investments made in the network and the operating costs incurred in undertaking regulated activities.

  The regulatory framework for the natural gas industry in Spain has a procedure for settlement compensation amongst companies in the sector for net billing of gas acquisition and other costs, so that each company receives the appropriate remuneration for their regulated activities.

- *Subjection to specific obligations:* The carrying out of regulated activities is subject to specific obligations to ensure the development of competition in retailing. The two main obligations in this sense consist of permitting access by third parties to the transport and distribution pipelines (including regasification and storage) and the obligation to keep the regulated and non-regulated activities separate.
  Royal Decree 948/2015, of October 30th regulates access by third parties to the network, which is managed by a single telematic platform, as well as the rights and obligations of each person involved in the system, changing the procurement regime capacity established in 2001 by Royal Decree 949/2001, of August 3rd. The owners of the transport and distribution pipelines have the right to receive tolls and levies in consideration for this access, which are updated annually under ministerial order.

The legislation establishes the duty of functional separation, which means not only accounting separation, in order to avoid cross-subsidization and increase the transparency of the calculation of rates, tolls and levies, and legal separation, through separate companies, but also the requirement of independent operation of the regulated subsidiary company with regard to the other companies in the group.

2.1.1 Transport

The transport activity includes regasification, storage and transport of gas through the high pressure gas pipeline network:

- *Regasification:* Natural gas is imported to Spain through a pipeline network (in gas form) and by gas tankers (in liquid form, hereinafter, liquefied natural gas). The regasification is the activity that involves the conversion of liquefied natural gas, stored in cryogenic tanks generally at regasification plants, into a gaseous state, which is then pumped into the national gas pipeline network.

- *Transport:* once the natural gas is imported or produced and, if necessary, regasified, it is injected in gas form into the high pressure gas pipeline transport network. The transport network crosses most regions in Spain and transports the natural gas to the major consumers, such as electricity plants and industrial customers and local distributors.

  The transport network is owned primarily by Enagás, S.A., although other companies own a small proportion of it.

- *Storage:* facilities consist mainly of underground tanks, which are necessary to ensure a constant supply of natural gas that is not affected by seasonal changes and other demand peaks. These facilities also serve to fulfil the obligation established by Royal Decree 1766/2007 of December 28th to maintain minimum security reserves. Current legislation also allows for unregulated underground storage facilities with third-party access, negotiated and previously authorised by the Spanish Government, although no such facilities currently exist.

The Royal Decree-Law 13/2014, of October 3rd, introduced a number of urgent measures in relation to the gas sector and ownership of nuclear plants.

This Royal Decree-Law formally accepted the relinquishment of the Castor natural gas storage plant and the termination of the concession to operate the plant held by Escal UGS, S.L. Additionally, the ongoing administration and maintenance of the facility was assigned to Enagás, S.A., with the related costs remunerated by the gas system. Finally, the amount of 1,351 million euros was paid to Escal UGS, S.L., based on the net value of the investment in the facility. This sum was paid by Enagás, S.A. in exchange for a claim against the gas system whereby the amount is to be recovered over the following 30 years.

In accordance with the Judgement of the Constitution Court of 21 December 2017, that declares articles 4 to 6 and article 2.2, additional provision one and transitional provision one of that Royal Decree Law, null and void, Ministerial Order TEC/1367/2018, of 20 December, does not include these collection rights of Enagás for 2019.

The Ministry Order ETU/1997/2016, of December 23rd, established the remuneration for the companies owning transport assets for the year 2017.

The Ministry Order ETU/1283/2017, of December 22nd, has established the remuneration for the companies owning transport assets for the year 2018.

The Ministry Order TEC/1367/2018, of December 20th has established the remuneration for the companies owning transport assets for the year 2019.

2.1.2 Distribution

Natural gas is transported from the high pressure transport pipeline network to the final consumer through the medium and lower pressure transport pipeline network owned by distribution companies.

According to Royal Decree-Law 5/2005, of March 11th, distribution businesses operate under a system of administrative authorisations that provides a distributor the right to exclusive operation within a given distribution zone. Additionally, Law 12/2007, of July 2nd, gives the distributor within a given zone the preference to obtain authorisations for adjoining zones.

Until July 1st, 2008, distributors also had the obligation to act as supplier of any consumer that accepted the regulated tariff. From July 1st, 2008 onwards, the distributor's activity is restricted to the expansion and management of distribution networks, with separate supply companies being responsible for the supply of gas to the end consumer, as discussed in section 2.2.2.

Royal Decree-Law 13/2012, of March 30th, transposes into Spanish law EU directives concerning common rules for internal gas and electricity markets, and electronic communications, as well as introducing measures to correct the deviations resulting from the imbalance between revenues and costs of the electricity and gas sector. In relation to the gas sector, measures introduced to correct the imbalance include the suspension of administrative authorisation of pipelines, except for those that are subject to international commitments, suspension of authorization of new regasification plants, as well as delays to remuneration of underground storage facilities.

Royal Decree-Law 8/2014, of July 4th, which was later transcribed into Law 18/2014, of October 17th, introduced measures for growth, competitiveness and efficiency. The key aspects of this Law as applied to the natural gas sector are described below:

- The principle of the gas system's economic and financial sustainability is established, whereby any regulation relating to the sector that entails an increase in costs for the gas system or a reduction in revenue must also bring an equivalent reduction in other cost items or an equivalent increase in revenue to ensure a balance in the system.

- The principle of economic and financial sustainability means that the revenue generated from the use of the facilities must meet all system costs. Gas system revenue will be employed solely to remunerate the regulated activities performed to supply gas.

- Annual deficits between system costs and revenue may not exceed 10% of revenue payable for the period, or the cumulative outstanding deficit within the system may not exceed 15%. If this sum is exceeded, tolls will be automatically revised to cover the portion that exceeds said limit. The portion of the deficit which, without exceeding the limits, is not offset by the rise in tolls and charges, will be financed by the parties to the settlement system, in proportion to the remuneration applicable to them. Each party will be entitled to recover its deficit contributions over the following five years including interest costs calculated using prevalent market rates.

- The remuneration methodologies for the natural gas sector will take into consideration the costs incurred by an efficient, well-managed company to perform the activity under the principle of realization whereby the activity must be performed at the lowest possible cost to the system.

- Regulatory periods spanning six years have been established for the remuneration of regulated activities, allowing for possible adjustments every three years to the system's remuneration parameters (including unit reference values for customers and sales, operating and maintenance costs, etc.) in the event of significant changes to revenue and costs of the system. The first regulatory period will end on 31st December 2020.

- The remuneration system for transmission, regasification and storage facilities is based on homogenous principles including the use of the net asset value of an operator as the basis for calculating investment remuneration, inclusion of variable remuneration based on gas transported, re-gasified or stored by asset type and elimination of all automatic review procedures for values and parameters based on price indices.

- With respect to new secondary transmission facilities, remuneration is included in the remuneration methodology for distribution facilities, linking remuneration to customers' growth and to new demand generated.

- With regard to distribution facilities, remuneration is calculated for each distribution company and all its facilities based on the number of customers connected and the volume of gas supplied. However, automatic reviews are eliminated based on the Consumer Price Index and Industrial Price Index, and the parametric remuneration formula is established to distinguish remuneration categories between supplies at pressures equal to or below 4 bars, between consumers with an annual consumption of less than 50 MWh and consumers with a higher consumption, so as to guarantee the adequacy of system revenue at all consumption levels, taking into account the toll revenues in each case. The remuneration established in the Order IET/2446/2013, of December 27th is maintained, for the period from January 1st of 2014 to when the Royal Decree-Law 8/2014 came into force.

- In order to incentivise network expansion to non-gasified zones and bring remuneration into line with actual costs incurred by companies, different unit values are used depending on whether or not customers and consumption are in recently-gasified municipalities.

- With respect to the gas system's accumulated deficit as at December 31st 2014, which is supported by the subjects of the liquidation system, has been recognised, in the final liquidation applicable to the year 2014. This deficit will be financed by facility owners over a 15-year period; annual payments will be included as a system cost including interest costs calculated using prevalent market rates. On December 1st, 2017, the Company subscribed a loan agreement with a banking entity for the nominal amount pending collection (Note 9).

- A new system cost is introduced corresponding to the remuneration of natural gas assigned to the tariff marked under the Algeria contract, supplied through the Maghreb pipeline, as a result of the Award issued by the Paris International Court of Arbitration on August 9th 2010. The amount to be collected is up to 164 million euros, and will be paid from the year 2015 during five years, including interest costs calculated using prevalent market rates.

Order ETU/1977/2016, of December 23rd established the remuneration for the regulated activities of the gas sector for 2017. Specifically, the initial remuneration recognised by Madrileña Red de Gas for the year 2017 was 140,010 thousand euros for the period between January 1 and December 31st of 2017.

Order ETU/1283/2017, of December 22nd, established the remuneration for the regulated activities of the gas sector for 2018. Specifically, the initial remuneration recognised by Madrileña Red de Gas for the year 2018 is 142,817 thousand euros for the period between January 1st and December 31st of 2018. The Order includes an adjustment of the remuneration for 2016 and 2017 for an amount of 2,432 thousand euros of higher income without assuming a significant impact on the income statement.

Order TEC/1367/2018 of December 20th has established the remuneration for the regulated activities of the gas sector for 2019. Specifically the initial remuneration recognized by Madrileña Red de Gas for the year 2019 is 142,299 thousand euros for the period between January 1st and December 31st of 2019.The order includes an adjustment of the remuneration for 2017 and 2018 for an amount of 1,700 thousand euros of higher income without assuming a significant impact on the income statement

During the year ended on June 30th 2017, the Company received the final liquidation of the regulated activities of the gas sector corresponding to the years 2014 and 2015, and its impact on the income statement was immaterial. The gas sector deficit of 2014, which includes the accumulated deficit in previous years, was 1,025 million euros (of which 47.4 million euros correspond to Madrileña Red de Gas, S.A.U.), which would be recoverable by the facility owners over a period of 15 years, from November 25th 2016 until November 24th 2031, including interest costs calculated using prevalent market rates. For the interest rate , in order ETU/1977/2016 a provisional interest rate of 1.104% was proposed by the CNMC and this interest has been defined like definitive in the order TEC/1367/2018. On December 1st 2017 The Company agreed the assignment of the account receivable derived from the gas deficit for the year 2014 (Note 10).

In 2015, the deficit was 27 million euros (of which 1.3 million euros correspond to Madrileña Red de Gas, S.A.U.), which will be recoverable by facility owners over a period of five years (from November 25th 2016 until November 25th 2021), including interest costs, which were yet to be established., However, in order ETU/1977/2016, the CNMC proposed a provisional interest rate of 0.836%, this interest has been defined like definitive in the order TEC/1367/2018, that considers the new collection right holders as parties to the clearing system due to the rights assigned.

During the 6 month fiscal year ended December 31st, 2017, the Company has received the final settlement of the regulated activities of the gas sector for 2016 without significant impacts on the profit and loss account. For 2016, the deficit figure has been closed at 90,01 million euros (of which 4,6 million euros correspond to Madrileña Red de Gas, SAU), which will be recoverable by the regulated subjects in five annuities at an interest rate in conditions equivalent to the market that is also not fixed yet, however, Order ETU/1283/2017 has proposed a provisional interest rate with the value of 0.503% as proposed by the CNMC, which has been defined as definitive interest rate of 0.716% by the Order TEC/1367/2018. On October 10th 2018, the Company has agreed the assignment of the account receivable derivated from the gas deficit for the years 2015 and 2016 (Note 10).

During the year ended on December 31th 2018, The company has received the final settlement of the regulated activities of the gas sector for 2017 without significant impacts on the profit and loss account. For 2017 the deficit figure has been closed at 24,8 million euros (of which 1,2 million euros correspond to Madrileña Red de Gas SAU) which will be recoverable by the regulated subjects in five annuities at an interest rate in conditions equivalent to the market that is also not fixed yet, however Order TEC/1367/2018 has stablished a definitived interest rate with the value of 0.923%.

2.2 Unregulated activities

2.2.1. Supplies

Taking into account the small volume of natural gas production in Spain, this section focuses on the international supply of natural gas.

The supply of natural gas in Spain is carried out mostly by gas operators through long-term contracts with gas producers. This supply, although being an unregulated activity, is subject to two types of limitations, the purpose of which is to ensure diversification of supply and the introduction of competition into the market: 1) no country can supply more than 60% of gas imported into Spain; and 2) since January 1st 2003 no business person or group can contribute, as a whole, natural gas for consumption in Spain that is greater than 70% of total national consumption, excluding self-consumption.

2.2.2. Commercialisation

As of July 1st 2008, under Law 12/2007, of July 2nd, and its enabling regulations, most importantly Royal Decree 1068/2007, of July 27, and Order 2309/2007, of July 30th, natural gas is supplied exclusively by gas supply companies, with supply under regulated tariffs (previously performed by distribution companies) been eliminated. Additionally, consumers connected at a pressure of less than 4 bar that did not exceed a certain consumption threshold (3 GWh, although this has been progressively reduced to the current 50 MWh/year) were entitled to be supplied at a maximum price called the last resort tariff (TUR). The calculation of the TUR is performed pursuant to legislation, and includes the cost of raw materials, access tolls, retailing costs and supply security costs.

In order to ensure that consumers do not have practical problems in changing their supply company, Law 12/2007, of July 2nd, ordered the creation of the Supplier Change Bureau, «Oficina de Cambios de Suministrador, S.A. (OCSUM)», which is owned by the major gas and electricity operators. As of July 2014, these functions were taken over by the CNMC.

Ministry of Industry, Energy and Tourism (MINETUR) issued Order ITC/1506/2010, of June 8th, establishing that a review of the TUR for natural gas be carried out under the ruling of the General Directorate of Energy Policy and Mines (DGPEM). The fixed and variable terms of the tariffs will be reviewed when there is a modification on the fixed and variables terms of the tolls and levies for access to the system or in the waste coefficients in force. The variable term will be reviewed quarterly, from the 1st day of the months of January, April, July and October of each year, provided that the cost of raw materials varies upward or downward by more than 2%.

Law 15/2012, of December 27th, on fiscal measures for energy sustainability included a number of changes affecting the natural gas sector including modifications to the tax on hydrocarbons, establishing a positive rate for natural gas employed as fuel in stationary motors, as well as for natural gas used for purposes other than as fuel (consumption). However, a reduced rate was established for natural gas employed for professional purposes once this was not used in generation or cogeneration of electricity.

With regards to energy efficiency, Royal Decree-Law 8/2014, of July 4th, subsequently approved as Law 18/2014, of October 15th, stipulates the following:

- The national energy efficiency obligations system is created, whereby gas and electricity supply companies, oil product wholesalers and liquefied petroleum gas (LPG) wholesalers will be allocated an annual energy-saving quota (saving obligations). Aggregate saving obligations will be equal to the target allocated to Spain in EU Directive2012/27/EU.

- The National Energy Efficiency Fund (FNEE) is created, to allow the implementation of economic and financial support mechanisms, technical assistance, training and information, or other measures to enhance energy efficiency in different sectors, which are necessary to achieve the Energy Efficiency Directive's objectives.

- The financial equivalence of the saving obligations will be determined based on the average cost of the support mechanisms, incentives and measures required to mobilise the investments necessary to fulfil the annual savings target, through actions by the FNEE, based on the findings of the technical analysis by the Institute for Energy Diversification and Saving.

- The Government is also authorised to establish and develop a final energy saving accreditation system, by issuing Energy Saving Certificates (ESC). Once launched, this will allow companies to progressively fulfil their saving obligations by directly promoting energy efficiency enhancement actions that fulfil the necessary guarantees.

Annually by Ministerial Order it established the obligations of contribution to the FNEE for each of the obligors.

Law 8/2015, of May 21st modifies Law 34/1998, of October 7th, of the Hydrocarbons Sector, introducing certain tax and non-tax measures in relation to the exploration, research and exploitation of hydrocarbons. This reform for sees the creation of an organised natural gas market organising activity across the Iberian Peninsula, facilitating the entry of new marketers and increasing competition, as well as establishing a new single operator of this market, responsible for managing the gas hub.

Royal Decree 984/2015, of October 30th, regulates the organised gas market and third-party access to natural gas system installations, while Resolution of December 4th 2015, issued by the Secretary of State for Energy (SEE), approved the market rules, membership contract and the resolutions of the organised gas market. The organised gas market, managed by MIBGAS, began operations in December 2015.

The SEE Resolution of June 6th 2016 approved various provisions concerning the organised gas market, including the number of market makers, the acquisition of cushion gas for Yela and the acquisition of heel gas and base gas.

The SEE Resolution of August 2nd 2016 approved the rules for the management of guarantees in the gas system. This Resolution lays down a standardised model for the provision of guarantees and determines the amount and duration of guarantees for mismatches in the virtual handover point and of guarantees required for contracting capacity, defines the valid instruments for concluding guarantees and, finally, establishes the protocol for communication with the Guarantee Manager and the action protocol in the event of non-compliance.

In addition, The SEE Resolution of August 2nd 2016 approved the framework contract for access to the facilities of the Spanish gas system. The purpose of the framework contract is for users (supply companies or direct customers in the market) to contract services for accessing the gas system facilities, excluding the contracting of handover point access services, to or from a gas pipeline connection with Europe.

Regulation of Liquefied Petroleum Gas (LPG)

The supply of piped LPG is regulated by Law 34/1998, of October 7th, of the Hydrocarbons sector.

The (MINETAD) (currently called Ministry of the Ecological Transition) establishes the selling rates for piped LPG for end consumers and the assignment prices of LPG at which it is purchased by piped LPG distributors, including specific rates and the methodology for automatically calculating and updating them. These selling rates are the maximum rate chargeable and apply to consumers in the whole of Spain, without prejudice to their specialties.

3. Basis for presentation

The most significant accounting policies and measurement criteria applied in the preparation of the Company's financial statements are described below. Such accounting policies have been applied consistently for all the periods presented, unless otherwise stated.

3.1.1 Transition to International Financial Reporting Standards (IFRS-EU) adopted by the European Union

The accompanying financial statements are prepared in accordance with the International Financial Reporting Standards (IFRS) and the International Financial Reporting Interpretation Committee (IFRIC) adopted by the European Union (all together, IFRS-EU), in line with the European Parliament Regulation and Council Regulation 1606/2002 and subsequent amendments, being these the first consolidated financial statement prepared under IFRS-EU.

The following financial statements have been prepared on a voluntary basis to show the equity and profit/loss for the operations according to IFRS, with the objective of comparing with other entities of the sector and to show the Company's financial magnitudes in accordance to an accounting framework that is globally recognized. The date for transition to IFRS was set as July 1st 2015.

For statutory purposes, and in order to comply with the legal obligations of corporate information, the Company has presented its annual accounts corresponding to the year ended on December 31st 2018 in accordance with the current mercantile legislation stated in the Code of Commerce reformed in accordance with Law 16/2007, of July 4th on reforming and adapting Spanish corporate accounting legislation for its international harmonization based on European legislation; RD 1514/2007, of November 20th (modified by RD 1159/2010, of September 17th), by which the General Chart of Accounts is approved; and RD 602/2016, of December 2nd.

The General Chart of Accounts (PGC) differs in certain aspects from IFRS. At the time of preparation of these financial statements, the Management has adjusted certain accounting and valuation principles applied to the annual accounts under PGC in order to comply with the IFRS. Additionally, December 31st 2018 and 2017, and the income statement at December 31st 2018 and 2017 have been re-stated including the effect of such adjustments.

The reconciliation of the transition effect from General Chart of Accounts to IFRS in the Company's equity and profit/loss for the year is shown in the Note 4.

These financial statements have been prepared under the historical cost convention.

The preparation of financial statements under IFRS-EU requires the Company to use certain estimates and judgements in relation to the future that are continuously assessed and are based on historical experience and other factors, including expectations of future events deemed reasonable under the circumstances. The estimates and assumptions that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are outlined in Note 6.

The IASB and the FASB have reached the same conclusions in many areas related to the accounting of leases, including the definition of a lease, the requirement, as a general rule, to reflect the leases in the balance sheet and the valuation of liabilities for leases. The IASB and the FASB also agreed not to incorporate substantial changes to the accounting by the lessor, maintaining requirements similar to those of the regulations previously in force.

However, there are still differences between the IASB and the FASB regarding the recognition and presentation of expenses related to leases in the income statement and in the statement of cash flows.

This standard will be applicable to annual periods beginning on or after January 1st 2019. Its application is permitted in advance if, at the same time, IFRS 15, "Ordinary income from contracts with customers" is adopted.

The Company is evaluating the possible impacts that the application of this rule could have in the future.

MRG has estimated that the amount of application of IFRS 16 that will come into effect next January 2019 amounts to 742 thousand euros to be recognized as assets and liabilities for leasing.

IFRS 9 (Modification) " Prepayment Features with Negative Compensation": The narrow-scope amendments made to AASB 9 Financial Instruments in December 2017 enable entities to measure certain prepayable financial assets with negative compensation at amortised cost. These assets, which include some loan and debt securities, would otherwise have to be measured at fair value through profit or loss.
To qualify for amortised cost measurement, the negative compensation must be 'reasonable compensation for early termination of the contract' and the asset must be held within a 'held to collect' business model. This standard will be applicable to annual periods beginning on or after January 1st 2019. Its application is permitted in advance.

IFRIC 23, " Uncertainty over Income Tax Treatments ": The interpretation explains how to recognise and measure deferred and current income tax assets and liabilities where there is uncertainty over a tax treatment. In particular, it discusses:

- how to determine the appropriate unit of account, and that each uncertain tax treatment should be considered separately or together as a group, depending on which approach better predicts the resolution of the uncertainty

- that the entity should assume a tax authority will examine the uncertain tax treatments and have full knowledge of all related information, ie that detection risk should be ignored

- that the entity should reflect the effect of the uncertainty in its income tax accounting when it is not probable that the tax authorities will accept the treatment

- that the impact of the uncertainty should be measured using either the most likely amount or the expected value method, depending on which method better predicts the resolution of the uncertainty, and

- that the judgements and estimates made must be reassessed whenever circumstances have changed or there is new information that affects the judgements.

While there are no new disclosure requirements, entities are reminded of the general requirement to provide information about judgements and estimates made in preparing the financial statements.

This standard will be applicable to annual periods beginning on or after January 1st 2019. Its application is permitted in advance

Norms, amendments and interpretations to existing standards, which have not been adopted by the European Union, and which have not been applied by the Company

At the date of approval of these consolidated annual accounts, the IASB and the IFRS Interpretations Committee had published the standards, amendments and interpretations detailed below, which are pending validation by the European Union:

- IFRS 10 (Amendment) and IAS 28 (Amendment) "Sale or contribution of assets between an investor and its associates or joint ventures".

- IFRS 17 "Insurance contracts".

- IAS 28 (Amendment) "Long-term interests in associates and joint ventures"

- Annual Improvements to IFRS Standards 2015-2017 Cycle (IFRS 3, IFRS 11, IAS 12 and IAS 23)

- Plan Amendment, Curtailment or Settlement – Amendments to IAS 19

- Amendments to IFRS 3 “Business definition”

- Amendments to IAS 1 and IAS 8 “Material definition”

3.1.3 Comparison of information

On May 31st 2017 the Board of Directors of the Group approved the modification of the year that until then comprised from July 1st to June 30th, and which will now coincide with the calendar year (from January 1st to December 31st). Consequently, previous year ended on December 31st 2017, in a transitory and exceptional way, includes from July 1st 2017 to December 31st 2017 (6 months). Therefore, each of the items of the balance sheet, the income statement, the statement of changes in equity and the cash flow statement and the notes to the financial statements relates to a 6-month period and consequently they are not directly comparable with the figures for the year ended on December 31st 2018.

3.2 Intangible assets

a) Goodwill

Goodwill represents the difference, at the acquisition date, between the cost of the combination of businesses and the fair value of the net identifiable assets acquired in the transaction. Therefore, goodwill is only recognised when it has been acquired for the consideration and related to future financial benefits from assets which cannot be identified individually and recognized separately.

Goodwill is not amortised but it is tested for impairment annually, or more frequently if events or changes in circumstances indicate that it might be impaired, and is carried at cost less accumulated impairment losses. Gains and losses on the disposal of an entity include the carrying amount of goodwill relating to the entity sold.

Goodwill is allocated to CGU for the purpose of impairment testing. The allocation is made to those CGUs or Groups of CGUs that are expected to benefit from the business combination in which the goodwill arose.

Value adjustments for impairment recognized in goodwill are not reversed in subsequent years.

b) Administrative authorisations

For the installation and commissioning of the distribution network in a specific distribution area, an administrative authorisation must be obtained.

In order to obtain the authorisation, the relevant distribution company must prove its legal, technical and economic capacity.

> a) Legal capacity: pursuant to Royal Decree 197/2010 of February 26th, it is necessary to be a limited liability company with Spanish nationality ("sociedad anónima") or from another EU member state.

b) Technical capacity: as set out in the RD 1434/2002 distribution companies are deemed to meet the required technical capacity levels.
c) Economic and financial capacity: as set out in the RD 1434/2002 distribution companies are deemed to have sufficient economic and financial capacity.

Most of the Company's administrative authorizations were acquired from Gas Natural Fenosa Group (currently called Naturgy).

The expenses incurred to obtain them have been recognised under the heading "Administrative Authorisations" as a part of the intangible assets. The administrative authorisations have an indefinite useful life (due to the fact that they allow the distribution network to be operated indefinitely) and therefore are not amortised, although any possible impairment is reviewed annually, valued at acquisition cost less accumulated impairment losses.

c) Software

Acquired computer software licences are capitalised on the basis of the costs incurred to acquire and bring to use the specific software. These costs are amortised over the assets' estimated useful life (4 years).

Costs associated with maintaining software programmes are recognised as an expense as incurred. Development costs that are directly attributable to the design and testing of identifiable and unique software products controlled by the Company are recognised as intangible assets when the following criteria are met:

- It is technically feasible to complete the software so that it will be available for use
- Management intends to complete the software and use or sell it
- There is an ability to use or sell the software
- It can be demonstrated how the software will generate probable future economic benefits
- Adequate technical, financial and other resources to complete the development and to use or sell the software are available, and
- The expenditure attributable to the software during its development can be reliably measured.

Expenses associated with software maintenance are recognised when incurred. Costs directly related to the production of identifiable and unique computer programs controlled by the Company and that will probably generate economic benefits exceeding costs beyond one year are recognised as intangible assets. Direct costs include the software development employee costs and an appropriate portion of relevant overheads.

3.3 Property, plant and equipment

Property, plant and equipment are recognised at fair value based on periodic valuations by external independent valuers, less subsequent depreciation for buildings. All other property, plant and equipment is recognised at historical cost less depreciation. Historical cost includes expenditure that is directly attributable to the acquisition of the items. Cost may also include transfers from equity of any gains or losses on qualifying cash flow hedges of foreign currency purchases of property, plant and equipment.

Subsequent costs are included in the asset's carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Company and the cost of the item can be measured reliably. The carrying amount of any component accounted for as a separate asset is derecognised when replaced. All other repairs and maintenance are charged to profit or loss during the reporting period in which they are incurred.

Increases in the carrying amounts arising on revaluation of land and buildings are recognised, net of tax, in other comprehensive income and accumulated in reserves in shareholders' equity. To the extent that the increase reverses a decrease previously recognised in profit or loss, the increase is first recognised in profit or loss. Decreases that reverse previous increases of the same asset are first recognised in other comprehensive income to the extent of the remaining surplus attributable to the asset; all other decreases are charged to profit or loss. Each year, the difference between depreciation based on the revalued carrying amount of the asset charged to profit or loss and depreciation based on the asset's original cost, net of tax, is reclassified from the property, plant and equipment revaluation surplus to retained earnings.

Depreciation is calculated using the straight-line method to allocate their cost or revalued amounts, net of their residual values, over their estimated useful lives or, in the case of leasehold improvements and certain leased plant and equipment, the shorter lease term as follows:

	Useful life
Plants (distribution network)	20 - 25
Other plant and machinery	8 - 20
LPG Plants	25 - 30

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at the end of each reporting period.

An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount (Note 3.4).

Gains and losses on disposals are determined by comparing proceeds with carrying amount.

These are included in profit or loss. When revalued assets are sold, it is Company policy to transfer any amounts included in other reserves in respect of those assets to retained earnings.

3.4 Impairment of assets

Goodwill and intangible assets that have an indefinite useful life are not subject to amortisation and are tested annually for impairment, or more frequently if events or changes in circumstances indicate that they might be impaired. Other assets are tested for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs of disposal and value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash inflows which are largely independent of the cash inflows from other assets or Groups of assets (cash-generating units). Non-financial assets other than goodwill that suffered an impairment are reviewed for possible reversal of the impairment at the end of each reporting period.

In this sense, for an analysis, the Company has included all assets in the CGU of gas distribution.

3.5 Financial assets

(i) Classification

From 1 January 2018, the group classifies its financial assets in the following measurement categories:

- those to be measured subsequently at fair value (either through OCI or through profit or loss), and
- those to be measured at amortised cost.

The classification depends on the entity's business model for managing the financial assets and the contractual terms of the cash flows. IFRS9(4.1.4),(5.7.1)

For assets measured at fair value, gains and losses will either be recorded in profit or loss or OCI. For investments in equity instruments that are not held for trading, this will depend on whether the group has made an irrevocable election at the time of initial recognition to account for the equity investment at fair value through other comprehensive income (FVOCI).

The group reclassifies debt investments when and only when its business model for managing those assets changes.

(ii) Recognition and derecognition

Regular way purchases and sales of financial assets are recognised on trade-date, the date on which the group commits to purchase or sell the asset. Financial assets are derecognised when the rights to receive cash flows from the financial assets have expired or have been transferred and the group has transferred substantially all the risks and rewards of ownership.

(iii) Measurement

At initial recognition, the group measures a financial asset at its fair value plus, in the case of a financial asset not at fair value through profit or loss (FVPL), transaction costs that are directly attributable to the acquisition of the financial asset. Transaction costs of financial assets carried at FVPL are expensed in profit or loss.

Financial assets with embedded derivatives are considered in their entirety when determining whether their cash flows are solely payment of principal and interest.

Debt instruments

Subsequent measurement of debt instruments depends on the group's business model for managing the asset and the cash flow characteristics of the asset. There are three measurement categories into which the group classifies its debt instruments:

- Amortised cost: Assets that are held for collection of contractual cash flows where those cash flows represent solely payments of principal and interest are measured at amortised cost. Interest income from these financial assets is included in finance income using the effective interest rate method. Any gain or loss arising on derecognition is recognised directly in profit or loss and presented in other gains/(losses) together with foreign exchange gains and losses. Impairment losses are presented as separate line item in the statement of profit or loss.

- FVOCI: Assets that are held for collection of contractual cash flows and for selling the financial assets, where the assets' cash flows represent solely payments of principal and interest, are measured at FVOCI. Movements in the carrying amount are taken through OCI, except for the recognition of impairment gains or losses, interest income and foreign exchange gains and losses which are recognised in profit or loss. When the financial asset is derecognised, the cumulative gain or loss previously recognised in OCI is reclassified from equity to profit or loss and recognised in other gains/(losses). Interest income from these financial assets is included in finance income using the effective interest rate method. Foreign exchange gains and losses are presented in other gains/(losses) and impairment expenses are presented as separate line item in the statement of profit or loss.

- FVPL: Assets that do not meet the criteria for amortised cost or FVOCI are measured at FVPL. A gain or loss on a debt investment that is subsequently measured at FVPL is recognised in profit or loss and presented net within other gains/(losses) in the period in which it arises.

Equity instruments

The group subsequently measures all equity investments at fair value. Where the group's management has elected to present fair value gains and losses on equity investments in OCI, there is no subsequent reclassification of fair value gains and losses to profit or loss following the derecognition of the investment. Dividends from such investments continue to be recognised in profit or loss as other income when the group's right to receive payments is established.

Changes in the fair value of financial assets at FVPL are recognised in other gains/(losses) in the statement of profit or loss as applicable. Impairment losses (and reversal of impairment losses) on equity investments measured at FVOCI are not reported separately from other changes in fair value.

(iv) Impairment

From 1 January 2018, the group assesses on a forward looking basis the expected credit losses associated with its debt instruments carried at amortised cost and FVOCI. The impairment methodology applied depends on whether there has been a significant increase in credit risk.

For trade receivables, the group applies the simplified approach permitted by IFRS 9, which requires expected lifetime losses to be recognised from initial recognition of the receivables.

(v) Accounting policies applied until 31 December 2017

The group has applied IFRS 9 retrospectively, but has elected not to restate comparative information. As a result, the comparative information provided continues to be accounted for in accordance with the group's previous accounting policy.

Classification

Until 31 December 2017, the group classified its financial assets in the following categories:

- financial assets at fair value through profit or loss,
- loans and receivables,
- held-to-maturity investments, and
- available-for-sale financial assets.

The classification depended on the purpose for which the investments were acquired. Management determined the classification of its investments at initial recognition and, in the case of assets classified as held-to-maturity, re-evaluated this designation at the end of each reporting period.

Reclassification

The group could choose to reclassify a non-derivative trading financial asset out of the held for trading category if the financial asset was no longer held for the purpose of selling it in the near term. Financial assets other than loans and receivables were permitted to be reclassified out of the held for trading category only in rare circumstances arising from a single event that was unusual and highly unlikely to recur in the near term. In addition, the group could choose to reclassify financial assets that would meet the definition of loans and receivables out of the held for trading or available-for-sale categories if the group had the intention and ability to hold these financial assets for the foreseeable future or until maturity at the date of reclassification

Reclassifications were made at fair value as of the reclassification date. Fair value became the new cost or amortised cost as applicable, and no reversals of fair value gains or losses recorded before reclassification date were subsequently made. Effective interest rates for financial assets reclassified to loans and receivables and held-to-maturity categories were determined at the reclassification date. Further increases in estimates of cash flows adjusted effective interest rates prospectively.

Subsequent measurement

The measurement at initial recognition did not change on adoption of IFRS 9, see description above.

Subsequent to the initial recognition, loans and receivables and held-to-maturity investments were carried at amortised cost using the effective interest method.

Available-for-sale financial assets and financial assets at FVPL were subsequently carried at fair value. Gains or losses arising from changes in the fair value were recognised as follows:

- for financial assets at FVPL – in profit or loss within other gains/(losses)
- for available-for-sale financial assets that are monetary securities denominated in a foreign currency – translation differences related to changes in the amortised cost of the security were recognised in profit or loss and other changes in the carrying amount were recognised in other comprehensive income
- for other monetary and non-monetary securities classified as available-for-sale – in other comprehensive income.

When securities classified as available-for-sale were sold, the accumulated fair value adjustments recognised in other comprehensive income were reclassified to profit or loss as gains and losses from investment securities.
Impairment

The group assessed at the end of each reporting period whether there was objective evidence that a financial asset or group of financial assets was impaired. A financial asset or a group of financial assets was impaired and impairment losses were incurred only if there was objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset (a 'loss event') and that loss event (or events) had an impact on the estimated future cash flows of the financial asset or group of financial assets that could be reliably estimated. In the case of equity investments classified as available-for-sale, a significant or prolonged decline in the fair value of the security below its cost was considered an indicator that the assets are impaired.

Assets carried at amortised cost

For loans and receivables, the amount of the loss was measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit losses that had not been incurred) discounted at the financial asset's original effective interest rate. The carrying amount of the asset was reduced and the amount of the loss was recognised in profit or loss. If a loan or held-to-maturity investment had a variable interest rate, the discount rate for measuring any impairment loss was the current effective interest rate determined under the contract. As a practical expedient, the group could measure impairment on the basis of an instrument's fair value using an observable market price.

If, in a subsequent period, the amount of the impairment loss decreased and the decrease could be related objectively to an event occurring after the impairment was recognised (such as an improvement in the debtor's credit rating), the reversal of the previously recognised impairment loss was recognised in profit or loss.

Assets classified as available-for-sale

If there was objective evidence of impairment for available-for-sale financial assets, the cumulative loss – measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that financial asset previously recognised in profit or loss – was removed from equity and recognised in profit or loss.

Impairment losses on equity instruments that were recognised in profit or loss were not reversed through profit or loss in a subsequent period.

If the fair value of a debt instrument classified as available-for-sale increased in a subsequent period and the increase could be objectively related to an event occurring after the impairment loss was recognised in profit or loss, the impairment loss was reversed through profit or loss.

Until 1 January 2018, the basis of presentation was the following:

a) Loans and receivables

Credits and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted on an active market and are not intended to be traded in the short-term. They are included in current assets, except for maturities longer than 12 months after the balance sheet date. These are classified as non-current assets.

These financial assets are initially recognized at fair value, including directly attributable transaction costs, and are subsequently measured at amortised cost. Accrued interest is recognized at the effective interest rate, which is the discount rate that brings the instrument's carrying amount into line with all estimated cash flows to maturity. Trade receivables falling due in less than one year are carried at face value at both initial recognition and subsequent measurement, provided that the effect of not discounting flows is not significant.

At the year-end, at least, the necessary value adjustments are made to account for impairment when there is objective evidence that all receivables will not be collected.

The amount of the impairment loss is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the effective interest rate prevailing at the date of initial recognition. Value adjustments, and reversals, where applicable, are recognized in the income statement.

b) Cash and cash equivalents

Cash and cash equivalents include cash at hand, time deposits with financial entities and other short-term investments noted for their great liquidity with an original maturity no longer than three months as from the acquisition date.

3.6 Financial liabilities

a) Trade and other payables

This category includes trade and non-trade payables and financial debts. Borrowings are classified as current liabilities unless the Company has an unconditional right to defer settlement for at least 12 months as from the balance sheet date.

Payables are initially recognized at fair value, adjusted for directly attributable transaction costs, and subsequently measured at amortized cost using the effective interest method. The effective interest rate is the discount rate that brings the instrument's carrying amount into line with the expected future flow of payments to the maturity date of the liability.

Trade payables falling due in less than one year without a contractual interest rate are carried at their face value at both initial recognition and subsequent measurement, provided that the effect of not discounting flows is not significant.

In the event of the renegotiation of existing debts, the financial liability is not deemed to change significantly when the lender of the new loan is the same as the initial lender and the present value of cash flows, including net fees, is not more than 10% higher or lower than the present value of cash flows payable on the original liability, calculated using the same method.

3.7 Inventories

Raw materials and stores, work in progress and finished goods are stated at the lower of cost and net realisable value. Cost comprises direct materials, direct labour and an appropriate proportion of variable and fixed overhead expenditure, the latter being allocated on the basis of normal operating capacity. Cost includes the reclassification from equity of any gains or losses on qualifying cash flow hedges relating to purchases of raw material but excludes borrowing costs. Costs are assigned to individual items of inventory on the basis of weighted average costs. Costs of purchased inventory are determined after deducting rebates and discounts. Net realisable value is the estimated selling price in the ordinary course of business less the estimated costs of completion and the estimated costs necessary to make the sale.

3.8 Equity

Ordinary shares are classified as equity.

Incremental costs directly attributable to the issue of new shares or options are shown in equity as a deduction, net of tax, from the proceeds.

Incremental costs directly attributable to the issue of new shares or options are shown in equity as a deduction, net of tax, from the proceeds.

When the Company purchases the company's equity instruments, the consideration paid, including any directly attributable incremental costs (net of income taxes) is deducted from equity attributable to the owners of the Company as treasury shares until the shares are cancelled or reissued. Where such ordinary shares are subsequently reissued, any consideration received, net of any directly attributable incremental transaction costs and the related income tax effects, is included in equity attributable to the owners.

The Company does not have any own shares.

Dividends on ordinary shares are recognized as a deduction from equity when they are approved.

3.9 Grants

Grants are recognised at their fair value where there is a reasonable assurance that the grant will be received and the Company will comply with all attached conditions. Government grants relating to costs are deferred and recognised in the profit or loss over the period necessary to match them with the costs that they are intended to compensate. Government grants relating to the purchase of property, plant and equipment are included in non-current liabilities as deferred income and are credited to profit or loss on a straight-line basis over the expected lives of the related assets.

3.10 Employee benefits

a) Pension commitments

Defined contribution pension plans

Under a fixed contribution plan, the Company makes fixed contributions to a separate entity and has no legal, contractual or implicit obligation to make additional contributions if this separated entity does not have sufficient assets to meet the commitments assumed.

The Company has recognised external defined contribution retirement and insured benefit plans to cover death and disability contingencies, which are in line with current pension plan and fund legislation and which cover its commitments to current personnel affected, It recognises certain economic rights for past services that are fully paid and is obligated to make a contribution of a percentage of computable salary according to the type of group. There are also defined retirement contribution plans to compensate management loyalty.

The annual contributions to cover the commitments accrued to the Company in relation to the plans are charged to the profit and loss account each year.

The Company recognises a liability in respect of the contributions to be made when at the year-end there are accrued contributions not paid.

b) Other post-employment obligations

The Company provide post-employment benefits to some of their retirees. The entitlement to these benefits is usually conditional on the employee remaining in service up to retirement age.

The expected costs of these benefits are accrued over the working life of the employees and the liability recognised for these commitments is equivalent to the current value of the obligation at the balance sheet date. The obligation for other commitments is calculated annually by the Company and it is reviewed by independent actuaries using the projected credit method. The current value of the obligation is determined by discounting the estimated future cash flows at a technical interest rate based in a curve of rates that takes into account the commitments duration and taking as reference the market performance, at the balance sheet date, corresponding to the emission of high credit rating bonds and obligations.

The Company's policy for amortizing the actuarial gains and losses of post-employment commitments consists of the immediate recognition in equity when they arise. The actuarial gains and losses arise from changes in the actuarial assumptions or from differences between the assumptions and reality.

c) Termination benefits

Termination benefits are payable when employment is terminated by the Company before the normal retirement date, or when an employee accepts voluntary redundancy in exchange for these benefits. The Company recognises termination benefits at the earlier of the following dates: (a) when the Company can no longer withdraw the offer of those benefits; and (b) when the entity recognises costs for a restructuring that is within the scope of IAS 37 and involves the payment of terminations benefits. In the case of an offer made to encourage voluntary redundancy, the termination benefits are measured based on the number of employees expected to accept the offer. Benefits falling due more than 12 months after the end of the reporting period are discounted to present value.

3.11 Provisions

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

The Company has the obligation to dismantle certain facilities at the end of its useful life. For this purpose, the present value of the cost of carrying value of these tasks is recorded in property, plant and equipment. This estimate is reviewed annually so that the provision reflects the present value of future costs by increasing or decreasing the value of the asset. The change in the provision arising from its financial update is charged to the "Financial expenses" caption.

Where there are a number of similar obligations, the likelihood that an outflow will be required in settlement is determined by considering the class of obligations as a whole. A provision is recognised even if the likelihood of an outflow with respect to any one item included in the same class of obligations may be small.

Provisions are measured at the present value of management's best estimate of the expenditure required to settle the present obligation at the end of the reporting period. The discount rate used to determine the present value is a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the liability. The increase in the provision due to the passage of time is recognised as interest expense.

Provisions maturing in one year or less, with an immaterial financial effect, are not discounted.

Where a part of the outflow necessary to settle the obligation is expected to be reimbursed by a third party, the reimbursement is recognised as a separate asset, just in the case that the collection is guaranteed.

The possible obligations coming as a consequence of past events, where its realization is conditioned to whether happens or not one or more future events independently of the Company's will are considered as contingent liabilities. Such contingent liabilities are not part of the accounting books and does not present details in the notes. (Note 23).

3.12 Income tax

The income tax expense or credit for the period is the tax payable on the current period's taxable income based on the applicable income tax rate for each jurisdiction adjusted by changes in deferred income tax assets and liabilities attributable to temporary differences and to unused tax losses.

The current income tax charge is calculated on the basis of the tax laws enacted or substantively enacted at the end of the reporting period in the countries where the company's subsidiaries and associates operate and generate taxable income. Management periodically evaluates positions taken in tax returns with respect to situations in which applicable tax regulation is subject to interpretation. It establishes provisions where appropriate on the basis of amounts expected to be paid to the tax authorities.

Deferred income tax is provided, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements. However, deferred income tax liabilities are not recognised if they arise from the initial recognition of goodwill. Deferred income tax is neither accounted for if it arises from initial recognition of an asset or liability in a transaction other than a business combination that at the time of the transaction affects neither accounting nor taxable profit nor loss. Deferred income tax is determined using tax rates (and laws) that have been enacted or substantially enacted by the end of the reporting period and are expected to apply when the related deferred income tax asset is realised or the deferred income tax liability is settled. The deferred tax liability in relation to investment property that is measured at fair value is determined assuming the property will be recovered entirely through sale.

Deferred income tax assets are recognised only if it is probable that future taxable amounts will be available to utilise those temporary differences and losses. Deferred income tax assets and liabilities are not recognised for temporary differences between the carrying amount and tax bases of investments in foreign operations where the company is able to control the timing of the reversal of the temporary differences and it is probable that the differences will not reverse in the foreseeable future.

Deferred income tax assets and liabilities are offset when there is a legally enforceable right to offset current tax assets and liabilities and when the deferred tax balances relate to the same taxation authority. Current tax assets and tax liabilities are offset where the entity has a legally enforceable right to offset and intends either to settle on a net basis, or to realise the asset and settle the liability simultaneously.

Current and deferred tax is recognised in profit or loss, except to the extent that it relates to items recognised in other comprehensive income or directly in equity. In this case, the tax is also recognised in other comprehensive income or directly in equity, respectively.

3.13 Revenue recognition

Revenues derived from contracts with customers must be 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 Madrileña Red de Gas 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. Revenue for the year includes the estimate of the energy supplied that has not yet been invoiced The 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 and transactions between Madrileña Red de Gas companies are eliminated.

In particular, the amount to receive from the regulated distribution and transmission activities, is calculated as described later.

The rights for the users' registrations are recorded as income in the year when the supply is contracted.

Revenue from services provided are only recognised when the amount of the gains, the realization grade, the incurred and outstanding costs, may be reliably estimated and it is probable that the economic benefits derived from the service will be collected. These gains are recognised considering the realization grade of the service provided at the balance sheet date.

Distribution activity

Note 2 describe the basic features of the regulations applicable to the Company.

The regulatory framework for the natural gas industry in Spain regulates a payment procedure for the redistribution amongst companies in the sector of the net turnover obtained, so that each company receives the remuneration recognised for its regulated activities.

The remuneration of the gas distribution is calculated and registered as income on the basis of the update of prior year remuneration, average increase of consumers, and the volume of energy circulated, according to the Ministerial Order that determines it each year and is adjusted by real data.

The remuneration gains from the distribution activities of each year are fixed with ex-ante character. In the Ministerial Orders that are published every year, a preview remuneration is established for the following year base on the sales expectations and customer attraction for the following year. This originates that the remuneration amount may be revised during two years, until the demands and customer's attraction data is analysed. Based on this, Order TEC/1367/2018 of December 20th has regularized the retribution for 2018 and 2017 and the order ETU/1283/2017 of December 22nd regularized the retribution for 2017 and 2016. according to the updated sales and customers' figures.

In the case of the distribution activity, the regulatory review carried out by Law 18/2014 was based on carrying out a new assessment of the remuneration bases of the agents who, reducing the total amount by approximately 110 million euros, considering positively the growth realized since the last regulatory review (realized in the year 2002) and giving a special value to the domestic consumption, that is the one that allows to introduce more tolls to the system. These remuneration bases will be updated annually, taking into account the increase in consumption and number of consumers connected to each distributor, especially encouraging the gasification of new municipalities, which will bring the national gasification index, currently 29%, to the countries average which are considerably higher. In order to do so, this law established unitary compensation values for each client and unit of energy incorporated, which in principle will remain fixed for the entire regulatory period (which will end on December 31st 2020) and, which are those applied to the growth's forecasts that each distributor has for the subsequent year, determine their provisional annual remuneration.

These Remunerations to the Distribution Activity will be adjusted once the Ministry of Industry, Energy and Tourism (currently called Ministry of ecological transition) establishes the definitive amounts of said remuneration from the actual figures of average increase of consumers and increase of vehicular kWh. The Company believes that there will be no significant differences between the amounts recorded and the final settlements.

However, these differences, when they occur, will be charged as a change of estimate in the Income Statement.

The Ministerial Order of October 28th 2002 by which the settlement procedures are regulated, establishes that the deviations occurred by the application of settlement procedures between the definite settled net gains and the credited remunerations each year, will be taken into account in the calculation of tariffs, tolls and levies for the following two years.

The Royal Decree-Law 8/2014, of July 4th (Note 2.1.2) establishes the accumulated deficit recognition of the gas system at December 31st 2014. The parties of the settlement system, including the Company, shall be entitled to recover said deficit for a period of fifteen years, with annuities to be included as a cost of the system and in which an interest rate shall be recognized in conditions equivalent to those of the market. On the other hand, the temporary mismatches produced between the revenues and costs of the gas system will be financed by the individuals in the settlement system, including the Company, generating a right to its recovery during the following five years, recognizing a type of interest in market conditions. As a result, the financing of the gas system's deficit of revenues is recorded as a financial asset according to which, under this regulation, there is the right to receive its refund without being subject to future contingent factors.

The Company recognises revenue when the amount may be reliably estimated, or in other words, when it is likely that the future economic benefits will flow to the Company.

Interest income

Interest income is recognised using the effective interest method.

3.14 Functional and presentation currency

The Company's financial statements are presented in euros, which is the functional and the presentation currency of the Company.

3.15 Transactions with related parties

Transactions between related parties are initially recognised at fair value. If applicable, where the agreed price differs from the fair value, the difference is recognised based on the economic reality of the transaction. Transactions are subsequently measured in accordance with applicable standards.

(Expressed in thousand of euros)

3.16 Leases

Leases in which a significant portion of the risks and rewards of ownership are not transferred to the Company as lessee are classified as operating leases. Payments made under operating leases (net of any incentives received from the lessor) are charged to profit or loss on a straight-line basis over the period of the lease. Lease income from operating leases where the Company is a lessor is recognised in income on a straight-line basis over the lease term. The respective leased assets are included in the balance sheet based on their nature.

3.17 Environmental assets

Expenses related to the decontamination and restoration of contaminated locations, waste disposal and other expenses deriving from compliance with environmental legislation are reflected as an expense in the year in which they arise unless they relate to the purchase cost of the assets included in the Company's equity to be used on a long-lasting basis in which case they are carried under the relevant Property, plant and equipment heading and depreciated using the same criteria.

4. Reconciliation from Spanish GAAP to IFRS-EU

The following reconciliation includes the reconciliation of the balance sheet between PGC and IFRS (Note 4.1) as of December 31st 2018 and December 31st 2017, the reconciliation of the profit/loss for the year and the global profit/loss for the financial years ended on December 31st 2018 and December 31st 2017, the effect in the profit/loss statement for the year ended on December 31st 2018 and December 31st 2017 (Note 4.2 and Note 4.3 respectively), as well as the re-classifications included because of the transition to IFRS (Note 4.4).

4.1 Reconciliation of the statement of financial position

The reconciliation of the statement of financial position at 31 December 2018 is as follows:

			Thousand euros 31 December 2018
	Local GAAP	Transition effect	IFRS
NON-CURRENT ASSETS	**991,505**	**199,576**	**1,191,081**
Intangible assets **(b)**	607,045	198,728	805,773
Property, plant and equipment	357,674	848	358,522
Financial assets	1,854	-	1,854
Deferred income tax assets	24,932	-	24,932
CURRENT ASSETS	**118,857**	**-**	**118,857**
Inventories	2,651	-	2,651
Trade and other receivables	52,490	-	52,490
Deferred expenses	674	-	674
Cash and cash equivalents	63,042	-	63,042
TOTAL ASSETS	**1,110,362**	**199,576**	**1,309,938**

(Expressed in thousand of euros)

			Thousand euros 31 December 2018
	Local GAAP	Transition effect	IFRS
EQUITY	**96,918**	**136,356**	**233,274**
Capital	1,048	-	1,048
Share premium	100,354	-	100,354
Reserves	15,430	65,437	80,867
Prior periods' losses	(23,746)	23,746	-
Profit/(loss) for the year	(9,494)	60,499	51,005
Grants, donations and legacies received (a)	13,326	(13,326)	-
NON-CURRENT LIABILITIES	**953,960**	**63,009**	**1,016,969**
Non-current provisions	4,661	-	4,661
Other non-current liabilities	1,656	-	1,656
Payables to related parties	942,640	-	942,640
Deferred income **(a)**	-	17,775	17,775
Deferred income tax liabilities (a) (b)	5,003	45,234	50,237
CURRENT LIABILITIES	**59,484**	**211**	**59,695**
Current provisions	2,336	-	2,336
Financial liabilities	84	-	84
Payables to related parties	12,007	-	12,007
Trade and other payables	45,057	211	45,268
TOTAL EQUITY AND LIABILITIES	**1,110,362**	**199,576**	**1,309,938**

The reconciliation of the statement of financial position at 31 December 2017 is as follows:

			Thousand euros 31 December 2017
	Local GAAP	Transition effect	IFRS
NON-CURRENT ASSETS	**1,090,586**	**118,910**	**1,209,496**
Intangible assets **(b)**	684,943	118,910	803,853
Property, plant and equipment	373,091	-	373,091
Financial assets	5,273	-	5,273
Deferred income tax assets	27,279	-	27,279
CURRENT ASSETS	**678,874**	-	**678,874**
Inventories	3,508	-	3,508
Trade and other receivables	58,580	-	58,580
Deferred expenses	761	-	761
Cash and cash equivalents	616,025	-	616,025
TOTAL ASSETS	**1,769,460**	**118,910**	**1,888,370**

(Expressed in thousand of euros)

	Thousand euros 31 December 2017		
	Local GAAP	Transition effect	IFRS
EQUITY	**229,181**	**75,619**	**304,800**
Capital	1,048	-	1,048
Share premium	222,954	-	222,954
Reserves	15,361	48,937	64,298
Prior periods' losses	(10,086)	10,086	-
Profit/(loss) for the year	(13,660)	30,160	16,500
Grants, donations and legacies received (a)	13,564	(13,564)	-
NON-CURRENT LIABILITIES	**964,227**	**43,291**	**1,007,518**
Non-current provisions	5,737	-	5,737
Other non-current liabilities	1,841	-	1,841
Payables to related parties	941,481	-	941,481
Deferred income (a)	-	18,092	18,092
Deferred income tax liabilities (a) (b)	15,168	25,199	40,367
CURRENT LIABILITIES	**576,052**	**-**	**576,052**
Current provisions	2,854	-	2,854
Financial liabilities	4,460	-	4,460
Payables to related parties	517,587	-	517,587
Trade and other payables	51,151	-	51,151
TOTAL EQUITY AND LIABILITIES	**1,769,460**	**118,910**	**1,888,370**

(a) Under previous GAAP, grants are classified within the equity caption, whereas under IFRS-EU grants are classified as deferred income under the "Deferred income" caption on in the balance sheet.

(b) This adjustment reflects the effect of amortization of goodwill and intangible assets reversed in 2018 and 2017 (Note 4.2(a)).

(Expressed in thousand of euros)

(a) According to the RD 602/2016 December 2nd, under PGC the administrative concessions are considered as assets with definite useful lives, so the assets must be amortized. Additionally, the goodwill also must be amortized during its useful life, with no evidence proving the contrary, it is said to be 10 years and its recovery is straight-line. Because of the differences in the accounting policies regarding NIIF such amortizations are reversed in the transition process to NIIF, as well as the tax effect.

4.3 Reconciliation of comprehensive income

The adjustments for the statement of comprehensive income of the year ended December 31st 2018 is as follows:

	Thousand euros 31 December 2018		
	Local GAAP	Transition effect	IFRS
Profit for the period	(9,494)	60,499	51,005
Items that will not be reclassified to profit or loss:			
Grants, donations and legacies received	1,324	(1,324)	-
On actuarial gains and losses and other adjustments (net of tax)	69	-	69
Income tax	(331)	331	-
Total income and expenses recognized in equity	1,062	(993)	69
Transfers to profit and loss			
Grants, donations and legacies received	(1,641)	1,641	-
Income tax	410	(410)	-
Total transfers to profit and loss	(1,231)	1,231	-
	(9,663)	60,737	51,074

The adjustments for the statement of comprehensive income of the year ended December 31st 2017 is as follows:

	Thousand euros 31 December 2017		
	Local GAAP	Transition effect	IFRS
Profit for the period	(13,660)	30,160	16,500
Items that will not be reclassified to profit or loss:			
Grants, donations and legacies received	505	(505)	-
On actuarial gains and losses and other adjustments (net of tax)	(15)	-	(15)
Income tax	(126)	126	-
Total income and expenses recognized in equity	364	(379)	(15)
Transfers to profit and loss			
Grants, donations and legacies received	(798)	798	-
Income tax	199	(199)	-
Total transfers to profit and loss	(599)	599	-
	(13,895)	30,380	16,485

4.4 Reclassifications due to the transition to IFRS.

The balance sheet at December 31st 2018 and 2017 include certain re-classifications that do not have impact in the Company's equity, as well as the re-classifications in the financial statement lines included in the statement of cash flow.

5. Financial Risk Management

The Company's activities have no significant exposure to exchange rate risk and the fluctuation of interest rate. However, the Company is exposed to credit and liquidity risk.

The Company´s Management focuses on maintaining a solid financial structure that optimises the cost of capital and the availability of financial resources to guarantee business continuity over the long term, in order to enhance value for shareholders while ensuring a solid credit profile. In this regard, the senior unsecured debt credit ratings assigned to the Company by Standard & Poor´s and Fitch remain, respectively at BBB.

5.1 Financial risk factors

Credit Risk

In accordance with its corporate objects, the Company collects for the gas system the amounts relating to tolls to access the connection point network located in its distribution territory by invoicing to supply companies. On a monthly basis and within the settlement system framework coordinated by CNMC, a calculation is performed of the excess or shortfall in access tolls invoicing with respect to the remuneration recognised to the Company. If toll invoicing exceeds the remuneration recognised, the Company must settle such difference in favour of other gas system companies. Otherwise, the Company will receive from such companies the remaining balance to complete the remuneration recognised.

Regulations in this respect consider tolls invoiced to the supply companies to be collected for the purposes of the settlement system described above, and therefore in the event of non-payment by such counterparties, the Company is exposed to a credit risk with respect to part of its revenues.

The Company actively manages the aforementioned credit risk through a follow-up of outstanding receivable balances. Similarly, and taking into account (i) the reduced average collection period, less than 30 days, (ii) the regulatory supervisory framework in which gas system activities are performed and (iii) the mechanisms for suspending the contracts for Third-party Network Access in the event of non-payment of tolls to the Company (after a period of 60 days after a reliable request of the counterparty), exposure to the credit risk is considered to be limited.

Interest rate risk

During the current year, the Company has been exposed to several financial risks, mainly to interest rate risk.

The Company´s interest rate risk results from long-term external borrowing.

Non-current borrowings issued at fixed rates expose the Company to the fair value of its financial liabilities.

Liquidity and availability of funding risks

The Company maintains a liquidity policy that ensures compliance with the payment commitments acquired, diversifying the coverage of financing needs and debt maturities. Prudent liquidity risk management includes the maintenance of sufficient cash and realizable assets and the availability of funds for an adequate amount to cover the obligations.

At December 31, 2018, available liquidity amounts to 263,042 thousand euros (December 31th 2017: 816,025 thousand euros), taking into account cash and equivalents (63,042 thousand euros in December 31st 2018 and 616,025 thousand euros in December 31^{sd} 2017) and unused equivalent credit lines (200,000 thousand euros in December 31st 2018 and 200,000 thousand euros in December 31^{sd} 2017) (Note 14).

The Company's business and investment plans are mainly financed through cash generated from on-going operations and, occasionally, through revolving credit facilities.

It is the Company policy to match the debt's amortisation calendar to its capacity to generate cash flows to meet these maturities. In particular, the Company's Management attempts to ensure that the operations over the next 12 months are always fully financed without the need to substantially modify the conditions and structure of the Company's debt.

Management considers the Company has enough cash reserves to address the payments to realize the following 12 months.

The tables below analyse the Company's financial liabilities into relevant maturity groupings based on their contractual maturities for all non-derivative financial liabilities. The amounts disclosed in the table are the contractual undiscounted cash flows (in thousand euros).

	31/12/2019	31/12/2020	31/12/2021	31/12/2022	Over 5 years	Total
At December 31, 2018						
Payables to related parties	28,284	28,284	28,284	28,284	1,053,914	1,167,050
Trade and other payables	40,690	-	-	-	-	40,690
Other accounts payable	84	204	204	204	1,044	1,740
Total	**69,058**	**28,488**	**28,488**	**28,488**	**1,054,958**	**1,209,480**

	31/12/2018	31/12/2019	31/12/2020	31/12/2021	Over 5 years	Total
At December 31, 2017						
Payables to related parties	547,669	28,284	28,284	28,284	1,082,199	1,714,720
Trade and other payables	45,370	-	-	-	-	45,370
Other accounts payable	4,460	204	204	204	1,229	6,301
Total	**597,499**	**28,488**	**28,488**	**28,488**	**1,083,428**	**1,766,391**

5.2 Capital Risk management

The management of the Company's capital focuses on maintaining a solid financial structure that optimizes the cost of capital and the availability of financial resources to ensure the continuity of the business over the long term, in order to improve shareholder value while guaranteeing a solid credit profile.

The Company monitors its capital structure based on the net adjusted financial debt/EBITDA ratio. The Company considers as its adjusted net financial debt the nominal amounts of the non-current and current debt with related parties (Note 14) less cash and its equivalents. The Company defines EBITDA as profit before interest, taxes, depreciation and amortization, excluding other results, provision excess, indemnities (Note 18), banking and similar services and changes in provisions for commercial operations (Note 18).

(Expressed in thousand of euros)

7. Intangible assets

The breakdown and movement in the items included in this heading of the balance sheet is as follows:

						Thousand euros
	Goodwill	Administrative authorizations	Computer applications	Other fixed assets	Licenses in progress	Total
Book value at 30-06-2017	57,381	740,265	1,586	1,244	1,988	802,464
Additions	-	-	924	103	846	1,873
Depreciation charge	-	-	(410)	(74)	-	(484)
Cost	57,381	740,265	10,198	1,547	2,834	812,225
Accumulated amortisation	-	-	(8,098)	(274)	-	(8,372)
Book value at 31-12-2017	57,381	740,265	2,100	1,273	2,834	803,853
Additions	-	-	826	157	2,037	3,020
Depreciation charge	-	-	(932)	(168)	-	(1,100)
Cost	57,381	740,265	11,024	1,704	4,871	815,245
Accumulated amortisation	-	-	(9,030)	(442)	-	(9,472)
Book value at 31-12-2018	57,381	740,265	1,994	1,262	4,871	805,773

The Goodwill comes from the merger through absorption between Madrileña Red de Gas, S.A.U. (merged company) and Madrileña Servicios Comunes, S.L.U. (merging company), on June 30th 2011 and the merger through absorption of Madrileña Red de Gas II, S.A.U. (merged company) and Nueva Madrileña de Gas, S.A.U. (merging company) on May 31, 2012.

<u>Impairment test for goodwill</u>

The core business of the company is the gas distribution activity for which it receives an annual retribution granted by regulation. The recoverable amount for the CGU is determined on the basis of calculating its value in use.

These calculations are based on forecasted cash flows included in the business plan approved by the Board of Directors covering the current year and time period of 5 years included a terminal value.

The key assumptions to determine the value in use are as follow:

- Projection period: current year, 5 years and remaining value
- Nominal growth rates: 0.5%, affecting only the residual value
- Discount rates after taxes: 5.10%

Apart from the discount rates, the most sensitive aspects that are included in the projections used and that are based on sector forecasts and historical experience are as follows:

- Revenue from remuneration
- The amount and growth of the remuneration approved by the regulator
- Operational and maintenance costs.
- Investments.
- Conversion costs of the supply points of LPG to Gas.

Historically, the forecasted cash flows included in the business plan and the actual results have not significantly differed.

The recoverable amount calculated based on value in use exceed its carrying value. A decrease in the EBITDA of 1,5%, a decrease in the long term growth rate of 0.5%, or a rise in pre-tax discount rate by 1%, considering all changes in isolation, would not result in an impairment loss.

At December 31st 2018 and 2017, no goodwill or administrative authorizations impairment has been registered.

Additions

At December 31st 2018 and 2017, the most important additions are registered under the financial statement line "Computer applications" and licenses in progress as consequences of the works being done for a logarithm's development that will allow the Company to optimize the lectures process and to reduce the percentage of losses in the distribution.

Other information

As of December 31st 2018, the Company has 6,828 thousands euros of intangible assets fully amortised considering the accounting effects of mergers set out in Note 1 (December 31st 2017: 5,867 thousands euros).

As of December 31st 2018 and 2017, the Company does not have any assets subject to reversion.

As of December 31st 2018 and 2017, the Company has no firm commitments to purchase intangible assets.

(Expressed in thousand of euros)

8. Property, plant and equipment

The breakdown and movement in the items included under this heading are as follows:

	Land	Plant	Transport equipment	Tooling	Furniture	Information processing equipment	Other fixed assets	Assets under construction	Total
Book value at 30-06-2017	**144**	**370,424**	**564**	**264**	**133**	**281**	**659**	**8,305**	**380,774**
Additions	-	1,276	-	20	-	12	152	5,972	7,432
Disposals	-	-	-	-	-	-	-	(2)	(2)
Transfer	-	1,406	-	-	-	-	-	(1,406)	-
Depreciation charge	-	(14,892)	(61)	(29)	(12)	(92)	(27)	-	(15,113)
Cost	144	586,625	719	565	227	855	1,065	12,869	603,069
Accumulated amortisation	-	**(228,411)**	**(216)**	**(310)**	**(106)**	**(654)**	**(281)**	-	**(229,978)**
Book value at 31-12-2017	**144**	**358,214**	**503**	**255**	**121**	**201**	**784**	**12,869**	**373,091**
Additions	-	3,813	-	213	59	45	121	9,058	13,309
Disposals	-	-	(87)	-	-	-	-	(1,142)	(1,229)
Transfer	-	5,751	-	-	-	-	-	(5,751)	-
Depreciation charge	-	(26,268)	(111)	(65)	(25)	(157)	(61)	-	(26,687)
Depreciation disposals	-	-	38	-	-	-	-	-	38
Cost	144	596,189	632	778	286	900	1,186	15,034	615,149
Accumulated amortisation	-	**(254,679)**	**(289)**	**(375)**	**(131)**	**(811)**	**(342)**	-	**(256,627)**
Book value at 31-12-2018	**144**	**341,510**	**343**	**403**	**155**	**89**	**844**	**15,034**	**358,522**

Additions to property, plant and equipment in the fiscal year ended at December 31st, 2018 and December 31st 2017 relate mainly to investments in the natural gas pipeline network in the municipalities where the Company carries out its activity. At December 31st 2018 the Company provide services to 903,346 (899,662 at December 31St 2017) connection points.

On June 9th 2016 a framework agreement was signed between Repsol Butano, S.A. and the Company for the purchase and transmission of LPG networks and installations for 61 million euros, which consists in approximately 41 thousand points of supply, to the purpose of its progressive conversion, within a maximum term of 5 year, to gas distribution assets, in accordance with the Company´s layout. After the approval by the CNMC on July 21st 2016 the agreement for the transmission of LPG networks and installations were formalized. As of December 31st 2018, 16,448 LPG supply points converted to gas supply points. As of December 31st 2017, 8,396 LPG supply points have been converted to gas supply points.

As of December 31st 2018, property, plant and equipment includes fully amortized elements still in use considering the accounting effects of mergers set out in Note 1, amounting 45,962 thousand euros (December 31st 2017: 39,770 thousand euros).

It is the Company policy to take out insurance policies to cover risks relating to property, plant and equipment. The coverage provided by these policies is considered to be sufficient.

(Expressed in thousand of euros)

At December 31st 2018 and 2017, there is no commitments to purchase transport vehicles. There are investments to amplify and improves the network for an amount of 1,600 thousand euros (December 31St 2017: 1,600 thousand euros), and also for the construction of liquefied gas plants for an amount of 453 thousand euros (December 31st 2017: 453 thousand euros).

Assets under operating lease

The breakdowns of the minimum payments for the operating leases are as follows:

	Thousand Euros	
	31/12/2018	31/12/2017
Less than 1 year	219	244
Between 1 and 3 years	-	219
More than 3 years	-	-
Total	**219**	**463**

The operating lease contracts maintained by the Company at December 31st 2018 and December 31st 2017 correspond mainly to the rent of its offices.

9. Financial instruments

The carrying value of each financial instrument category as set out in the accounting and measurement standard "Financial instruments" is as follows:

9.1 Analysis by category

a) Financial assets

	Thousand Euros	
	Long-Term financial investments	
	Credits, derivatives and others	
	31/12/2018	31/12/2017
Other financial assets at amortized cost (Note 10)	1,854	5,273
Total	**1,854**	**5,273**
	Short-Term financial investments	
	Credits, derivatives and others	
	31/12/2018	31/12/2017
Trade and other receivables at amortized cost (Note 10) (*)	47,131	52,248
Cash and other equivalent liquid assets (Note 12)	63,042	616,025
Total	**110,173**	**668,273**

(Expressed in thousand of euros)

b) Financial liabilities

	Thousand Euros			
	Long-term financial liabilities			
	Debts with credit institutions		Derivatives, Others	
	31/12/2018	**31/12/2017**	31/12/2018	31/12/2017
Trade and other payables (Note 14)	-	-	944,296	943,322
Total	**-**	**-**	**944,296**	**943,322**

	Thousand Euros			
	Short-term financial liabilities			
	Debts with credit institutions		Derivatives, Others	
	31/12/2018	31/12/2017	31/12/2018	31/12/2017
Trade and other payables (Note 14)(*)	-	-	52,781	567,417
Total	**-**	**-**	**52,781**	**567,417**

(*) Receivables and Liabilities with the Public Administrations have been excluded from the balance of loans and accounts receivable and loans and accounts payable.

9.2 Analysis by maturity date

At December 31st 2018 the long and short term debts with a determined or determinable maturity date, classified by the year in which they will mature, are as follows:

	2019	2020	2021	2022	Subsequent years	Total
Gas system income deficit financing	19,248	234	234	234	257	20,207
Trade and other receivables	27,883	-	-	-	895	28,778
Total	**47,131**	**234**	**234**	**234**	**1,152**	**48,985**

	2019	2020	2021	2022	Subsequent years	Total
Trade payables to related parties	12,007	-	-	1,800	940,840	954,647
Trade and other payables	40,690	-	-	-	-	40,690
Other financial liabilities	84	204	204	204	1,044	1,740
Total	**52,781**	**204**	**204**	**2,004**	**941,884**	**997,077**

(Expressed in thousand of euros)

At December 31st 2017 the long-term debts with a determined or undetermined maturity date, classified by the year in which they will mature, are as follows:

	2018	2019	2020	2021	Subsequent years	Total
Gas system income deficit financing	23,332	1,177	1,177	1,195	914	27,795
Trade and other receivables	28,916	-	-	-	810	29,726
Total	**52,248**	**1,177**	**1,177**	**1,195**	**1,724**	**57,521**

	2018	2019	2020	2021	Subsequent years	Total
Trade payables to related parties	517,587	-	-	-	941,481	1,459,068
Trade payables	45,370	-	-	-	-	45,370
Other financial liabilities	4,460	204	204	204	1,229	6,301
Total	**567,417**	**204**	**204**	**204**	**942,710**	**1,510,739**

The fair value of the financial assets and liabilities does not differ significantly from the carrying amount.

10. Trade and other receivables at amortized cost

The breakdown of this financial statement line as of December 31st 2018 and 2017 is as follows:

	Thousand Euros	
	31/12/2018	**31/12/2017**
Long-term financial investments		
Gas system tariff deficit	959	4,463
Guarantee deposits	895	810
	1,854	**5,273**
Short-term trade and other receivables		
Trade receivables for sales and services	36,428	36,687
Provisions for bad debts	(8,642)	(7,813)
Debtors	19,248	23,332
Loans to employees	97	42
	47,131	**52,248**

Gas system tariff deficit and sundry debtors

At December 31st 2018 and December 31st 2017, the item "Gas system tariff deficit" relates to mismatches between gas system revenues and costs accumulated by natural year 2015, 2016 and 2017 being as follows:

		Thousand Euro
Long-term Gas System Deficit	**31/12/2018**	**31/12/2017**
Deficit generated in 2015	-	813
Deficit generated in 2016	-	3,650
Deficit generated in 2017	959	-
	959	**4,463**

(Expressed in thousand of euros)

These mismatches generates a recovery right, and in the next five years, plus interest at a market rate (once liquidity is obtained). The amount of this financing has been recognized in the financial statement line "Other non-current financial assets" the amount to be collected in the long term, and the amount of short term in "Debtors" based on the estimated recovery period through system settlements.

On December 1st 2017, the Company entered into an agreement with a banking entity to assign the nominal amount pending collection derived from the cumulative gas deficit for 2014 and outstanding interest. By virtue of this agreement, the Company transferred the total credit recorded at that date for an amount of 44,940 thousand euros, registering a financial income for this concept for 245 thousand euros. The Management of the Company, after analyzing the agreement, considers that all the risks related to this credit have been substantially transferred and, consequently, the totality of the assigned credit has been written off.

On October 10th 2018, the Company has entered into an agreement with a banking entity to assign the nominal amount pending collection derived from the cumulative gas deficit for 2015 and 2016 and outstanding interest. By virtue of this agreement, the Company has transferred the total credit recorded at that date for an amount of 4,816 thousand euros.The Management of the Company, after analyzing the agreement, considers that all the risks related to this credit have been substantially transferred and, consequently, the totally of the assigned credit has been written off.

The breakdown of the financial statement line "Sundry Debtors" mainly collected between the deficit in 2015, 2016, 2017, 2018 and the deficit / surplus generated until December 31st 2018, being as follows:

	Thousand Euros	
Sundry Debtors	**31/12/2018**	**31/12/2017**
Deficit / (Surplus) generated in 2015	-	265
Deficit / (Surplus) generated in 2016	-	912
Deficit / (Surplus) generated in 2017	240	22,155
Deficit / (Surplus) generated in 2018	19,008	-
	19,248	**23,332**

As of the date of preparation of these annual accounts, the final assessments of the deficit of the year 2018 has not been received.

The company register in this financial statement line the deficit / surplus, generated during the 2018 financial year, the amount of deficit accrued until the month of October, mainly accounting in the financial statement line of "Sundry payables" the provision of November and December by the amount of 16,006 thousands euros (14,172 thousands euros at December 31st 2017 the provision of November and December) (Note 14).

Trade and rendering of services

As of December 31st 2018 and 2017, the amount included in the financial statement line "Trade receivables for sales and services" corresponds to the debtor balances by invoicing gas trading companies for the distribution activity in certain municipalities in the Autonomous Community of Madrid.

In general, the outstanding receivable toll invoices do not accrue interest, and the deadline for its payment by the supply companies is of 15 days after the invoice's emission date.

According to the approved Resolution of July 17th 2015 by the "Dirección General de Política Energética y Minas", which establishes the valuation and liquidation of the amounts of measure differences on natural gas distribution networks from 2008 to 2012, and the communication of Enagás as of May 31st 2016 that has published the amount of measure differences between distributors and trading during the period from July 1st 2008 to May 31st 2012 and during the period of 2014, corresponding to Madrileña Red de Gas, S.A.U. a net amount receivable of 14,835 thousand euros, being the entire amount received as of totally in previous fiscal years. Similarly, the Group has recognized a liability under "Suppliers" for the amount totally received at December 31st 2018 and December 31st 2017.

According to the approved Resolution of April 23rd, 2018 by the "Direccion General de Politica Energética y minas" which establishes the valuation ad liquidation of the amounts of measure differences on natural gas distribution networks from July 1st, 2012 to December 31st, 2013 was published the amount of measure differences between distribution and trading during the period of July 1st,2012 and December 31st, 2013 corresponding to Madrileña Red de Gas S.A.U a net amount payable of 4,926 thousand euros being the entire amount payed as of totally in this fiscal year. Similarly the Group has been a liability under "Suppliers" for the amount totally received for this.

On February 7th 2011 Gas Natural Fenosa (Currently called Naturgy) signed with the Company a contract for the sale of distribution branch business in certain municipalities in Madrid, establishing the agreements to the assignments of the network division. On June 30th, 2011, an addendum was signed to this agreement, through which the pacts relating to the sectorization works contained in the aforementioned contract were established and new sectorization works were agreed. On December 31st 2018, the network division process has not yet been finalized, and until then, collections/payments for the measurement differences that are not assigned to the Company, although on October 2017, at the request of Gas Natural Fenosa,(Currently called Naturgy) discussions began related to the date from which the measurement differences would correspond to the Company, not estimating a significant impact.On date annual accounts has been prepared there is not agreement yet.

The fair values of the loans and accounts receivable are the same as the book values.

(Expressed in thousand of euros)

The movement in the insolvency provision for trade receivables are as follows:

	Thousand Euros	
	31/12/2018	31/12/2017
Opening balance	**(7.813)**	**(6,345)**
Charge to insolvency provision	(863)	(1,543)
Disposals	34	64
Others	-	11
Closing balance	**(8,642)**	**(7,813)**

Long-term guarantees

The non-current guarantees do not have any specified maturity date.

11. Inventory

As of December 31st 2018 and 2017 inventories correspond mainly to LPG and others materials of replacement distribution network.

As of December 31st 2018 there are no commitments to purchase or sell gas.

12. Cash and cash equivalents

The breakdown of this financial statement line as of December 31st 2018 and 2017 is as follows:

	Thousand Euros	
	31/12/2018	31/12/2017
Cash and banks	63,042	316,025
Other equivalent liquid assets		300,000
	63,042	**616,025**

The treasury of the Company as of December 31st 2018 and 2017 is comprised mostly of checking accounts, with no availability limit and at market interest rate.

As of December 31st 2017 the Company maintained 300.000 thousand euros in a highly liquid deposit the amount received from one of its Sole Shareholder's loans during the year ended at June 30th 2017, that it had free availability at no cost, and accrues at an interest rate of the market. On September 4th 2018 the Company had drawn down this deposit as a result of the amortization of one of the loans received by the related company Madrileña Red de Gas Finance BV (Note 14).

(Expressed in thousand of euros)

13. Equity

The breakdown of this financial statement line as of December 31st 2018 and 2017 is as follows:

a) Share capital

	Thousand euros	
	31/12/2018	31/12/2017
Share capital	1,048	1,048
Total	**1,048**	**1,048**

At December 31st 2018 and 2017 the share capital was made up of 104,759 shares with a nominal value of 10 euros each, fully subscribed by Elisandra V, S.L.U. (Note 1).

b) Share premium

At December 31st 2018 the share premium amounted to 100,354 thousand euros (December 31st, 2017: 222,954 thousand euros).

On July 21st 2015 the sole shareholder approved the distribution of a dividend charged to the issue premium reserve amounting to 63,000 thousand euros, paid on July 29, 2015.

In addition, on February 8th 2016 the sole shareholder approved another dividend charged to the share premium of 25,000 thousand euros, whose disbursement occurred on March 1st 2016.

On October 20th, 2017 the sole shareholder approved the distribution of a dividend which was charged in the amounts of 17,885 thousand euros to voluntary reserves, 15,272 thousand euros to merger reserves and 1,843 thousand euros to share premium reserves. As at December 31st, 2017, of this declared dividend, an amount totalling 30,625 thousand euros has been disbursed with 4,375 thousand euros (Note 14) whose disbursement occurred on this fiscal year.

On April 25th, 2018 the sole shareholder approved the distribution of a dividend which was charged in the amounts of 116,000 thousand euros charged to the share premium that has been disbursement on 2018.

On November 28th 2018 the sole shareholder approved the distribution of dividend which was charged in the amounts of 6,600 thousand euros charged to the share premium that has been disbursement on 2018.

At December 31st 2018 this reserve is freely available.

(Expressed in thousand of euros)

c) Reserves

	Thousand euros	
	31/12/2018	31/12/2017
Legal and statutory:		
- Legal reserve	210	210
Other reserves:		
- Voluntary reserves	65,437	48,937
- Merger reserves	-	-
- Goodwill reserves	15,734	15,734
- Actuarial reserves	(514)	(583)
Total	**80,867**	**64,298**

Voluntary reserves

This reserve is freely available for distribution. On November 4th 2016 the Company's Sole Shareholder approved a dividend distribution with charge to voluntary reserves of 94,800 thousand euros. Aditionally, on October 20th 2017 the sole shareholder approved the distribution of a dividend which was charged in the amounts of 17,885 thousand euros to voluntary reserves, 15,272 thousand euros to merger reserves and 1,843 thousand euros to share premium reserves. As at December 31st, 2017, of this declared dividend, an amount totalling 30,625 thousand euros was disbursed with 4,375 thousand euros (Note 14) which has been disbursement during fiscal year 2018. The Company does not have limits for the dividends distribution others than the ones established in the article 273 of the Spanish Companies Act.

Merger reserve

This is the result of the merger through absorption of Madrileña Servicios Comunes, S.L.U. and Madrileña Red de Gas, S.A.U. on June 30th 2011 in the amount of (5,861 thousand euros), and the merger through absorption between Madrileña Red de Gas, S.A.U and Madrileña Red de Gas II, S.A.U. on September 24th 2013, in the amount of 9,411 thousand euros. On October 20th 2017 the sole shareholder approved the distribution of a dividend which was charged in the amounts of 17,885 thousand euros to voluntary reserves, 15,272 thousand euros to merger reserves and 1,843 thousand euros to share premium reserves. As at December 31st, 2017, of this declared dividend, an amount totalling 30,625 thousand euros has been disbursed with 4,375 thousand euros, (Note 14) which has been disbursement during fiscal year 2018. On December 31st 2018 and 2017 the Company has not merger reserve.

Actuarial reserves

This corresponds to the actuarial profits and losses recorded directly against equity (Note 16.1).

Goodwill reserve

(Expressed in thousand of euros)

After the approval of the Royal Decree 602/2016 of December 2nd, in the years starting on January 1st 2016, the goodwill reserve will be re-classified to voluntary reserves and will be available starting on that date in the amount that exceeds the registered goodwill in the balance sheet's asset.

Proposed distribution of profit

The profit and reserves distribution proposal to be presented to the Sole Shareholders is as follows:

	Thousand euros	
	31/12/2018	31/12/2017
Available for distribution		
Profit for the year	**51,005**	**16,500**
Application		
To voluntary reserves	51,005	16,500
To goodwill reserve	-	-
	51,005	16,500

14. Financial liabilities

The movement in this financial statement line is shown in the following table:

	Thousand Euros	
	31/12/2018	31/12/2017
Long-term debts		
Other financial liabilities-guarantees	1,656	1,841
Debts with group and associate companies (Note 20)	942,640	941,481
Total	**944,296**	**943,322**
Short-term debt		
Other financial liabilities	84	4,460
Trade Payables	21,769	28,026
Sundry payables	16,161	14,601
Accrued wages and salaries	2,760	2,743
Debts with group and associate companies (Note 20)	12,007	517,587
	52,781	**567,417**
	997,077	**1,510,739**

Current and non-current payables to related parties:

The Company recorded under "Long-term payables to group companies and associates" the loans received during the fiscal year 2014 from the related company Madrileña Red de Gas Finance, BV (MRG Finance BV) and three new loans received during the fiscal years ended at June 30th 2016 and June 30th 2017 from the Sole Shareholder, Elisandra Spain V, S.L.U. through which it transferred to the Company the amounts obtained from the bond issues by MRG Finance, of which the Company is a guarantor:

(i) Issue in September 2013 by MRG Finance BV, of bonds with a nominal amount of 500,000 thousand euros and maturity in September 2018, under its EMTN programme secured by the Company. The amount of this issue was transferred to the Company under a financing agreement signed with MRG Finance BV. The bonds issued bear interest at a fixed rate of 3.799%,per year payable annually in September, and may be redeemed at maturity. On September 4th 2018 the Company has amortized the loan who received by MRG Finance BV related to the emission repaid bond issue obligation for an amount of 519,835 thousand euros (amount and interest).

(ii) Issue in December 2013 by MRG Finance BV of bonds with a nominal amount of 275,000 thousand euros maturing in December 2023, under its EMTN programme secured by the Company. The amount of this issue was transferred to the Company under a financing agreement signed with MRG Finance BV. The bonds issued bear interest at a fixed rate of 4.50% per year payable annually in December and may be redeemed at maturity.

(iii) Issue in March 2016 by MRG Finance BV of bonds with a nominal amount of 75,000 thousand euros maturing in March 2031, under its EMTN programme secured by the Company. The amount of this issue was transferred to the Company under a financing agreement signed with Elisandra Spain V, S.L.U., Sole Shareholder of the Company, which it has signed a financing agreement with MRG Finance BV. The bonds issued bear interest at a fixed rate of 3.5% per year payable annually in March and may be redeemed at maturity.

(iv) Issue in April 2017 by MRG Finance BV of bonds with a nominal amount of 300,000 thousand euros maturing in April 2025, under its EMTN programme secured by the Company. The amount of this issue was transferred to the Company under a financing agreement signed with Elisandra Spain V, S.L.U., Sole Shareholder of the Company, which it has signed a financing agreement with MRG Finance BV. The bonds issued bear interest at a fixed rate of 1,375% per year payable annually in April and may be redeemed at maturity.

(Expressed in thousand of euros)

(v) Issue in April 2017 by MRG Finance BV of bonds with a nominal amount of 300,000 thousand euros maturing in April 2029, under its EMTN programme secured by the Company. The amount of this issue was transferred to the Company under a financing agreement signed with Elisandra Spain V, S.L.U., Sole Shareholder of the Company, which it has signed a financing agreement with MRG Finance BV. The bonds issued bear interest at a fixed rate of 2,25% per year payable annually in April and may be redeemed at maturity.

The main terms and conditions for these loans are as follows:

Notional amount of the loan	Start date	Maturity date	Term	Annual interest rate	Payment of interest	Repayment of principal
500,000	11.09.2013	11.09.2018	5 years	3.877%	Annual	04.09.2018
275,000	04.12.2013	04.12.2023	10 years	4.598%	Annual	04.12.2023
1,800	11.09.2013	11.09.2022	9 years	5.000%	Annual	11.09.2022
75,000	03.03.2016	03.03.2031	15 years	3.696%	Annual	03.03.2031
300,000	11.04.2017	11.04.2025	8 years	1.571%	Annual	11.04.2025
300,000	11.04.2017	11.04.2029	12 years	2.446%	Annual	11.04.2029
1,451,800						

Other financial liabilities

The Company recorded under "Other financial liabilities" at December 31th 2017, the dividends pending disbursement that the Company had with Elisandra Spain V, S.L.U. amounting to 4,375 thousand euros.

Current payables to related parties

The Company recorded under "Short-term payables to group companies and associates" the outstanding interest payable on the loans mentioned in the previous section amounting to 12,007 thousand euros (17,587 thousand euros at December 31st, 2017) Moreover on December 31st 2017, there was one of the loans received during the year 2014 from the related company Madrileña Red de Gas Finance, BV (MRG Finance BV) maturing in 2018, described in the previous paragraph and which has been amortized on September 4th 2018.

The financial expenses accrued at December 31st, 2018 amounts to 42,520 thousand euros (24,473 thousand euros at December 31st, 2017).

(Expressed in thousand of euros)

Accounts payable and sundry payables

At December 31st 2018 and 2017 the Company has registered in the financial statement line "Accounts Payable" mainly the remaining balance to pay off the roadwork made on distribution network (Note 7). At the same time, on December 31st 2018 this mentioned financial statement line includes also an amount of 8,983 thousand euros corresponding to a net amount payable due to the measuring differences, resulting from the amount receivable explained in the Note 10 that corresponds to the other distribution companies (14,099 thousand euros at December 31st, 2017).

On the financial statement line "Sundry Payables" the Company includes, on December 31st 2018 and 2017 the provision resulting from the difference between the billing made on November and December, and the remuneration that truly corresponds to the settlements (Note 10).

Available credit lines

At December 31st 2018 and 2017 the Company has the following available credit lines of:

	Thousand Euros	
	31/12/2018	31/12/2017
- Credit for general corporate purposes	200,000	200,000
	200,000	**200,000**

At December 31st, 2018 and 2017, the Company has not provided any credit lines.

Information on delays in payments to suppliers. Additional Provision 3 of "Duty to inform" of Law 15/2010, of July 5th:

The details of the required information regarding the average payment period to suppliers is as follows:

	31/12/2018	31/12/2017
	Days	Days
Average payment period to suppliers (1)	66	65
Ratio paid transactions (2)	66	65
Ratio of outstanding payment transactions (3)	61	67
	Thousand Euros	Thousand Euros
Total payments made in the year	57,383	17,863
Total outstanding payments	5,112	3,508

(1) Calculation considering the amounts paid and payables at December 31, 2018 and 2017
(2) Average payment period in transactions paid during the year
(3) Average length of outstanding balance providers

(Expressed in thousand of euros)

Law 31/2014, of December 3rd, modified the law 15/2010 regarding the provision of information relating to a company's average payment period for suppliers. Subsequently, the ICAC Resolution of January 29th 2016 developed the methodology for the calculation of the average payment period to suppliers and the required disclosures in the notes to the financial statements. This resolution came into force on February 5th 2016 and applies to annual accounts from the year started on January 1st 2015.

15. Deferred income

The breakdown of the "Deferred income" includes collections for the distribution network. The movement in this category is shown in the following table:

	Thousand euros	
	31/12/2018	31/12/2017
Opening balance	**18,092**	**18,385**
Additions	1,324	505
Disposals	(1,641)	(798)
Closing balance	**17,775**	**18,092**

16. Provisions

The breakdown of provisions is as follows:

	Thousand Euros	
	31/12/2018	31/12/2017
Provisions for personnel expenses	1,333	1,476
Decommissioning provisions	3,328	4,261
Non-current provisions	**4,661**	**5,737**

	Thousand Euros	
	31/12/2018	31/12/2017
Decommissioning provisions	2,336	2,854
Short-term provisions	**2,336**	**2,854**

16.1 Employee benefit obligations

The total provisions amount at December 31st 2018 and 2017 corresponds to commitments for bonuses to the natural gas consumption and health insurance for current personal from Gas Natural Fenosa (currently, Naturgy), during post-retirement period.

(Expressed in thousand of euros)

The movement in the liability recorded in the balance sheet for actuarial obligations is as follows:

	Thousand Euros	
	31/12/2018	31/12/2017
Opening balance	**1,476**	**1,469**
Cost of service in financial year	48	27
Cost of interests	28	14
Actuarial gains and losses (recorded in equity)	(69)	15
Benefits paid	(10)	(6)
Disposals	(140)	(43)
Closing Balance	**1,333**	**1,476**

The actuarial assumptions used to value the gas credit commitments are as follows:

	31/12/2018	31/12/2017
Technical discount rate	2,12%	1,94%
Cost increase (annual)	1,50%	1,50%
Inflation rate (annual)	1,50%	1,50%
Mortality table	Tablas INE	Tablas INE

16.2 Decommissioning provisions

After the acquisition of LPG assets, the Company's Management has evaluated the necessary costs for the LPG plants' dismantling that will not be utilized once the process of converting the LPG points finishes. In this sense and according to the best estimate the Company has made, it has been registered in the long-term an amount of 3,328 thousand euros and in the short-term an amount of 2,336 thousand euros (4,261 thousand euros in the long-term and 2,854 in the short-term at December 31st 2017, respectively).

17. Tax situation

From July 1st 2015 the Company began to file consolidated tax returns as a subsidiary of Tax Group No. 474/15, parented by Elisandra Spain IV, S.L.

The Tax Consolidated Group No. 474/15 is formed by the parent Elisandra Spain IV, S.L. and the companies Elisandra Spain V, S.L.U, Aliara Energía, S.L.U. y Madrileña Red de Gas S.L.U.

(Expressed in thousand of euros)

Set out below is the reconciliation between net income and expense for the year ended at December 31st 2018 and corporate tax base:

	Thousand Euros					
	Income statement			Income and expenses recognized in equity		
	Additions	Disposals	Total	Additions	Disposals	Total
Profit (loss) for the year			**51,005**			69
Corporate income tax	16,744	-	**16,744**	-	-	-
Permanent differences	-	58	**58**	-	-	-
Temporary differences	1,437	(43,673)	**(42,236)**	-	-	-
Tax base			25,571			69

Set out below is the reconciliation between net income and expense for the year ended at December 31st 2017 and corporate tax base:

	Thousand Euros					
	Income statement			Income and expenses recognized in equity		
	Additions	Disposals	Total	Additions	Disposals	Total
Profit (loss) for the year			**16,500**			(15)
Corporate income tax	5,572	-	**5,572**	-	-	-
Permanent differences	23	-	**23**	-	-	-
Temporary differences	1,561	(24,603)	**(23,042)**	-	-	-
Tax base			(947)			(15)

On March 31st 2012 the Official State Gazette published Royal Decree-Law 12/2012 (March 30), which was subsequently amended by Royal Decree-Law 20/2012 (July 12), introducing several tax and administrative measures to reduce the public deficit. This Royal Decree-Law establishes a general limit to the deduction of financial expense. In general the amount of net deductible financial expense in the tax period is reduced to 30% of operating profits for the year (applying certain corrections) and, in any event, financial expense not exceeding 1 million euros are deductible. These limitations will apply to the tax periods commencing as from January 1st 2012.

Article 7 of Law 16/2012 (of December 27th), which adopts several tax measures to consolidate public finances and encourage economic activities, introduces a temporary limitation in 2013 and 2014 affecting tax deductible amortisation and only 70% of the amortisation recognised by companies that do not comply with the requirements of Article 108 of the Spanish Corporate Income Tax Act, which regulates the requirements for the small company classification, may be deducted.

(Expressed in thousand of euros)

On December 31st 2018 the disposals of temporary differences include the reversal of 2,949 thousand euros (December 31st 2017: 1,992 thousand euros) due to the limitation on the amortization of PP&E. The disposals of temporary differences include also the tax depreciation of administrative authorisations in an amount of 37,040 thousand euros (December 31st 2017: 18,666 thousand euros), the tax amortisation of goodwill in an amount of 2,869 thousand euros (December 31st 2017: 1,440 thousand euros). The additions of temporary differences include 865 thousand euros (December 31, 2017: 1,271 thousand euros) due to the personnel liabilities, 133 thousand euros (December 31st 2017: 57 thousand euros) for a non-deductible allowance for tax purposes and 439 thousand euros (December 31st 2017: 222 thousand euros) for the difference between tax and accounting amortisation, according to Royal Decree 3/93.

At December 31st 2018 the Company had made interim corporate income tax payments totalling 5,483 thousand euros (December 31st 2017: 1,544 thousand euros).

Corporate income tax expense is analysed below:

	Thousand euros	
	31/12/2018	**31/12/2017**
Current tax	(5,834)	237
Deferred tax	(10,910)	(5,809)
	(16,744)	**(5,572)**

The current corporate tax results from the application of the 25% to the tax base. At December 31st, 2018, it is also included tax differences adjustments from prior tax years by the amount of 465 thousand euros as a decreasing expense (4 thousand euros at December 31st 2017 as an increasing expense) and adjustments for deductions for an amount of 94 thousand euros as a decreasing expense.

(Expressed in thousand of euros)

Deferred income tax assets and liabilities

Movements during the year in deferred tax assets and liabilities, without taking into account the offset of balances, were as follows:

Deferred income tax assets	Provisions	Financial expenses	Merger fixed asset	Asset amortisation	Insolvency provisions	Total
Balance at 30/06/2017	1,039	17,860	3,016	4,229	109	26,253
Charged/(credited) to profit or loss	316	(553)	(278)	(264)	(54)	(833)
Other	-	1,859	-	-	-	1,859
Balance at 31/12/2017	1,355	19,166	2,738	3,965	55	27,279
Charged/(credited) to profit or loss	(194)	-	(297)	(529)	(22)	**(1,042)**
Other	-	(1,305)	-	-	-	(1,305)
Balance at 31/12/2018	1,161	17,861	2,441	3,436	33	24,932

Deferred income tax liabilities	Tax amortisation RD3/93	Tax amortisation Administrative concessions	Tax amortisation goodwill	Total
Balance at 30/06/2017	(502)	(33,208)	(1,687)	(35,397)
Charged/(credited) to profit or loss	56	(4,666)	(360)	(4,970)
Balance at 31/12/2017	(446)	(37,874)	(2,047)	(40,367)
Charged/(credited) to profit or loss	110	(9,260)	(718)	(9,868)
Other	-	(2)	-	(2)
Balance at 31/12/2018	(336)	(47,136)	(2,765)	(50,237)

The deferred tax assets arising from tax loss carry forwards available to offset are recognised as it becomes likely that the Company will obtain future tax profits to offset them. At December 31st 2018 and 2017 the Company records no tax bases pending to offset.

At the date of the annual accounts formulation, it is open the process of inspection for the last 4 years of the main taxes (VAT, IRPF and Corporate Tax).

The Company is under one process of inspection in relation to VAT and Corporate Tax to the financial years 2012 and 2013 (Note 23).

(Expressed in thousand of euros)

In accordance with current legislation, tax returns cannot be deemed definitive until they are verified by the tax authorities or until they pass their statute of limitation. The Company has not yet submitted the declaration of corporate income tax for the year ended on December 31st 2018, although in its calculation are taken into consideration the various legislative provisions apply.

As a result, among other things, of the different interpretations the fiscal legislation may have, as well as the results of the inspections that could happen in the verification years, it may arise additional liabilities with contingent character for the Company, that are not susceptible to objective quantification. The Company's Directors do not expect additional liabilities to arise as a consequence of the said resources nor the inspection of the outstanding fiscal years (Note 23).

The amount included under "Other receivables/payables to Public Administrations" breaks down as follows:

	Thousand euros	
	31/12/2018	**31/12/2017**
Debit balances		
VAT receivable	-	769
Tax receivable for other items (Note 23)	5,359	5,563
Total debt balances	**5,359**	**6,332**
Credit balances		
Vat payable	72	-
Current tax	907	2,486
Other payable for withholdings made	(1)	(2)
Other debts with Public Administrations	3,452	3,155
Social Security payables	148	142
Total credit balances	**4,578**	**5,781**

The amount included in "Other debts with Public Administrations" relates to the credit balances with Councils for public land occupancy tax.

(Expressed in thousand of euros)

18. Income and expense

a) Revenue

	Thousand Euros	
	31/12/2018	31/12/2017
Revenue		
Remuneration (Note 2)	146,958	66,610
Other non-regulated income	4,296	2,555
Other non-regulated income by indemnities	153	55
Other regulated income	16,526	8,629
Non regulated LPG income (Note 2)	59	-
LPG income (Note 2)	18,286	7,778
Total	**186,278**	**85,627**

The entirety of the company's revenues relate to activities carried out in the Region of Madrid.

<u>Other regulated income</u>

Other regulated income corresponds to services related to natural gas distribution activity, where its prices are determined in the regulation. These services include the renting of gas meters, periodic inspections and network services.

<u>Other non-regulated income</u>

Other non-regulated income are also for services relating to the natural gas distribution activity, where its prices are not regulated, such as services like the operations realized in the final user's home and other auxiliary services.

b) Consumption of goods

The breakdown of the consumption of goods at the end of the financial year is as follows:

	Thousand Euros	
	31/12/2018	31/12/2017
Consumption of goods		
Other	(15,916)	(7,741)
Variation in merchandise inventory	857	76
Impairment of merchandise, raw materials and other supplies	(111)	-
Total	**(15,170)**	**(7,665)**

(Expressed in thousand of euros)

c) Personnel expenses

	Thousand Euros	
	31/12/2018	31/12/2017
Wages, salaries and similar	(8,061)	(3,917)
Social charges:		
- Contributions and allocations for pensions	(89)	(46)
- Other social charges	(2,395)	(1,415)
Indemnities	(1,123)	(1,632)
Total	**(11,668)**	**(7,010)**

The number of employees by professional category and gender at December 31, 2018 by category is as follows:

	Male	Female
Senior Managements / Managers	15	6
Administrative	7	8
Business development	22	9
Operations	70	13
	114	**36**

The number of employees by professional category and gender at the end of the year ended on December 31th 2017 by category was as follows:

	Male	Female
Senior Managements / Managers	15	6
Administrative	8	7
Business development	24	8
Operations	79	11
	126	**32**

The average number of employees' professional category and gender of the Company in the fiscal year ended at December 31st 2018 is as follow:

	Male	Female
Senior Managements / Managers	15	6
Administrative	8	8
Business development	23	9
Operations	76	11
	122	**34**

(Expressed in thousand of euros)

The average number of employees by professional category and gender of the Company in the year for 6 months ended December 31th 2017 was as follow:

	Male	Female
Senior Managements / Managers	15	5
Administrative	8	7
Business development	25	8
Operations	80	11
	128	**31**

During the fiscal years ended at December 31st 2018 and 2017 no employees with a disability higher or equal to 33% have been hired.

d) Other operating expenses

		Thousand euros
	31/12/2018	**31/12/2017**
Other operating expenses		
Leases and royalties	(453)	(236)
Repairs and maintenance	(3,267)	(1,582)
Professional services	(1,299)	(723)
Insurance	(357)	(186)
Bank services and similar	(238)	(85)
Publicity	(22)	(41)
Supplies	(479)	(123)
Taxes	(4,130)	(1,336)
Losses, impairment and changes in provisions for commercial operations	(829)	(1,479)
Other operating expenses	28	(11)
Other expenses	(8,024)	(4,097)
Other services	(2,866)	(1,257)
Total	**(21,936)**	**(11,156)**

The "Other expenses" financial statement line largely relates to expenses accruing in the financial year due to the reading of meters carried out by external parties, management services for the billing and charging and other items related to the overall operation of the Company.

(Expressed in thousand of euros)

e) Other results

	Thousand Euros	
	31/12/2018	**31/12/2017**
Other results		
Other non-recurring expenses	(746)	(220)
Total	**(746)**	**(220)**

At December 31st 2018 and 2017 the financial statement line "Other results" includes expenses for professional services received for non-recurring corporate projects.

f) Financial expenses

	Thousand Euros	
	31/12/2018	**31/12/2017**
Financial income:		
Marketable securities and other financial instruments		
- Third parties	33	699
	33	**699**
Financial expenses		
Interest on debts with group companies (Note 14 and 20)	(42,520)	(24,473)
Interest on debts with third parties	(376)	(222)
	(42,896)	**(24,695)**
Financial results	**(42,863)**	**(23,996)**

19. Remuneration of the Board of Directors and Management

In the years ended at December 31st 2018 and 2017 the members of the Board of Directors have not received remuneration in the form of salaries or other remunerations. In addition, they have not been granted loans or advances, rights relating to pensions or life insurance or others of a similar nature at the Company's expense.

The Company considers senior management staff understood "Senior Management ", not only those cases where there are employment contracts of senior management but also those people who exercise functions related to the general objectives of the Company, such as planning, management and control activities, performing its functions independently and with full responsibility, limited only by higher bodies that represent them.

The total final remuneration paid during the year ended at December 31st, 2018 to senior management amounts to 2,770 thousands euros (1,375 thousand euros in December 31st 2017), of which 1,834 thousand euros (1,042 thousand euros in December 31st, 2017) relates to short term compensation, 835 relates to indemnities (280 thousand euros in 31st, December 2017) and 91 thousand euros (53 thousand euros in December 31st, 2017) corresponds to contributions to pension fund. The total amount of the liabilities incurred in relation to senior management life insurance amounts to 10 thousands of euros (0 thousands of euros in December 31st 2017). During the fiscal year ended at December 31st 2018 and 2017 the company did not granted any loans to senior management.

Director's conflict of interest

As regards the duty to avoid conflicts of interest with the Company, during the year the Board of Directors fulfilled the obligations stipulated in Article 228 of the Spanish Companies Act. Both the Directors and their related parties avoided the conflict of interest scenarios envisaged in Article 229 of the Act, except for cases in which the necessary authorisation was obtained.

On April 30th, 2018, the assignment of Mr. Guillaume D'Engremont and Mr. Jerôme Sousselier were revoked and on June 5th 2018, the new directors assigned are Mr. Maxime Nekoian and Mr. Pierre Alexandre Marie Benoist-d'Anthenay.

On July 23 rd, 2018 the assignment of Mr Maxime Nekoian was revoked and the new director assigned is Mrs.Fanny Marie Colette Grillo.

On March 22nd, 2019, the assignment of Mr. Michael Andrew Bryan and Mrs. Rong Yan were revoked and the new directors assigned are Mr. Dong Dong and Mr. Andrew Wilkie.

20. Related-party transactions

Related parties are as follows:

- The Sole Shareholder of Madrileña Red de Gas, S.A.U., Elisandra V, S.L.U. and the ultimate parent company Elisandra IV, S.L., and its significant shareholders Realgaz, S.A.S (previously called C41 S.A.S), Stichting Depositary PGGM Infrastructure Funds, JCSS Mike S.A.R.L and LPPI Infrastructure Investments LP.

- Directors and executives of the company, and their immediate families. The term "director" means a member of the Board of Directors; "executive" means a member of the Senior Management of Madrileña Red de Gas, S.A.U.

- Companies of Madrileña Red de Gas, S.A.U., Elisandra Spain IV, S.L., Elisandra Spain V, S.L.U., Aliara Energía, S.L.U., and Madrileña Red de Gas Finance B.V.

(Expressed in thousand of euros)

a) Balances with related parties

31/12/2018	Group companies	Other related parties	TOTAL
	Thousand Euros		
Long-term debts with group and associate companies (Note 14)	(942,640)	-	**(942,640)**
Short-term debts with group and associate companies (Note 14)	(12,007)	-	**(12,007)**

31/12/2017	Group companies	Other related parties	TOTAL
	Thousand Euros		
Long-term debts with group and associate companies (Note 14)	(941,481)	-	**(941,481)**
Short-term debts with group and associate companies (Note 14)	(517,587)	-	**(517,587)**

At the year ended at December 31st 2018 the Company recorded under "Long-term and short-term payables to group companies and associates" loans from the related company Madrileña Red de Gas Finance BV and its Sole Shareholder Elisandra Spain V, S.L.U. in the amount of 954,647 thousand euros (1,459,068 thousand euros in December 31st 2017) where the loans conditions are described in the Note 14.

b) Transactions with related parties

31/12/2018	Group companies	Other related parties	TOTAL
	Thousand Euros		
INCOME			
Services rendered	9	-	**9**
EXPENSES			
Interest expenses (Note 18)	(42,520)	-	**(42,520)**
Others	(129)	(175)	**(304)**

(Expressed in thousand of euros)

			Thousands euros
31/12/2017	**Group companies**	**Other related parties**	**Total**
INCOME			
Services rendered	5	-	**5**
EXPENSES			
Interest expenses (Note 14)	(24,473)	-	**(24,473)**
Other	(172)	(87)	**(259)**

At December 31st 2018 Consilia Asesores S.L., which holds the presidency of the Board of Directors represented by Pedro Mielgo, has received 175 thousand euros (December 31st 2017: 87 thousand euros) for advising and consulting regarding the signed contract.

All the transactions realized between group companies are at market price.

21. Auditors' fees

The fees charged at December 31st 2018 financial year by PricewaterhouseCoopers Auditores, S.L. for auditing the annual accounts and other related limited reviews and audits works were 71 thousand euros (December 31st 2017: 31 thousand euros). On December 31 2018 and 2017 has not been earned by fees charged for other audit related services

Similarly, the fees accruing at December 31st 2018 financial year for other companies using the PricewaterhouseCoopers brand as a result of other services provided to the Company were 409 thousand euros (December 31st 2017: 116 thousand euros).

22. Environmental information

The Company has not received any subsidies or income as a result of activities related to the environment. The Company has no assets related to the environment and has incurred expenses to comply with and adapt to current legislation and regulations, as well as to the maintenance of the environmental management.

On August 27th 2004 Royal Decree Law 5/2004 was passed which governs the system of trading emission rights of greenhouse gases, with the purpose of assisting to comply with the obligations deriving from the Kyoto Convention and Protocol. Due to the nature of its activities the Company does not have allocations of CO_2 emissions nor expenses deriving from the consumption of emission rights. The Management of the Company does not anticipate any type of penalty or contingency deriving from compliance with the requirements laid down in Act 1/2005.

23. Other Commitments and contingencies

Commitments

As of December 31st 2018 there is a total of 38,480 thousand euros guaranteed (December 31st 2017: 5,721 thousand euros) by different bank entities. Of the aforementioned total amount; 4,836 thousand euros are guaranteed by different banks entities against local city councils for work carried out in the municipalities in which the Company operates; and 33,644 thousand euros guaranteed by different banks entities against tax authorities for the open inspections of 2012-2013. The Company's Directors estimates that given the nature of the guarantees, it does not exist any risk that originates no preview liabilities.

Contingencies

As a result of the tax inspections which commenced in the year 2015 over the 2010 and 2011 tax, on February 17th 2016 the Company was notified of the settlement agreement for corporate income tax relating to 2010, which resulted in tax payable totalling 5,487,857 euros, paid by the Company on April 5th 2016, largely due to the inspector's approach to the deductibility of certain expenses, facts that have not arisen any sanction. Additionally, on February 29th 2016 the Company was notified about the corporate income tax settlement agreement for 2011 and as explained above, although it resulted in an adjustment to the accounting result which reduced the Company's losses by 1,752 euros, it resulted in zero tax payable. Both assessments were contested,

On March 15th 2016 the Company filed two economic-administrative claims against the Settlement Agreements to the Central Economic and Administrative Tribunal (TEAC), requesting its accumulation for both claims to be processed jointly and in a single procedure, where the TEAC has answer on October 5, 2016 with a notification accepting the request, as well as the disclosure of both files with a period of one month to review and to formulate the corresponding allegations. At November 4, 2016, the Company has presented to the TEAC the allegations showing the two economic-administrative claims against the Settlement Agreements, which at the annual accounts formulation date, have not received any answer.

In case that the claims do not succeed, the greater risk for the Company amount 8,024 thousand euros in instalments, plus 929 thousand euros as default interest up to the present date.

According to the legal advisor's opinion, at December 31st 2018, the Company's Directors consider that there are high probabilities of succeeding in the economic-administrative claims. As a result, at December 31st 2018, the Company's Management has considered not necessary to register any expense regarding the amount claimed and to maintain account receivable with the Public Administrations for the amount referred before (5,359 thousand euros) in the financial statement line "(Public Administration – other credits)", as well as in the previous financial year.

Additionally, on March 15th 2016, April 22nd 2016 and May 25th 2016, the tax authorities informed the Company of the initiation of a corporate tax review for the fiscal years ended in 2012 and 2013, and a VAT review for the second semester of 2011, and for the years 2012 and 2013.

As a result of such inspections, on July 17th 2017 the tax authorities issued provisional assesments resulting in a proposal for tax payable of 28,008 thousand euros in respect of corporate income tax plus late-payment interest of 5,036 thousand euros, on the understanding that the expenses relating mainly to the tax amortization of the administrative concessions, increase in the value of assets and goodwill, among others, are not deductible in those years as they do not yet meet the requirements to be tax deductible. The assessments raised include no penalty in respect of the tax in question and 122 thousand euros for VAT as a consequence of the inspection criteria on the deductibility of certain expenses plus late-payment interest of 24 thousand euros. The company has signed both tax assessments in disagreement and has filed its response to the assessments and is awaiting the receipt of the final settlement agreements, of the Corporate Income Tax, that has been payed by the Company on March 1st, 2018.

On January 16th, 2018, the Company was notified of the definitive settlement agreement corresponding to the Value Added Tax, which confirms the content of the provisional assesments, in accordance with the previous paragraph, for an amount of 122 thousand euros in installments and 26 thousand euros for late-payment interest. and have been payed on 1st 2018, by the company.

On March 8th, 2018, the Company has been notified of the definitive settlement agreement corresponding to the Corporate Income Tax, which confirms the content of the provisional assesments, in accordance with the previous paragraph, for an amount of 28,022 thousand euros in installments and 5,622 thousand euros for late-payment interest.

In case of future allegations do not succeed, the greater impact for the Company for the two years that were reviewed (2012 and 2013) will be an expense of 16,280 thousand euros as a greater corporate tax quota, and a default interest expense of 6,508 thousand euros corresponding to corporate income tax until the date of notification of the settlement agreement and a lower deferred tax asset by 5,219 thousand euros and a lower deferred tax liability of 16,714 thousand euros, although the right to deduct part of the expenses questioned by the inspection would remain in force.

At the annual accounts formulation date and for the next fiscal years, some of the circumstances questioned in the inspections would remain in force.

Having realised the allegations of the claims filed, and according to the Company's legal advisor's opinion, at the time the annual accounts were drafted, the Company considers that it has solid arguments to defend its position in relation the deductibility of such expenses, and as a result, at December 31st 2018, the Company's Management considers it reasonable to not recognise any expense or assets relating to the amounts claimed.

24. Subsequent events

There have been no significant events since the end of the year and up to the date of the preparation of these financial statements, which the Company believes may significantly affect them.

MADRILEÑA RED DE GAS, S.A.U.

DIRECTORS REPORT FOR THE YEAR ENDED ON 31 DECEMBER 2018

COMPANY'S ORIGIN

On February 11th 2009, the National Competition Commission (NCC) resolved to subordinate the authorisation of the concentration process by which the Gas Natural Group (Gas Natural) would acquire Unión Fenosa, subject to the former meeting certain divestment commitments.

These divestment commitments were described in an action plan approved by the NCC on 17th March 2009.

As a result of this divestment process, on 30th April 2010 MSIP Violín BV, acquired the natural gas distribution activity in certain municipalities of Madrid, split on 30th March 2010, from Gas Natural Distribución SDG S.A..This acquisition was authorised by the NCC on 24th March 2010.

Subsequently, on January 24th 2011, the NCC amended the action plan requiring Gas Natural to carry out additional divestments. As a result of the above and of a new split, the natural gas distribution activity was contributed to Madrileña Red de gas II, S.A. in various municipalities of Madrid, and some of its districts. This line of activity was also being carried out by Gas Natural Distribución SDG S.A. This split was entered in the Barcelona Mercantile Registry on June 30th 2011.

On this date the Madrileña Red de Gas group acquired Madrileña Red de Gas II, S.A. This acquisition, which had been authorised by the NCC and by the National Energy Commission on 11th and 12th May 2011 respectively, was subject to authorisation by the Community of Madrid. This authorisation was given on May 31st 2011.

On May 7th 2015, MSIP Violín BV sold all its shares to Elisandra V Spain, S.L., controlled by the consortium formed by Gingko Tree Investment Ltd., PGGM Infrastructure Funds and EDF Invest with the subsequent inclusion of Lancashire County Pension Fund to the consortium, it has been set up the solely shareholder of the company at the closing date of the tax year.

On July 25th, 2017, The General Meeting of Shareholders approved the transfer of the shareholdings held by Lancashire County Pension Fund, representing 12.50% of the share capital of Elisandra Spain IV, S.L to LPPI Insfrastructure Investment LP. By October 2017 Lancashire County Pension Fund had contributed its 12.5% stake in the company to the pooled investments vehicle, LPPI Infrastructure Investments LP, which is owned by it and the London Pension Fund Authority.

(Expressed in thousand of euros)

DEVELOPMENT OF THE BUSINESS

The Company obtained an EBITDA of 141.4 million euros during the year ended on December 31st, 2018.

Revenues in the period ended on December 31st, 2018 amounted to (1) 187.9 million euros, of which 169.6 million euros relate to the gas natural business. The remaining 18.3 million euros are derived through the supply of LPG. Within the natural gas business, 87% of revenues are derived from regulated remuneration relating to distribution activity, composed of the figures established through the Ministry of Industry, Tourism and Commerce Order, 1367/2017 published in Official Gazette No. 308 of December 22, 2017, 11% of revenue relating to natural gas is derived from other regulated services with the remaining and 2% derived from other non-regulated services. In November 2016, the Company acquired, from Repsol, 505 LPG plants and related network assets comprising 41,054 supply points, in the territory of Madrid. This business contributed revenue of 18.3 million euros during the year, with an EBITDA of 4.0 million euros.

	Natural Gas	LPG	Total	
Remuneration	147.0	-	147.0	
Other regulated income	18.2	18.3	36.5	
Other non-regulated income	4.4	-	4.4	
Turnover figure	**169.6**	**18.3**	**187.9**	(1)
Operating result	**137.4**	**4.0**	**141.4**	(2)
Operating result %	81%	22%	75%	

(1) The difference in turnover is due to the charging connection and extension rights (approx. 1.6 million euros).
(2) EBITDA is defined as operating income + depreciation and amortisation + other results + provision excess + variation of provisions for commercial operations + severance payments (Note 18.c) + bank services and similar (Note 18.d) + Impairment of merchandise, raw materials and other supplies (Note 18.b).

The Company, at the year end, has administrative authorisations to perform distribution activities in 59 municipalities, including the city of Madrid, where it has authorisation for 5 districts. The total number of connection points to which the Company provides services is 903,346, of which 879,301 correspond to natural gas and 24,045 points of LPG (16,448 have been transferred to natural gas).

MRG considers financial strength as a key strategic pillar, and aims to maintain an investment grade rating as well as high ratio levels relating to solvency and liquidity. Increases in debt are accompanied by additional cash generation derived from the new investments. The company maintains a robust capital structure that is appropriate for the profile of a regulated business.

In this context, on April 11th 2017, the Company completed two new issuances under the existing EMTN program. The issuance was completed by Madrileña Red de Gas Finance BV, which then on lent the funds to MRG through an inter-company loan structure. Both issuances were for 300 million each with terms of 8 and 12 years. At the same time, the Company secured a contingent credit facility (Revolving Credit Facility) totalling 200 million euros with a 5 years maturity, replacing previous credit lines totalling 175 million euros. The program is guaranteed by MRG and is listed on the Luxembourg stock exchange.

The net equity of Madrileña Red de Gas S.A.U. is €233.3 million, the majority of which consists of freely-available reserves. On April 27th, 2018 the sole shareholder approved the distribution of a dividend which was charged in the amounts of 116,000 thousand euros charged to the share premium that has been disbursement on 2018. On November 28th 2018 the sole shareholder approved the distribution of dividend which was charged in the amounts of 6,600 thousand euros charged to the share premium that has been disbursement on 2018. There was 4,375 thousand euros pending to be disbursed, which has been disbursement this fiscal year.

Share capital is currently represented by 104,759 ordinary registered shares with a par value of 10 euros each, fully paid in and with the same voting and economic rights.

BUSINESS OUTLOOK

The company's strategy for the following years continues to focus on financing the growth of its current distribution network to municipalities adjacent to its existing territories which do not currently have natural gas supply, as well as gaining new connection points in its existing territories of operation.

As part of this strategy, the Company will continue to undertake the conversion of LPG supply points it owns to natural gas connection points

ENVIRONMENT

The Company has not received environmental subsidies or income as a result of the activities relating to the environment. The Company has no assets nor has it incurred in expenses related to the environment. The company has incurred in some expenses in order to accomplish and adapt to the current legislation and regulation, thereby to the maintenance of the management environmental system.

STAFF

There were 150 Company employees at the 2018 fiscal year end, of whom 21 are part-time retirees.

RESEARCH AND DEVELOPMENT

The Company has carried out research and development processes during the year.

TREASURY SHARES

The parent Company has not acquired treasury shares during the year.

AVERAGE PAYMENT PERIOD TO SUPPLIERS

The average payment period of suppliers is of 66 days (65 days in at December 31st 2017)

SUBSEQUENT EVENTS

There have been no significant events since the end of the year and up to the date of the preparation of these annual accounts, which the Company believes may significantly affect them.

USE OF FINANCIAL INSTRUMENTS

The Company's activities have no significant exposure to exchange rate risk and the fluctuation of interest rate. However, the Company is exposed to credit and liquidity risk.

The Company´s Management focuses on maintaining a solid financial structure that optimises the cost of capital and the availability of financial resources to guarantee business continuity over the long term, in order to enhance value for shareholders while ensuring a solid credit profile. In this regard, the senior unsecured debt credit ratings assigned to the Company by Standard & Poor´s and Fitch remains, respectively at BBB.

Credit risk

In accordance with its corporate objects, the Company collects for the gas system the amounts relating to tolls to access the connection point network located in its distribution territory by invoicing to supply companies. On a monthly basis and within the settlement system framework coordinated by CNMC, a calculation is performed of the excess or shortfall in access tolls invoicing with respect to the remuneration recognised to the Company. If toll invoicing exceeds the remuneration recognised, the Company must settle such difference in favour of other gas system companies. Otherwise, the Company will receive from such companies the remaining balance to complete the remuneration recognised.

Regulations in this respect consider tolls invoiced to the supply companies to be collected for the purposes of the settlement system described above, and therefore in the event of non-payment by such counterparties, the Company is exposed to a credit risk with respect to part of its revenues.

The Company actively manages the aforementioned credit risk through a follow-up of outstanding receivable balances. Similarly, and taking into account (i) the reduced average collection period, less than 30 days, (ii) the regulatory supervisory framework in which gas system activities are performed and (iii) the mechanisms for suspending the contracts for Third-party Network Access in the event of non-payment of tolls to the Company (after a period of 60 days after a reliable request of the counterparty), exposure to the credit risk is considered to be limited.

Interest rate risk

During the current year, the Company has been exposed to several financial risks, mainly to interest rate risk.

The Company's interest rate risk results from long-term borrowings.

Borrowings issued at fixed rates expose the Company to the fair value of its financial liabilities.

Liquidity and availability of funding risks

The Company maintains a liquidity policy that ensures compliance with the payment commitments acquired, diversifying the coverage of financing needs and debt maturities. Prudent liquidity risk management includes the maintenance of sufficient cash and realizable assets and the availability of funds for an adequate amount to cover the obligations.

At December 31, 2018, available liquidity amounts to 263,042 thousand euros (December 31st 2017: 816,025 thousand euros), taking into account cash and equivalents (63,042 thousand euros in December 31st 2018 and 616,025 thousand euros in December 31st 2017) and unused equivalent credit lines (200,000 thousand euros in December 31st 2018 and 200,000 thousand euros in December 31st 2017) (Note 14).

The Company's business and investment plans are mainly financed through cash generated from on-going operations and, occasionally, through revolving credit facilities.

It is the Company policy to match the debt's amortisation calendar to its capacity to generate cash flows to meet these maturities. In particular, the Company's Management attempts to ensure that the operations over the next 12 months are always fully financed without the need to substantially modify the conditions and structure of the Company's debt.

Management considers the Company has enough cash reserves to address the payments to realize the following 12 months.