# FINANCIAL STATEMENTS AT DECEMBER 31, 2016

*Giacopiane Dam*



# TIRRENO POWER SPA

**Registered Office: Via Barberini 47, Rome**
**Share Capital Euro 60,516,142.00 fully paid**
**VAT no., Fiscal Code and Business Register of Rome n. 07242841000**
**Administrative Business Registry n. 1019536**
Administrative office and Naples facility: Stradone Vigliena 39, Naples
Torrevaldaliga facility: Via Aurelia 2, Civitavecchia (Rome)
Vado Ligure facility: Via A. Diaz 128, Valleggia of Quiliano (Savona)
Renewable Sources Area: Corso Torino 1, Genoa

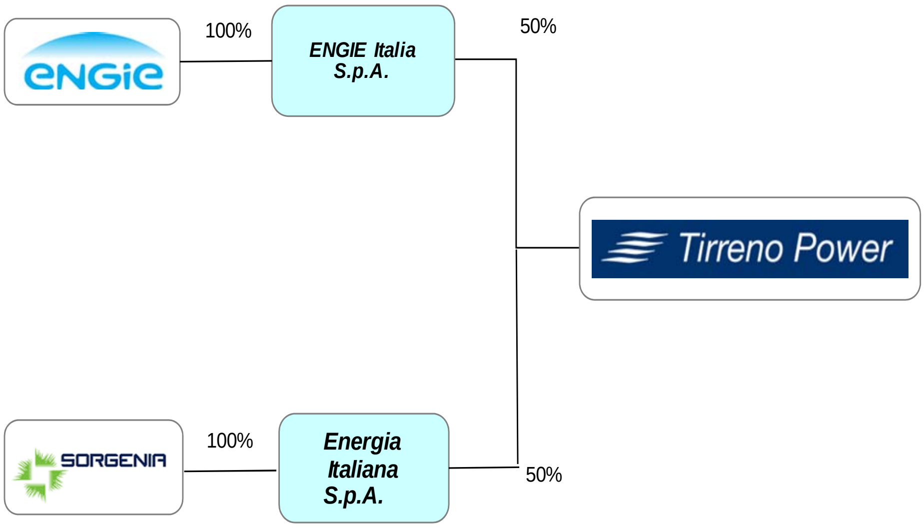
INDEX

*Osiglia Dam*

## Introduction

### Ownership structure

The Company at December 31, 2016 is jointly owned by Energia Italiana S.p.A. and Engie Italia S.p.A.. It should be noted that, effective from September 1, 2016, GDF SUEZ Energia Italia S.p.A. changed its name to ENGIE Italia S.p.A..



## Corporate bodies

| Board of Directors | |
|---|---|
| **Chairman** | Alberto Bigi |
| **Directors** | Aldo Chiarini<br>Giovanni Chiura<br>Angelica Orlando<br>Pascal Renaud<br>Giuseppe Gatti<br>Antonio Cardani *<br>Roberto Garbati * |

| Board of Statutory Auditors | |
|---|---|
| **Chairman** | Gianluca Marini |
| **Statutory Auditors** | Carlo De Matteo<br>Maurizio Lauri<br>Adriano Rossi<br>Riccardo Zingales |
| **Alternate auditors** | Hinna Danesi Goffredo<br>Panagia Giuseppe |

| Independent Auditors |
|---|
| *EY S.p.A.* |

** Independent directors, as set forth in the Company's Articles of Association.*

## Operating structure

The Company operates in Italy through thermoelectric and renewable plants along the Tyrrhenian Sea area.

The following table summarises the main characteristics of such facilities:

| Production Units | Gross reference capacity - commercial operation (MW) as at 12.31.2016 | as at 12.31.2015 | Region |
|---|---|---|---|
| Vado Ligure plant | 793 | 1453* | Liguria |
| Torrevaldaliga plant | 1,176 | 1,176 | Lazio |
| Naples plant | 401 | 401 | Campania |
| **Thermoelectric total** | **2,370** | **3,030** | |
| **Total - Renewable Sources** | **75** | **75** | Primarily in Liguria |
| **Total** | **2,445** | **3,105** | |

* as at December 31, 2015, the two coal-fired production units were also included, definitively now out of service

With its production plants, the Company is able to generate electricity with high flexibility and competitiveness:

- the thermoelectric production units consist of 4 gas-powered combined-cycle plants;
- the renewable sources include 18 hydroelectric plants (divided equally between "run-of-river" and "power regulation" stations) located along the entire Ligurian Apennines.

It should be noted, on June 6, 2016, the Company's Board of Directors held that the conditions did not exist to allow a future return to service of coal-fired units 3 and 4 of the Vado Ligure plant, for a total capacity of 660 MW, that were already discontinued since they were subject to a seizure order from the Court of Savona starting from March 2014.

In fact, the Board acknowledged that, 27 months on from the seizure, during which the logistics infrastructures essential for the operation of coal-fired units also gradually stopped working, the social context changed considerably: the end of electricity production from coal is a stated objective of the Government, local institutions and is also expected by the general population. In this regard, it should be noted that, on December 23, 2016, the Company obtained a favourable opinion from the Ministry of Economic Development for definitively putting coal-powered units VL3 and VL4 out of service.

Tirreno Power - fully aware that the definitive cessation of activities in the coal-fired plants in Vado Ligure deprives the area of one of the most important industrial companies and employers - has launched an initiative for the re-industrialisation of the site, aimed at encouraging the installation of new companies with the objective of contributing to the search for solutions that may provide future jobs for workers and growth prospects for the area.

For complete disclosure, it should be noted that, in this regard:

- On March 11, 2014 the G.I.P. of the Court of Savona, in the criminal proceedings opened by the Prosecutor of the Republic of Savona due to an environmental disaster, initiated in previous years against unknown persons and which, from the month of November 2013 saw the previous Central Managers as well as the previous General Manager as suspects, in upholding a request by the prosecutor, has ordered the seizure of the VL3 and VL4 units, believing that the free availability on the part of the suspects, of the industrial coal plant may aggravate the offense for which the criminal investigation is ongoing. On March 14, 2014, the Company received notice from Ministry of Environment of the invitation to start, by the middle of April, works on the construction of a new coal-fired unit (VL6), under penalty of suspension of operation of the VL3 and VL4 parts of the plant. On April 9, 2014, the Company filed an appeal to the Lazio Regional Administrative Court against the formal notice received, requesting, based on prior suspension of the execution, the cancellation of the Ministry's provision. On April 11, 2014 the Presiding Judge of the Regional Administrative Court upheld the application for a precautionary measure of a single judge of the applicant (i.e. suspension of the effectiveness of the measure disputed by the Company), postponing the collective discussion of the precautionary application to the Council Chamber of May 7, 2014.
- On April 10, 2014, the Company presented the G.I.P. (Preliminary Judge) of the Court of Savona with an application for the temporary and restricted operation of the VL3 and VL4 units subject to seizure, in order to dispose of coal stocks present at the Vado Ligure site, taking into account the proposed danger of spontaneous combustion of the same because of the pronounced state of oxidation. The application has not been upheld.
- On May 6, 2014 an application was filed for early renewal of the AIA (integrated environmental authorisation) of the entire Vado Ligure production site that makes provision for a series of environmental works, divided into two phases, aimed at improving the emissions of the coal units with alignment with MTDs (Best Available Technology) from the outset.



- The Lazio Regional Administrative Court, during the hearing on May 7, rejected the application for suspension of the effectiveness of the MATTM (Ministry of the Environment and Land and Sea Protection) measure on the start of works of the VL6 unit owing to lack of actual and concrete injury (danger in delay), but at the same time, recognised the existence of a connection with the decision of the appeals pending for the cancellation of the AU (single authorisation) of the VL6 and of the AIA, discussed on May 15, asking the Presiding Judge of the Regional Administrative Court to assign the analysis of the merits of the case to the most appropriate section of the Court. At the hearing on May 15 cited above, the Lazio TAR (Regional Administrative Court) section II quater, considering the application for renewal submitted by the company, ordered the cancellation of the appeals from the roll, assigning a deadline to the interested parties for the resumption of the appeals following the outcome of the AIA (integrated environmental authorisation) renewal procedure.
- On May 14, 2014 applications were filed for the release from seizure and for the replacement of the legal custodian; only the latter was upheld.
- In light of the Vado Ligure situation, the company Certiquality suspended the ISO14001 certification for coal plants, and the Italian EMAS section of the Committee for Ecolabel and Ecoaudit suspended the EMAS registration of the plant. In fact, in view of the preventive seizure of March 11, 2014 making it impossible to verify the environmental management system of some of the activities included in the scope of certification, the decision was taken to suspend the certification with reference to production units VL3 and VL4. Given that the gas turbine units of the Vado Ligure site is not affected by the aforementioned restraint measure, also in view of the

results of checks carried out in January 2014, which did not highlight any elements as such to prevent retention of the ISO 14001 certification, the suspension decision does not apply for said unit.

- On July 21, 2014 the Savona GIP (preliminary judge) issued a decision by which it rejected the request for release from seizure / temporary operation of the seized units VL3 and VL4; the Company has decided not to appeal against that decision pending the conclusion of the AIA renewal process already started.
- The Company, in response to requests received gradually from the CT appointed by the prosecutor in Savona, provided all the required documentation.
- On October 13, 2014, the MATTM sent Tirreno Power the convocation to the Services Conference (CdS) for the issue of the AIA for November 18, 2014, by sending the Preliminary Investigation Definitive Opinion (PIC) of the IPPC Commission and the ISPRA Monitoring and Control Plan (PMC).
- The Company submitted observations to the MATTM, and also requested a hearing before the Investigating Group in order to be able to adequately explain its position. In fact, the provisions of the PIC were divided into three categories for observation purposes: those which cannot be upheld, those not feasible from a technical point of view, because if not resolved render any activity impossible, and finally those that require some clarifications. That hearing took place on November 14, 2014.
- On October 31, 2014 the Services Conference was held for obtainment of the authorisation of the MISE (Ministry of Economic Development) for the construction of the bunker; the conference was successful. On November 6, the Liguria Region resolved to stipulate the agreement required for the issuance of the Single Authorisation for the construction of the roof for the coal facility. It is still awaiting issuance of the Decree by the MISE.
- On November 18, 2014, the Services Conference, at the MATTM, was postponed to November 25, 2014 at the request of the mayors of the municipalities of Vado Ligure and Quiliano and Liguria Region, who could not be present because of the bad weather emergency in Liguria in the days immediately prior to the conference. On November 25, 2014 during the course of the Services Conference two memorandums were produced, one by the Ministry of Health and one by the ASL 2 of Savona; the representatives of the Region therefore requested the conference to be put back another week to better evaluate the information in the above memorandums. The mayors of the municipalities of Vado Ligure and Quiliano share the request and the Ministry has called a new conference for December 4, 2014. Meanwhile, the Region and the Local Authorities resolved, to cancel the previous resolutions of consent to Tirreno Power’s proposal, to not be able to express an opinion as part of the early renewal of the AIA for the operation of the Tirreno Power thermoelectric plant and, consequently, to request the suspension of the procedure from the MATTM, in order to involve the Council of Ministers. The MATTM, by means of its memorandum, has rejected the requests of the Region and Local Authorities, by asking them, under Article. 14 quater of Law 241/90, to express an opinion at the Services Conference, in fact, considering the failure to express an opinion equivalent to agreeing with the opinion of the Investigation Commission.
- The Services Conference, which took place on December 4, basically ratified the decisions of the IPPC Commission Investigation, requiring Tirreno Power to implement the upgrades planned in one phase, with even more restrictive limits than those proposed by the Company, thereby preventing plant operations for about 16/20 months.

- On December 31, 2014 the company was also notified of the decree of the Ministry of Economic Development containing the single authorisation for the bunker roof. On February 27, 2015 Tirreno Power filed an appeal against this decree to the Lazio Regional Administrative Court. The main reason for the appeal concerns the illegitimacy of the term for the start of works prescribed in the decree, as it does not take into account the provisions of Art. 1-quater of Law 290/03. This Article sets forth that the proposer has the right to start works in the 12 months following the incontestability of the authorisation measure.

- January 13, 2015 saw the publication in the Official Gazette of the Italian Republic, of the press release regarding the issuing, on December 31, 2014, by the Ministry of the Environment and for Land and Sea Protection, of AIA Decree no. 323 for the operation of the Vado Ligure Plant.

- On February 23, 2015 Tirreno Power filed an appeal to the Lazio Regional Administrative Court against the abovementioned AIA decree. The main reasons for the objection regard:
  - the lack of investigation by the IPPC commission (Integrated Pollution Prevention Control) with respect to the proposal of the Manager in relation to the emission limits to be respected, to their gradual achievement through two phases and the timing of the work that takes into account the unavailability of the plant because of its seizure.
  - The unreasonable timelines set forth for the construction of the bunker (March 14, 2015).
  - Unsound reasoning of the request for the immediate construction of the plant for the treatment of the “boron” parameter in wastewater, owing to the need for such treatment only with the coal sections in operation.
  - The inconsistency of the request of the construction of the plant necessary for the start-up of coal units through the use of methane, without allowing a transitional period equal to the time required to supply and install the necessary components, in the face of an almost zero environmental benefit.



- On June 18, 2015 Tirreno Power was informed of the notice of conclusion of preliminary investigations, pursuant to art. 415 bis of the Criminal Procedure Code on the criminal proceedings pending before the Public Prosecutor of Savona (environmental disaster). The process involves senior management and employees of Tirreno Power for offences under Article 434 paragraph I and II of the Criminal Code, in relation to an alleged health and environmental disaster caused by the operation of the thermal power plant located in Vado Ligure (SV) as well as for complicity in abuse of office (art. 323 of the Criminal Code) in administrative proceedings for the issuing of AIA measures and multiple manslaughter. In the proceedings, the prosecutor sought and was granted by decree of the preliminary judge of Savona of March 11, 2014 - executed on the same date - the preventive seizure of the generator units called VL3 and VL4 of the Vado Ligure thermoelectric plant, whose operation is still restricted.

- On July 20, 2016 the Company was notified by the Prosecutor of Savona of a new notice of conclusion of preliminary investigations pursuant to art. 415 bis of the Code of Criminal Procedure. This new notice involved:
  - the reduction of the number of suspects to 27;
  - the objection to the offence of environmental and health disaster, due to negligence (and no longer malicious conduct);

  - the removal of the notification of multiple manslaughter, to allow the prosecutor to conduct further investigations in order to prove the essential causal link between the emissions of the T.P. Vado/Quiliano plant and the harmful events in order to ascertain the individual responsibilities;
  - the removal of the objection of abuse of office transmitted to the Rome Judicial Authorities given considered jurisdictionally responsible.

- On October 25, 2016, the Public Prosecutors filed a request to the Office of the Judge for the Preliminary Hearing to postpone the proceedings, in relation to the charges described in the second notice pursuant to art. 415 of the Code of Criminal Procedure. The current charge includes, in effect, slight changes with respect to the latest notice of closing remarks of the preliminary investigations. In relation to the description of the disaster event, allegedly caused by the wrongful conduct of the defendants, significant deterioration of “marine sediments” is no longer included, alongside that of air quality and the conditions of the flora. The Preliminary Hearing notice has still not been notified, which is expected to be set no earlier than the summer of 2017.

- On January 28, 2017, the Preliminary Judge of the Court of Rome issued a judgment of dismissal pursuant to articles 409 and 410 of the Code of Criminal Procedure, upholding the request from the Public Prosecutor at the Court of Rome, in relation to the offence of abuse of office contested in the notice of closing of the preliminary investigations of July 20, 2016 vis-a-vis institutional and technical top management of the Liguria Region, the Province of Savona and the Municipalities concerned, as well as against an executive of Tirreno Power, abuse allegedly committed in order to obtain the AIA for the VL3 and VL4 coal-powered plants.

In addition, on May 9, 2014 the Company was served notice of the closure of the preliminary investigations regarding the criminal proceedings concerning waste management and, at the same time, the inclusion of the same in the register of suspects pursuant to Law 231/2001. In relation to said proceedings, the Preliminary Judge of the Court of Genoa, with judgment filed on March 6, 2015, declared that the Court did not hold territorial jurisdiction, referring the case to the Public Prosecutor’s Office at the Court of Turin. At the date of drafting of this document, no request to postpone sentencing had been formulated.



Please refer to note 28.2 for the evaluations regarding the contingent liabilities connected with the provisions that concern the coal units of the Vado Ligure site.


*Vado Ligure plant*

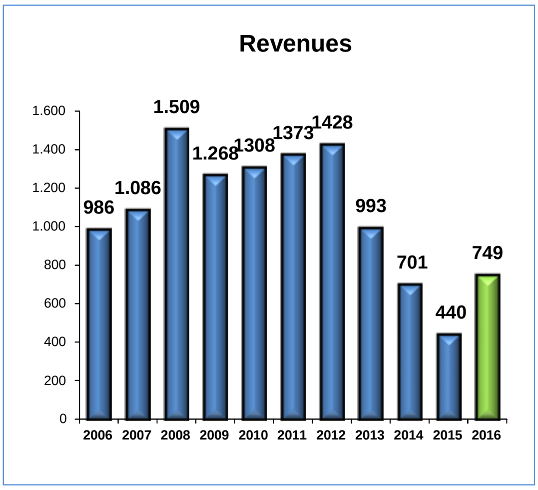
## Focus on Results

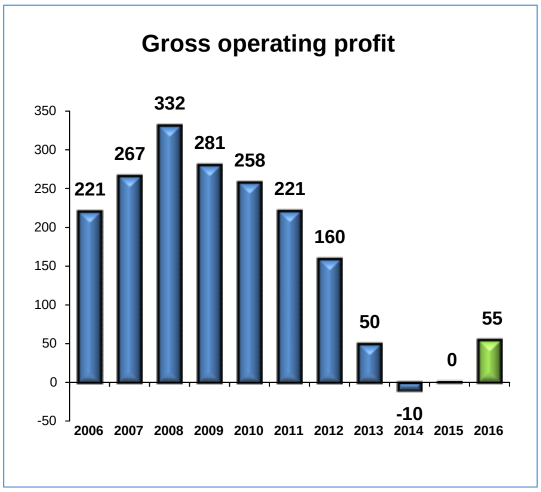
With the objective of presenting the results and analysing the financial structure, the tables below contain some “alternative performance indicators” which management feels are most representative of the economic and financial results that are contained in the reclassified schedules that differ from those set forth in the international accounting standards adopted. In this section we provide the criteria used to calculate these indicators, in line with ESMA recommendation Guidelines on Alternative Performance Measures. The data, unless otherwise specified, may be directly deduced from the financial statements.

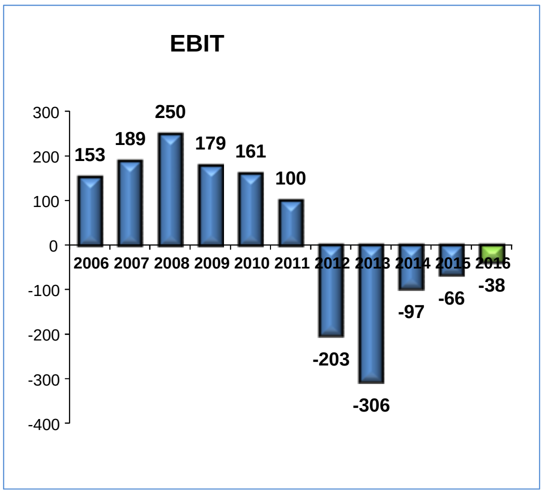
## Highlights of the Company

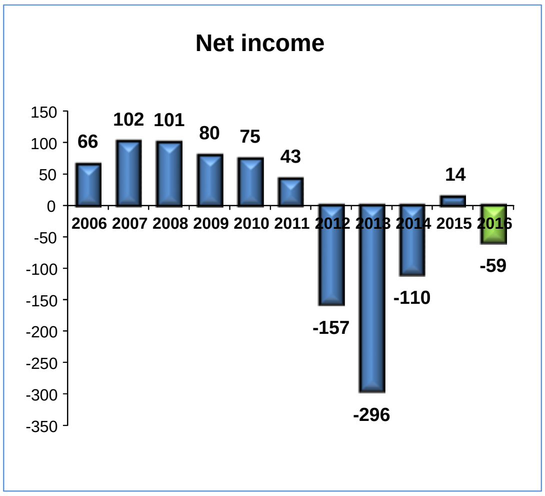
| | 12.31.2016 | 12.31.2015 | Change % |
|---|---|---|---|
| **Income statement data** (millions of Euro) | | | |
| Total revenues | 748,7 | 440,1 | 70,1% |
| *-of which revenues from energy sales* | *738,4* | *424,3* | *74,0%* |
| Gross operating profit | 54,7 | 0,2 | *n.a.* |
| EBITDA | 21,8 | (8,8) | 348,1% |
| EBIT | (38,2) | (66,5) | 42,6% |
| Net income for the period | (58,7) | 13,9 | -522,5% |
| **Equity and financial data** (millions of Euro ) | | | |
| Investments in fixed assets | 40,8 | 4,9 | 728,6% |
| Cash flow from operating activities | 91,5 | (36,5) | *350,5%* |
| Shareholders' equity | 198,7 | 257,9 | *-22,9%* |
| Net capital employed | 713,2 | 823,0 | -13,3% |
| Net financial debt | 514,4 | 565,1 | -9,0% |
| Debt/Equity | 2,6 | 2,2 | *18,1%* |
| **Operating data** | | | |
| Energy sold (GWh) | 14.317 | 6.386 | 124,2% |
| Energy Injected (GWh) | 5.541 | 2.940 | 88,5% |
| Average amount (units) | 383 | 387 | -1,2% |
| **Economic/financial indicators** | | | |
| Unit revenue from energy sale (€/MWh) | 51,6 | 66,4 | -22,4% |
| ROS (Return on Sales) | -5,1% | -15,1% | -66,2% |
| ROI (Return on Investment) | -5,0% | -8,3% | -39,8% |
| **Market indicators** (annual averages) | | | |
| Price of Brent crude oil ($/barrel) (source "Platt") | 43,66 | 52,40 | -16,7% |
| US Dollar/Euro exchange rate (source UIC) | 1,054 | 1,089 | -3,2% |
| 1-month Euribor @ 365 average (source www.euribor-ebf.eu) | -0,37% | -0,21% | 79,3% |

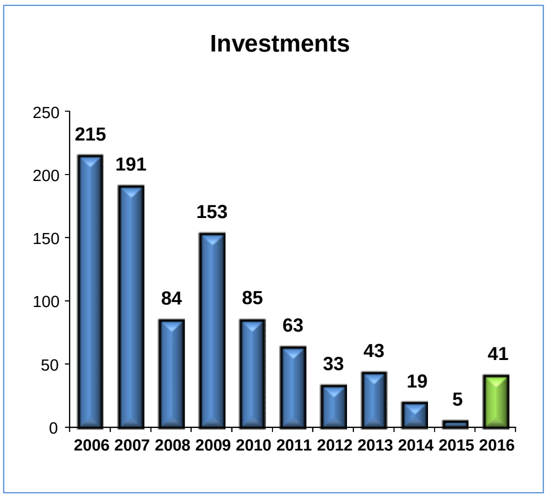
The criteria used for the construction of the indicators listed above are set out in the section Management Performance.

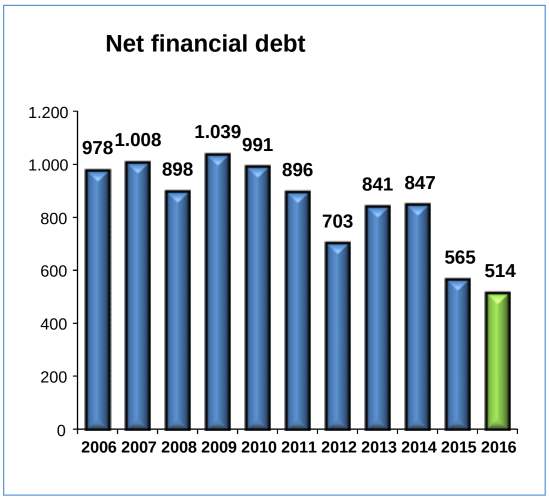

Revenues
1.509
1.268
1308
1373
1428
1.086
986
993
701
749
440
2006 2007 2008 2009 2010 2011 2012 2013 2014 2015 2016


Gross operating profit
332
267
281
258
221
221
160
50
55
0
-10
2006 2007 2008 2009 2010 2011 2012 2013 2014 2015 2016


EBIT
250
153
189
179
161
100
-203
-306
-97
-66
-38
2006 2007 2008 2009 2010 2011 2012 2013 2014 2015 2016


Net income
66
102
101
80
75
43
14
-157
-296
-110
-59
2006 2007 2008 2009 2010 2011 2012 2013 2014 2015 2016


Investments
215
191
84
153
85
63
33
43
19
5
41
2006 2007 2008 2009 2010 2011 2012 2013 2014 2015 2016


Net financial debt
978
1.008
898
1.039
991
896
703
841
847
565
514
2006 2007 2008 2009 2010 2011 2012 2013 2014 2015 2016

**Main events of 2016**

The year 2016 saw the completion of significant initiatives targeted at compliance with the Business Plan, which made it possible not only to reach all the economic and financial objectives set for 2016, but to greatly exceed them, and also allowed the finalisation of the personnel costs restructuring process and confirmation of the functioning of solely the natural gas powered units, initiatives both considered essential for compliance with the contents of the Restructuring Agreement.

In this regard, as outlined previously, it should be noted, on June 6, 2016, the Company's Board of Directors held that the conditions did not exist to allow a future return to service of coal-fired units 3 and 4 of the Vado Ligure plant, for a total capacity of 660 MW, that were already discontinued since they were subject to a seizure order from the Court of Savona starting from March 2014.

In fact, the Board acknowledged that, 27 months on from the seizure, during which the logistics infrastructures essential for the operation of coal-fired units also gradually stopped working, the social context changed considerably: the end of electricity production from coal is a stated objective of the Government, local institutions and is also expected by the general population. This decision confirmed the need to reduce the workforce through company redundancies.

In fact, in consideration, on the one hand, of compliance with the assumptions of the Plan and, therefore, the Restructuring Agreement and, on the other, the impossibility of maintaining the current staff levels, owing to the definitive putting out of service of the coal-powered units, the Company initiated a new redundancy scheme in November 2016 upon expiry of the solidarity contracts.

Therefore, following a series of meetings with social and institutional parties, an agreement was signed on December 2 with the Trade Union Organisations for the management of redundancies which makes provision not only for the use of social shock absorbers for a one-year period at all company sites (CIGS - extraordinary wage guarantee fund - for company crisis in Rome, Naples and Civitavecchia; extraordinary CIGS deriving from the correction to the Jobs Act for Vado Ligure), but for financial incentives both for voluntary exits of workers who will meet the pension requirements by 2024, and all those who declare their intention to leave the Company.

## Macroeconomic scenario

The conditions in the global economy have improved slightly. However, the prospects remain subject to factors of uncertainty; those in the United States depend on the economic policies of the new administration, whose details have still not been defined: there may be an expansionary impact, currently difficult to quantify, resulting from the initiatives announced concerning budget policy, but there could be unfavourable repercussions stemming from the adoption and circulation of commercial restrictions. Global growth could be slowed by turbulence in emerging economies connected with the normalisation of US monetary policy.

Growth continues to be modest in the Euro area, albeit gradually strengthening. The risks of deflation have fallen; inflation rose again in December, but core inflation remains low. To ensure the expansionary monetary conditions are adequate to guarantee an increase in inflation, the Governing Council of the ECB extended the bond-buying programme until at least December 2017, or longer if necessary. Monthly purchases will return to Euro 60 billion from April, as in the initial phase of the programme.

According to the available indicators, the recovery of the Italian economy continued in autumn, albeit a modest rate. Considering the trend in industrial production, electricity consumption and goods transport, which all registered growth, and the elevated business confidence indicators, GDP could have risen at a rate of around 0.2% in the fourth quarter of 2016 compared to the previous period.



The projections for the Italian economy, updated on the basis of the most recent trends, indicate that, on average, GDP should have increased by 0.9% in 2016 (based on figures corrected for the number of working days); the increase would be 0.9% for the current year too, and 1.1% for both 2018 and 2019. Economic activity would still be driven by domestic demand and, from 2017, by the gradual strengthening of foreign demand. GDP in 2019 would still be around 4% lower than 2007. The economic scenario presumes the maintenance of low long-term yields and generally relaxed credit conditions, in terms of cost and availability. This reflects the assumption of no tensions arising on the financial and banking markets in the Euro area and in Italy, nor significant increases in risk premiums and volatility; it also reflects the assumption, incorporated in market prices, of no interruption to the process of reform implemented in recent years in Italy.

On the whole, with respect to these projections, the risks for growth are still mostly downside. The main factors of uncertainty stem not only from the financial conditions but the global context. There is a particularly high risk of expansion in the global economy, with respect to that incorporated in the projections, being impacted not only by the implementation and dissemination of protectionist measures, but potential turbulence in the emerging economies.

(*source*: *Economic Bulletin no. 1, January 2017 - Bank of Italy)*

## Reference scenario

### The energy product markets

In 2016, all energy commodities marked important and above all continuous increases in value, despite recording an average below 2015.

In 2016, the price of Brent crude oil (ARA Spot Average), which significantly affects the unit cost of liquid and gaseous fuels purchased, recorded a continuous increase in price, increasing from $ 30.69/barrel in January to $ 53.60/barrel in December; however, recording an annual average below that of 2015, actually dropping from $ 52.40/barrel in 2015 to $ 43.66/barrel in 2016 (*source*: *"Platt's Crude Oil Marketwire"*).

The average price of low-sulfur fuel oil, which registered a similar trend to that of Brent crude oil, actually recorded a constant growth trend but saw a decrease in the annual average compared to the previous year, going from $ 281.15 / ton in 2015 to $ 230.92 / ton in 2016, even reaching its lowest value of $ 140.99 / ton in January 2016 (*source*: *"Platt's"*).

The average price of coal increased when compared to 2015, rising from $ 56.73 / ton to $ 59.67 / ton in 2016; the figures recorded constant growth throughout the year starting from February 2016 (lowest value recorded of $ 43.88 / ton), hitting $ 90.08/ ton in December 2016 (*source*: *"Argus"* index API#2 Northwest Europe Cif ARA).

The average price of natural gas fell compared to 2015, down from 22,005 €/MWh to 15,615 €/MWh in 2016 (source: PSV "Heren" index).

The average US dollar/Euro exchange rate was 1.10670 in 2016, a slight drop of 0.2% compared to the same period in 2015, when it stood at 1.10881 (*source*: *Italian Exchange Office).*



### Production and demand for electricity in Italy

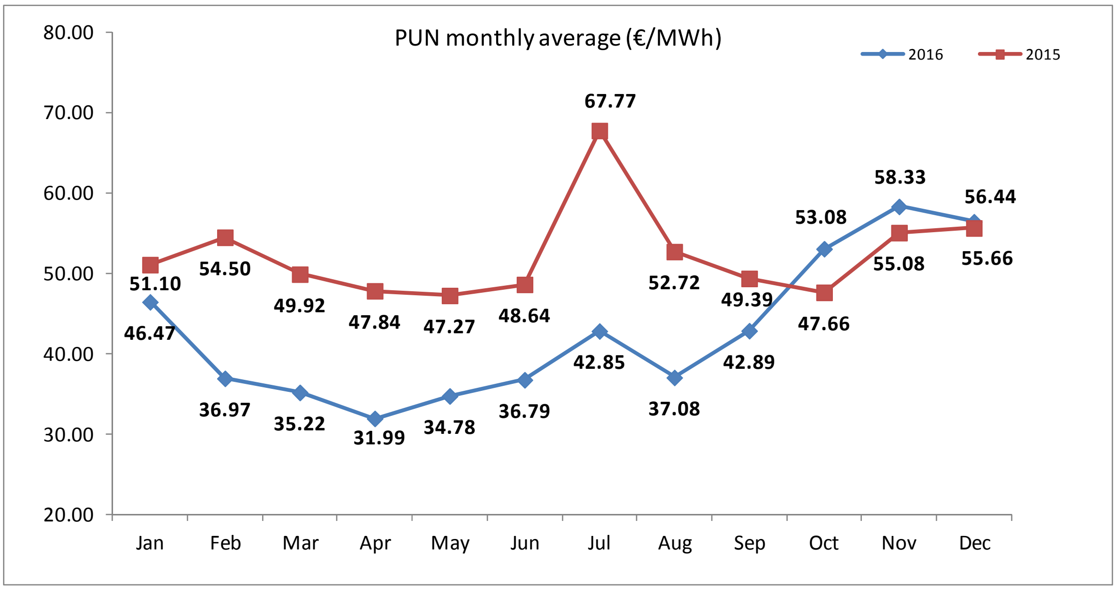
In 2016, the aggregate value of net production (276 TWh) rose slightly (+1.2%) compared to 2015, while the value of electricity supply (310 TWh) recorded a drop of 2.1% over 2015; this decrease was homogeneous in all zones of the Italian electricity market. Worthy of note is the decrease in hydroelectric production (-4 TWh, -9%), while pumping increased (+0.5 TWh equal to +27%); the foreign balance fell by as much as 9 TWh (-20%), especially in the final quarter, while wind power rose (+3 TWh, +19%); photovoltaic production was stable and, lastly, thermoelectric production rose by 5 TWh (+2.5%) (*source: Terna - Monthly Report on the Electricity System - Final balance December 2016)*

**Trend in energy sales prices**

In 2016, the arithmetic mean price of energy on the Power Exchange (PUN) amounted to € 42.78 / MWh, down by 18% compared to the 52.31 €/MWh recorded in 2015 (*source: GME*).

The price up to September always remained well below that of 2015, reflecting the lower cost of gas (Spark Spread always above 2015, with the exception of July); by contrast, the final quarter recorded a higher price than the previous year, essentially due to the criticalities which led to the shutdown of a number of French nuclear reactors, with the northern zone of the Italian electricity system in particular taking advantage of the situation. Despite the rise in the gas price, thermoelectric plants registered the best margins in the energy markets in the final quarter of the year.

The combined cycle has made the price for about 70% of the hours. The presence of a large installed photovoltaic capacity, totaling 17.7 GW (*source*: *GSE-ATLASOLE*), helps to create a price squeeze in the central hours; the price of the time profile has an average pattern that has a first peak between the hours of 8 and 11 and a second more marked peak between the hours of 18 and 22.



## Legislative and regulatory framework

The following notes report the main legislative and regulatory events of 2016, which affect Tirreno Power's reference markets.

***The implementation of the European Regulation on transparency of the wholesale market (so-called REMIT)***

The year 2015 saw the launch of the first operational phase of the regulation on the transparency of the wholesale market (so-called REMIT) with the entry into force of the obligation of communication to the European regulator (ACER) of information on standard contracts concluded in organised markets (starting in October 2015). The second phase of operations, launched in April 2016, covers the obligation of reporting of information on non-standard contracts stipulated on different platforms from the organised markets.

***European regulations relating to the electricity system***

Some European electricity system regulations are in the process of being defined, regarding balancing in particular. In particular, the European regulation on electricity balancing (Balancing Guidelines) is under discussion, which makes provision for the harmonisation of European balancing markets with the definition of common regulations for the sharing of dispatching resources between the different transmission network operators.

Furthermore, regulations (System Operation Guidelines) for the safe management of the system and regulations and responsibilities for the coordination of network operators for the management of dispatching and acquisition of the relevant services are being defined.



These regulations and their developments must be considered by the Italian regulatory authorities as part of the reforms being overseen in relation to electricity balancing (see subsequent notes).

At the end of November, the European Commission implemented a structured package of energy proposals ('winter package') which, inter alia, entailed a proposed Directive on renewable sources and proposed directives and regulations for the electricity market design. The documents outline some regulations relating to the introduction of capacity remuneration mechanisms in Europe, indications regarding price caps and floors for the wholesale markets and on priority dispatching of renewable sources.

Lastly, the Commission published its final report on the inquiry launched in 2015 on capacity remuneration mechanisms in Europe, which contained a positive judgment on the use of specific market instruments, such as the Italian capacity market, for maintaining the adequacy of the electricity system.

## Evolution of the wholesale electricity market regulations

### *Expected launch of the capacity market*

In 2016, the mechanism for the remuneration of electricity production capacity (already set forth in resolution ARG/elt 98/11) continued its pre-notification process commenced last year by the Ministry of Economic Development ("MiSE"), with the involvement of the Authority, at the Directorate-General for Competition of the European Commission.

In October, Terna published a proposed regulation for the phase of first implementation of the capacity market and a proposed amendment to the regulation for the phase of full implementation of the capacity market already approved by means of Ministerial Decree of June 30, 2014. The regulation framework makes provision for some corrections to the regulation already issued with the objective, inter alia, of ensuring it is compatible with the guidelines on State aid for the environment and energy 2014-2020 adopted by the European Commission.

Following these activities, the Authority presented consultation document 713/2016/R/eel in December, in which it defined some specific guidelines on the functioning of the mechanism, highlighting, inter alia, the need to: "anticipate the entry into operation of the capacity market through the definition of a phase of initial and prompt implementation of the mechanism" containing some specific guidelines on the functioning of the mechanism. In saying that, the Authority makes explicit reference to resolution 95/2015/R/eel, whose objective was the accelerated start-up of the mechanism with first delivery in 2017.



The actual start of the system requires approval from the European Commission and acknowledgement of the modifications made to the regulation by Terna in the latest consultation document filed in the records of the Authority and of the Ministry of Economic Development.

## The electricity dispatching reform (so-called Project RDE)

By means of Resolution 393/2015/R/eel, the Authority launched a comprehensive reform of electricity dispatching (so-called project RDE), which incorporates a series of procedures, some of which have already been in place for some time. The project is in place for the long-term, both because the framework of reference European regulations is still not definitive, and because the development times of some measures and their implementation are fairly broad.

In implementation of this reform project, in 2016 the Authority issued:

- a consultation document (298/2016/R/eel) targeted at allowing access to the Dispatching Services Market to distributed generation, to demand and all dimensions of non-programmable renewable sources, including through aggregations. Owing to the fact the European regulations on electricity balancing (see previous chapter) are currently incomplete, in the document, the Authority proposes to launch new relevant regulations in 2017 for a temporary period of around two years; however, the adoption process has still not been completed.
- A consultation document (316/2016/R/eel) targeted at revising the mechanism for the valuation of imbalances starting from 2017, which spawned resolution 444/2016/R/eel, which established some priority measures regarding effective imbalances valid from August 1, 2016.

The resolution concerns new regulations for determining the imbalance price for units of consumption and unauthorised units other than non-programmable renewable sources and, more generally speaking, the exclusion of offers accepted for secondary adjustment from the determination of imbalance prices.

- A consultation document (684/2016/R/eel) regarding imbalances containing additional proposals and which gave rise to subsequent resolution 800/2016/R/eel. The latter provisions extends the imbalance system currently in force to April 2017, in the assumption of amendments to the mechanism from May 2017 through the introduction of an imbalance system based on actual measurements.

**Other events relating to the electricity market**

In 2016, as regards the architecture of the electricity market, Terna introduced new intra-day market sessions, coordinated with new balancing services market sessions, improving the possibility for adjustment of the production profiles for operators.

In December, by realigning the Italian system with the European standards, the GME started the new weekly settlement system in relation to the Day-ahead and Intra-Day and the PCE (forward energy accounts platform) energy markets.

In December, in implementation of European Regulation 1222/2015, so-called CACM, the Authority launched a consultation targeted at coordinating the Italian intra-day market with the European one.

**Ministerial Decree on incentives for renewable sources**



In June 2016, the Ministerial Decree containing the regulation of incentives for plants powered by renewable sources other than photovoltaic power was definitively approved (Ministerial Decree of June 23, 2016). The new rules shall replace the provisions of the previous decree of 2012 and will apply until the pre-set total expenditure on incentives is reached (Euro 5.8 billion / year).

The decree does not contain any substantial changes to the previous regulations, with the main elements of the regulation remaining unchanged, including the provision of quotas for capacity that can be incentivised, differentiated by source and diversified access mechanisms based on plant size (auctions and registers).

According to the elements outlined by the Government, the decree may provide incentives of up to Euro 9 billion (over a period of 20 years) for a capacity quota of 1,370 MW.

In 2016, as set out in the Ministerial Decree of July 6, 2012, the Green Certificates mechanism was definitively replaced with a new form of incentive. The entities that already accrued the right to receive green certificates on their production (owners of IAFR qualified plants) retain the benefit for the remaining facilitated period that is transformed to a tariff (additional tariff with respect to the revenues obtained for the sale of energy) paid by GSE based on the net production of energy.

**Evolution of the gas sector legislation**

**The reform of the gas balancing market**

In June 2016, the Authority defined the gas balancing code (valid from the thermal year 2016-17), in implementation of the relevant EU Regulation of 2014. The resolution also defines the start of the new gas balancing system, with the associated criteria for intervention from the balancing manager, the methods of determining the imbalance price and disclosure obligations. An organised market is also introduced for the exchange of stored gas accessible, in cases of operational or safety requirements, by the balancing manager too.

**The reform of the transfer of gas transportation capacity**

Following two consultations held in 2015 on the matter, in 2016 the Authority issued the expected reform of the gas transfers for redelivery points that feed thermoelectric plants (pilot project that may later be extended to additional gas network users).

Resolution 336/2016/R/gas, partly deviating from the proposal contained in the last consultation, makes provision for the maintenance of an ex-ante transfer, with the introduction of a daily product by January 2017. By contrast, the penalties applicable solely to the delivery point are expected to be recalculated on a daily basis from the start of the current thermal year.

**Acts directly relating to Tirreno Power**



***The judgment of the Council of State on gas pricing 2014-2017***

In 2015, the Council of State published the Judgment by means of which it definitively upheld the petitions of certain operators (including Tirreno Power) against the 2014-2017 gas transportation tariff system defined by the Authority (Council of State Judgment 3735/2015). As reported by the applicants, in fact, the regulator did not take into account specific legal rules that established the need for flexibility and cost-effectiveness measures for those entities subject to the highest consumption of natural gas (so-called tariff digression). The judgment confirms the guidelines previously expressed by the Lombardy Regional Administrative Court.

The Authority is required to comply with the operative part of the ruling, by introducing measures to revise the pricing criteria for the 2014-2017 period.

Even though, last September, by means of resolution 429/2015/R/gas, the Authority had launched a procedure for defining the criteria for compliance with the provisions of the Council of State, the recent resolution regarding gas transfers (see previous paragraph) does not contain suitable measures for compliance with the provisions of the judgment and does not make reference to the procedure launched.

As a result of that, Tirreno Power and the other operators, already plaintiffs against the provisions relating to the 2014-2017 gas tariffs, initiated proceedings at the Lombardy Regional Administrative Court for compliance with the provisions of the relevant administrative judge.

The outcomes of these proceedings, which could involve, at most, benefits for the Company, cannot be predicted at present.

***Start of proceedings for the evaluation of potential abuse in the wholesale electricity market***

In June, by means of resolution 342/2016/R/eel, the Authority launched an investigation relating to alleged abusive behaviour in the wholesale electricity market. The investigation, launched in accordance with the European REMIT Regulation, concerns two separate cases: the first refers to the alleged adoption of consumption unit scheduling strategies and plants powered by non-programmable renewable sources not consistent with the standards established by the Authority in previous measures; the second regards production units authorised to submit offers on the Dispatching Services Market that would not have offered their capacity on energy markets, encouraging Terna to establish units for balancing the system and subsequently increasing its costs. The investigation aims to evaluate the adoption of prescriptive or asymmetric adjustment measures in order to promote competition on the wholesale market.

By means of subsequent resolution (459/2016/E/eel), the Authority extended the scope of the investigation, initiating additional proceedings. Tirreno Power was notified of inclusion in the investigation as regards both situations, and the Company provided the information requested by the Authority regarding its offer conduct.

In relation to the investigation, by means of subsequent measures, the Authority ordered:

- by means of resolution 477/2016/E/eel, the transmission to the Antitrust Authority of the documentation regarding the offer conduct of some operators involved (which do not include Tirreno Power) in the investigation in consideration of potential violations of the competition protection regulations;
- by means of resolution 575/2016/R/eel, the methods of automatic retrocession to end customers of amounts eventually recovered following the proceedings launched;
- by means of resolution 609/2016/E/eel, some asymmetric adjustment measures for plants subject to proceedings (which do not include those of Tirreno Power available) declared to be essential for the safety of the electricity system;
- by means of resolution 813/2016/E/eel, it ordered the first dismissals of the individual proceedings launched against some operators.



As regards Tirreno Power, the outcome of the proceedings has still not been notified in relation to both strands of the investigation and, at the current state of play, any negative consequences for the Company are considered unlikely.

***Expected reimbursements for non-allocation of ETS allowances***

As is well-known, Tirreno Power's Napoli Levante plant was, in due course, excluded from the allocation of free emission allowances envisaged in the second period of the Emission Trading System (ETS 2008-12) due to the depletion of the reserves put at the disposal of production plants that entered into service during the period (so-called new entrants reserve). For such systems, the Legislator had made provision for a mechanism for the purchase with consideration of allowances reimbursed through a procedure established in recent years and based on the collections obtained by the GSE from the allocation of the allowances at auction in the next period (2013-2020). In that contest, Tirreno Power is the holder of a credit of around Euro 28 million which, in relation to the terms of the Restructuring Agreement, was transferred to Intesa Sanpaolo S.p.A. as Issuer Bank, as security for the obligations deriving from the new endorsement loan agreement. The credit will be paid on the basis of the resources that are made available for reimbursements by auctions for the allocation of allowances of the new period started in 2013.

In 2016, Intesa Sanpaolo S.p.A., as assignee, collected the first instalment of the credit for an amount of around Euro 10.5 million (principal and interest), recorded under non-current financial assets.

***The dispute over the recalculation of the capacity payment for the years 2010/2011***

Following a complex administrative dispute, by means of Resolution 400/2014/R/eel, the Authority ordered the recalculation the fees to cover the second component for the remuneration of the production capacity for the years 2010 and 2011. In particular, the measure levied costly reimbursements on some operators, including Tirreno Power, which was required to repay a total of around Euro 5.5 million in 2014. Given the seriousness of the situation brought about by the resolution and in consideration of the lack of legitimacy of the measure, Tirreno Power joined other operators penalised by the latter in filing an appeal against the aforementioned resolution before the Lombardy Regional Administrative Court. In June 2016, a hearing was held which led to a ruling which cancelled the measure contested and established the need to renew the procedure for determining the fee.

The Authority filed an appeal against the first instance ruling (Council Chamber set for next May 11).

The outcomes of these proceedings, which could involve, at most, benefits for the Company, cannot be predicted at present.

***The regulation of imbalances for the period 2012-2014***



The regulation of the actual imbalances in the electricity market for the period 2012-2014 was the subject of a long dispute which ended with the second instance cancellation of a number of the Authority's resolutions. In respect of this cancellation, Terna has performed recalculations of imbalances by using the criteria defined by the Authority before the issuing of the acts found to be unlawful. This generated, for Tirreno Power, the billing of negative amounts in relation to the periods covered by the recalculation of approximately Euro 4.5 million in 2015.

Tirreno Power challenged, before the Lombardy Regional Administrative Court, the communication in which Terna acknowledged its desire to perform the recalculations.

Simultaneously, the Authority initiated proceedings for the adoption of a new regulation for the period in which the cancellation judgments determined legislative uncertainty. In that context, following a consultation process, the Regulator issued a new resolution, DCO 333/2016/R/eel, which takes account of the confidence generated in operators by the regulation in force at the time of its production planning, although subsequently cancelled. According to the resolution, Terna performed recalculations for the adjustments of the considerations in October 2016. At the end of October, Tirreno Power collected roughly Euro 5.1 million. The aforementioned resolution is currently being challenged by some operators at the Lombardy Regional Administrative Court, meaning the Company incurs a risk of repayment, in respect of which an allocation was made to the provisions for risks and charges for the same amount.

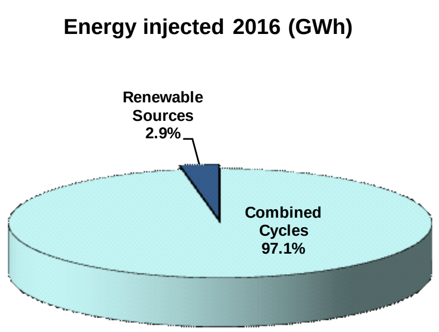
## Production scenario

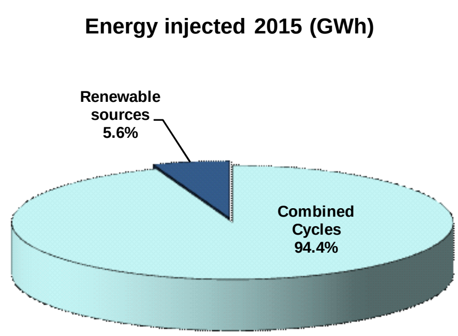
The **energy injected** in the period amounted to 5.54 TWh, up by 2.60 TWh compared to 2.94 TWh in 2015.

The following table provides details of the energy injected, with respect to the same period last year, broken down by unit and plant:

| Energy Injected (GWh) | 12.31.2016 | 12.31.2015 | Diff. |
|---|---|---|---|
| **By technology** | | | |
| **Combined Cycles** | **5.380** | **2.775** | ***2.605*** |
| - TV5 | 1.586 | 653 | *933* |
| - TV6 | 393 | 149 | *243* |
| - VL5 | 2.193 | 1.255 | *938* |
| - NA4 | 1.209 | 718 | *491* |
| **Traditional** | **-** | **-** | ***-*** |
| - TV4 | - | - | - |
| **Renewable Sources** | **162** | **165** | ***(4)*** |
| **Total** | **5.541** | **2.940** | ***2.601*** |
| | | | - |
| **By plant** | | | |
| Vado Ligure | 2.193 | 1.255 | *938* |
| Torrevaldaliga | 1.978 | 802 | *1.176* |
| Naples | 1.209 | 718 | *491* |
| Genoa | 162 | 165 | *(4)* |
| **Total** | **5.541** | **2.940** | ***2.601*** |

*(source: Company database)*



In particular, the energy injected in the last quarter of 2016 stood at 1,932 GWh, roughly 35% of the entire year, while in the same period energy sales on the Power Exchange came to 2,489 GWh, more than 36% of 2016. This increase is due primarily to the rise in the average PUN in the period, up from an average of 38.34 (€/MWh) in the January-September period, to an average of 55.95 (€/MWh) in the October-December period, with spikes of 80.00 (€/MWh) in the period, a level altogether anomalous with respect to the seasonal averages of the last few years. That is mainly due to the fact that France had to temporarily shut down more than one-third of its nuclear plants, partly for routine maintenance and partly for extraordinary controls: 21 reactors out of 58.

All combined cycle units benefitted, with respect to 2015, from an increase, of the Clean Spark Spread, which made them more competitive in all time brackets, with an increase in MGP (day-ahead market) sales deriving from a more favourable market scenario.

Some regional situations verified in the network (especially in the Torrevaldaliga and Napoli Levante areas) consequently made it possible to operate in the MSD (Dispatching Services Market).

In 2016, the Vado Ligure plant injected 2,193 GWh of energy into the network, 938 GWh more than in 2015, despite the scheduled shutdown of the unit from March 13 until May 24.

The Torrevaldaliga Sud plant recorded an increase in production volumes of 1,176 GWh compared to the previous year; the TV5 unit in particular contributed to this result, registering higher production volumes (+933 GWh compared to 2015), taking advantage of greater market margins.

The Napoli Levante plant recorded production of 1,209 GWh in 2016 (+491 GWh compared to 2015), with high production volumes in the Dispatching Services Market, especially during nighttime hours and at weekends.



The production from renewable sources in 2016 amounted to 162 GWh, marking a decrease of around 4 GWh compared to the same period in 2015, due to the low rainfall recorded throughout 2016, especially in January, April, May, November and December.

**Plant maintenance**

The Vado Ligure plant underwent scheduled maintenance (Major Inspection) to the VL5 unit in April/May 2016; in particular, general inspections were conducted on the two gas turbine units and the three generators, and the low pressure body of the steam turbine was inspected.

As regards the Torrevaldaliga Sud plant, the TV6 unit was subject to scheduled maintenance which started on October 1, 2016, returning to operation at the start of March 2017.

The Napoli Levante site was subject, from June 29, to a planned shutdown for ordinary maintenance targeted at cleaning of the condensing unit and the restoration of the gas turbine discharge cone, completed on July 15. In addition, the Naples unit saw the continuation, until December 2, of the shutdown commenced on November 27 for other gas turbine accelerations (humming), for which fine-tuning with the supplier Ansaldo was necessary.

The hydroelectric sector recorded extraordinary maintenance work for the channels of the Chiesuola and Argentina plants (refurbishment of damaged sections and of waterproofing systems present in the reservoir) and of unit 2 of the Cairo plant (general overhaul of turbine and alternator).

Lastly, the functioning of the bottom drainage system of the Piana Crixia dam was restored.

***Damage to plants***

With reference to the Vado Ligure plant, no significant faults or accidents were recorded.

As regards the Torrevaldaliga Sud plant, the by-pass MP pipe of the GVRC on the TV6 unit was broken in January 2016, due to a water hammer during start-up. The unit became available again after 7 days, following repairs.

In January 2016, a fault was identified on the switch of the TV (steam turbine) machine at the Napoli Levante unit; the replacement of the damaged parts of the switch took about 12 days.

As for the hydroelectric sector, accidents were recorded at the Tigliolo site (damage to the transformer for atmosphere fulmination).

In addition, as a result of a flood which occurred on November 24, 2016, major damage was recorded by the Millesimo (flooding of room housing the electrical control panels of the dam and of the central turbine station, destruction of handrails, balconies, stairs, various structural works and damages from blockages caused by mud in the adduction channels) and Cairo (destruction of handrails, balconies, stairs, various structural works and adduction valve).

The Cairo plant returned to full operation on February 25, 2017; whereas given the restoration of the Millesimo plant will take longer, it is expected to be relaunched by June 2017.

## Environment and Safety Policy

### Introduction



In 2016, the Company's main objective continued to be to reach high levels of environmental protection and worker safety, both internally and with respect to third party companies.

The Environmental and Safety Policy is inserted in the Environmental Statements of the sites on which EMAS registered thermoelectric plants are built and constitute one of the means by which the knowledge of corporate conduct in the environmental field is widespread.

### The organisation

In order to effectively achieve the maximum levels of environmental protection and safety, the Company's organisational model provides special powers of attorney with which the General Manager assigns the Heads of the Production units full powers for the fulfilment of the duties related to the protection of the environment, of workplace health safety and of plant safety.

### The tools

The main tools used for the implementation of the Company's environmental policy are:

1. *The environmental management systems*

The Company has chosen to adopt the EMAS registration (Eco Management and Audit Scheme) for all of the thermoelectric plant sites.

The EMAS registration is the most prestigious environmental certification in Europe. During 2016 such records were maintained and / or renewed for Naples and Torrevaldaliga sites.

By contrast, for Vado Ligure, certification UNI EN ISO 14001 was renewed for the combined cycle unit.

2. *Training and information*

Environmental training and information are used to improve employees' skills and to increase their professionalism.

In 2016 they continued activities aimed at staff training on environmental issues, taking into account the evolution of applicable regulations.

The focus on environmental training has made it possible to increase the number of staff, operating in both the main structure at the production sites, in possession of the title of Qualified Environmental Auditor.

3. *Environmental reporting*

The environment management systems of certified sites provide periodic reports on data and environmental performances that are subject to management review for the analysis of the comments and non-conformities, in order to identify and implement the necessary corrective actions.

The main environmental figure for the year 2016 refers to atmospheric emissions of $CO_2$, amounting to 2.2 million tons.



**The financial resources dedicated to the environment**

In 2016, the Company carried out investments directly related to the environmental field amounting to Euro 604 thousand, primarily carried out at the Vado Ligure plant and connected to the gasification of the auxiliary boiler and the rainwater recovery system.

In addition, the current costs incurred in the period totalled Euro 759 thousand, broken down between the various plants and the central facilities, according to the following table:

| Environmental expenses | (Euro) |
|---|---|
| Renewable Sources Sector | 36,576 |
| Naples plant | 54,164 |
| Torrevaldaliga plant | 141,108 |
| Vado Ligure plant | 451,685 |
| Central Departments | 75,496 |
| **Total** | **759,029** |

These expenses refer primarily to analysis and waste treatment activities (Euro 214 thousand) and the maintenance of the systems for the monitoring of injections and emissions (Euro 163 thousand). The remaining expenses concern monitoring activities for compliance with AIA decrees and activities involved in maintaining EMAS certifications.

**The main environmental events**

The main environmental events by plant were:

***Vado Ligure***

- decision to abandon production of electricity from coal by the BoD, communicated to the MATTM (Ministry of Environment and Land and Sea Protection) by means of prot. no. 4226 of November 4, 2016;
- obtainment of an opinion from the Ministry of Economic Development for definitively putting coal-powered units VL3 and VL4 out of service (prot. no. 36403 of December 23, 2016);
- performance by Arpal of an inspection between November 11 and 12, who took samples and conducted surveys, considered useful by ISPRA for the purposes of the planned ordinary inspection regarding AIA decree no. 323 of 12/31/2014.

***Torrevaldaliga Sud***

- positive conclusion of the AIA review procedure, in relation to the a new osmosis system for the production of demineralised water (MATTM memorandum 27871 of 11/16/2016);
- validation of the environmental statement in 2015 by the Institute of Certiquality Certification and Eco Committee and Ecoaudit.
- performance by ARPA Lazio, from October 20 to 25, of the ordinary inspection, in implementation of the authorisation decree DVA - DEC no. 140 of 05/04/2011 which did not reveal significant non-compliance;
- approval of the Plan for the Monitoring of greenhouse gas emissions by the ETS Committee.



***Napoli Levante***

- renewal of EMAS registration, with expiry on 05/28/2017;
- validation of the 2015 environmental declaration by the Certification Body Certiquality.
- performance by the Inspection Group, from November 15 to 17 and December 16 to 17, of the ordinary inspection in implementation of the authorisation decree DEC MIN no. 320 of 11/12/2013 which did not reveal significant non-compliance;
- approval of the Plan for the Monitoring of greenhouse gas emissions by the ETS Committee.

***Ligure hub - hydroelectric***

- obtainment by the MATTM, of the exclusion from the Environmental Impact Assessment for the performance of adjustment works in respect of the 1000-year flood of the Zolezzi dam, by means of management decision no. DVA-DEC-2016-0000450 of 12/15/2016.

**Safety**

The Company pays special attention to safety-related problems.
It continued, in the year 2016, the activities aimed at maintaining the OHSAS 18001 certifications for the 4 Tirreno Power Production Units involved.

The OHSAS 18001 certification (British Standard 18001 Occupational Health and Safety Assessment Series) defines the requirements of the Worker Health and Safety Management System. These requirements are verified by a qualified body, which, in the event of a positive outcome, issues the relevant Compliance Certificate:

- Torrevaldaliga Plant Production Unit: renewal audit carried out successfully on November 3 and 4, 2016 by the certification body Certiquality;
- Renewable Sources Sector Production Unit: renewal audit carried out successfully on March 21, 22, 23 and 24, 2016 by the certification body Certiquality;
- Rome Headquarters Production Unit: surveillance audit carried out successfully on November 14, 2016 by the certification body Certiquality;
- Vado Ligure Plant Production Unit: surveillance audit carried out successfully on July 20 and 21, 2016.

In April 2016, the SGS OHSAS 18001 certification process commenced for the 5th Tirreno Power Production Unit, the Napoli Levante Thermoelectric Plant. The first step in the certification (stage 1) was completed on December 13, 2016 by the certification body Certiquality. The process was completed on February 7, 2017 with obtainment of the certification.



Thanks to the achievement of this significant result, all Tirreno Power Production Sites are OHSAS 18001 certified.

Three accidents occurred in 2016:

- one at the Vado Ligure Production Unit on January 12, 2016, resulting in 36 working days lost.
- one at the Rome Headquarters on June 16, 2016, resulting in 26 working days lost;
- one at the Napoli Levante Plant Production Unit on October 7, 2016, resulting in 23 working days lost.

The year 2016 therefore closed with an average severity rate of 0.17 and with an average frequency rate of 6.11.

By contrast, there was one accident involving staff employed by external firms in 2016, albeit a minor one, resulting in 9 working days lost.

**Training, information and education**

In 2016, training was provided on safety in order to ensure the necessary continuity of training, as required by Legislative Decree 81/08 and subsequent amendments and additions and the new State-Regions Agreement of July 7, 2016.

**Risk Assessment Document (DVR)**

In 2016 the company continued to ensure the updates of the Risk Assessment Documents of the Company's Production Units, in accordance with the requirements of the OHSAS standard (and also Seveso for the Vado Ligure Plant Production Unit) and in compliance with the adjustment of new regulatory requirements introduced by Legislative Decree 81/08.

**The financial resources dedicated to safety**

The company completed investments in safety in 2016 totalling Euro 901,414, mainly relating to the activities carried out at the Bevera, Cairo and San Michele hydroelectric plants.

In addition, the current costs incurred in the period totalled Euro 1,186 thousand, broken down between the various plants and the central facilities, according to the following table:

| Safety costs | (Euro) |
|---|---|
| Renewable Sources Sector | 296,094 |
| Naples plant | 171,799 |
| Torrevaldaliga plant | 253,514 |
| Vado Ligure plant | 427,344 |
| Central Departments | 36,801 |
| **Total** | **1,185,552** |



These expenses refer primarily to those for full compliance with the regulations governing safety and the protection of workers' health (testing, checks and adaptation of equipment and work vehicles, personal protective equipment, etc.) amounting to Euro 493 thousand, expenses relating to fire prevention regulations totalling Euro 377 thousand and expenses of Euro 167 thousand for medical/sanitary services.

## Investment plan

During 2016, the Company reported investments totalling Euro 40,833 thousand, of which Euro 40,552 relating to tangible fixed assets and Euro 281 thousand to intangible fixed assets.

With regard to intangible fixed assets, investments are attributable to new licenses and the development of applications.

As for tangible fixed assets, it is noted that in the Napoli Levante plant, a total of Euro 8,885 thousand was invested, mainly dedicated to the early shutdown for the Major Inspection, the LTSA maintenance contract and completion works on the road network at the entrance to the plant.

A total of Euro 21,980 thousand was invested for the Vado Ligure Plant, mainly for the Major Inspection of the gas turbines and the steam turbine of the VL5 combined cycle unit. In addition, the following main initiatives were recorded: start of extraordinary maintenance on the pier (which is also expected to continue into 2017 and 2018), the repair to the 300 MVA transformer and the launch of site segmentation works, with the protection of Sala Manovra 2 and the Coal storage facility control room, which will continue throughout 2017.

As for the Torrevaldaliga Sud site, a total of Euro 7,876 thousand was invested, mainly attributable to the shutdown for the Major Inspections of the combined cycle TV6 unit and advance payment made for the order for the supply of the new reverse osmosis system (supply and assembly in 2017).

By contrast, as regards hydroelectric power plants, a total of Euro 1,702 thousand was invested, mainly relating to the refurbishment of the channels of the Chiesuola and Argentina plants, strengthening of the Zolezzi dam, as well as various safety initiatives.



## Human resources and organisation

### Legislation and Personnel Administration

The year 2016 saw the continued administrative management of two defensive solidarity contracts signed at the end of 2014, expiring respectively on October 31, 2016 for the management staff and personnel of the Naples and Civitavecchia plants, and on November 9, 2016 for the Vado Ligure Plant personnel.

As a result of the applications submitted in the last few months of 2015 to the Ministry of Labour, requesting authorisations relating to the second period of solidarity set forth in the trade union agreements with a term of 12 months (November 1, 2015- October 31, 2016 and November 10, 2015 - November 9, 2016), the two necessary ministerial decrees were issued in February 2016.

As a result of these provisions, all the necessary authorisations were issued in the last quarter of the year by INPS (national social security institute), so the company was able to adjust the amounts paid in advance to workers on behalf of the institution.

The residual credit as at December 31, 2016 amounted to around Euro 1.2 million, which will be recovered in 2017.

It should be stressed that the use of the solidarity facility made it possible to record a saving of around Euro 2.4 million, equal to 10% of personnel costs incurred in the year.

The complex and well-structured redundancy management plan drawn up by the company after the expiry of the solidarity contracts, which formed the object of the agreement signed with the trade union organisations on December 2, 2016, details of which will be provided in the next section “Organisational development and industrial relations”, determined the need to set aside an allocation in the 2016 financial statements for costs to be incurred in respect of the different instruments and initiatives set forth in the agreement, for a total value of Euro 20,229 thousand.

It should be noted that, in December, the company submitted an application to the Ministry of Labour and Social Policies for use of the Cassa Integrazione Guadagni Straordinaria (extraordinary wage guarantee fund) for company crisis for personnel at the Naples, Rome and Civitavecchia sites, as well as an application for use of the CIGS in accordance with art. 44, paragraph 11 bis of Legislative Decree 148/2015 (companies operating in areas of complex industrial crisis) for personnel at the Vado Ligure site, for a maximum of 155 suspended workers, for which the Decree was obtained on March 1, 2017.

The programme of suspensions started on December 19, 2016 and will end on December 18, 2017.

The effects of the labour cost saving guaranteed by use of the social shock absorber, equal to around 70% of the average unit cost, will become apparent in 2017.

As part of the overall framework of initiatives targeted at correcting the company’s economic position, the issue was also defined relating to the programme of incentives (bonuses and meritocracy) envisaged for 2013, to be disbursed in 2014 based on the attainment of set targets.

An agreement was signed in April with social partners which makes provision for the cancellation of the company performance-related pay pertaining to 2013, both the part connected with company profitability and that dependent on specific productivity targets.



The decision not to apply performance-related pay relating to 2013 therefore determined the recognition of a contingent asset of roughly Euro 1 million in the first half.

For the aforementioned reasons, the trade union agreement on company performance-related pay was not renewed for 2016, as set forth in the national contractual legislation for the industry, putting said commitment back to 2017.

To this end, it was deemed appropriate to allocate an amount of Euro 0.9 million in 2016, estimated on the basis of the proposed agreement that the company prepared for the meeting with the trade union organisations.

Lastly, it should be noted that an outline agreement for renewal of the CCNL (national collective labour agreement) was signed on January 25, 2017, which expired on December 31, 2015.

The agreement reached with the trade union organisations does not envisage expenses payable by the company for 2016 given that the increase in the contractual minimum salaries will take effect in 2017, and no disbursement to cover the period of contractual vacancy has been agreed.

**Organisational Development and Industrial Relations**

In 2016, the Company continued to implement initiatives targeted at increasing the efficiency of processes and optimising the management of resources.

The staff continued to operate in line with the registered reductions specified in the solidarity contracts signed with the trade unions in 2014.

In March, the company adopted an organisational structure suited to meeting the challenges of the market and consistent with its operational dimension.

A total of 6 departments report to the General Manager: Legal Affairs, Administration, Finance and Control, Personnel, External Relations, Energy Management and Production, Engineering, Purchasing and Information & Communication Technology.

The restructuring helped the company achieve the objective of creating a flat organisation, with a shortening of decision-making levers, with the accurate identification of the areas of responsibility assigned to the dedicated departments that enjoy greater autonomy.

On the trade union front, workers became increasingly worried during the first half about the uncertainty over the relaunch of coal plants, which resulted in conflicts, first concentrated in the Vado Ligure site, then extended to all plants.



On June 23, the company officially informed national and regional trade unions and the RSU (unitary workplace union structure) of the Board of Directors' decision to discontinue the production of electricity from coal and the associated reduction in personnel.

September saw the start of the redundancy scheme, to bring the company down to 196 staff, with the associated compulsory exit of 186 staff members.

The launch of the redundancy scheme brought the case of Tirreno Power to the attention of the institutions, with some meetings with the Ministry of Economic Development, chaired by the Deputy Minister, who strongly encouraged the company to revoke the scheme.

On September 20, at the end of a ministerial meeting, the Company revoked the redundancy scheme, accepting the invitation of the Deputy Minister and setting November 30 as the last day to reach an agreement with the trade unions, an agreement that should have resulted in the company headcount declared in the redundancy scheme.

In September 2016, the Savona area was recognised as an "complex crisis area" and a correction to the Jobs Act recognised the possibility of including this industrial site in the request for an additional year of the cassa integrazione straordinaria - extraordinary wage guarantee fund (before the issuing of the corrective measure, this assumption was not possible due to the discontinuation of production from coal).

In light of this new scenario connected with social shock absorbers, the company and the trade unions commenced a series of meetings which led to a well-structured and highly innovative redundancy management agreement, both in terms of the initiatives contained therein and the definition of a process which, at the end of 2017, will see the forced layoff of staff over and above 196 units, the planned company headcount.

Therefore, an agreement was signed on December 2 for the management of redundancies (186 units) which makes provision not only for the use of social shock absorbers at all company sites (CIGS - extraordinary wage guarantee fund - for company crisis in Rome, Naples and Civitavecchia - extraordinary CIGS deriving from the correction to the Jobs Act for Vado Ligure), but for financial incentives both for voluntary exits of workers who will meet the pension requirements by 2024, and financial incentives for employees who declare their intention to leave the company voluntarily. For all other individuals, the company will implement a series of initiatives targeted at repositioning, also by availing itself of specialised outplacement companies.

In fact, from the launch of the salary integration instruments and until March 20, 2017, for all workers who accepted the voluntary redundancy arrangement and did not oppose the layoff, the Company will recognise a financial incentive based on their specific contribution situation.

Workers who have not subscribed voluntarily to the redundancy incentive plan as at the aforementioned date of March 20, 2017, will be involved in a series of initiatives known as "Process of enhancement of professional skills and employment", which offers, in short, the following possibilities:

1. self-employment;
2. training and outplacement (with the choice of two specialised companies);
3. reindustrialisation with potential repositioning at third party companies that will set up on the Vado Ligure site;
4. shareholder job posting;
5. industry solidarity (set out in the new CCLN);
6. other proposals by Tirreno Power.



The total estimated expense payable by the Company deriving from the application of the aforementioned agreement was allocated to provisions for risks and charges in these financial statements.

Therefore, Ministerial agreements were signed in December for the application of the Cassa Integrazione (Wage Guarantee Fund) and, in the same month, worker suspensions commenced.

The year 2016 saw the performance of planned training activities on safety and/or the retraining of technical personnel, especially in the first half of the year. The second half of the year was dedicated, in particular, to the preparation of a new training plan for 2017 which took account of the future structure of the Company. The managerial development plan targeted at executives and organisational managers was also implemented at the Vado Ligure and Naples sites.

All costs incurred for training activities described were financed by interprofessional funds (Fondirigenti and Fondimpresa).

**Information & Communication Technology**

In the application domain, 2016 saw the adjustment of Tirreno Power's data banks and the HR management system to acknowledge the changes dictated by the new organisational structure.

Also, in 2016, in accordance with company guidelines, which indicated the need to initiate a process of dematerialisation, a project process was launched and a contract formalised for the purchase of licences and development of the application that will be used for the digitalisation of company processes.

The application called "Plant technical data management" was released for the Energy Management Department in 2016. The goal of the project is the replacement of the current custom tool for the supervision and management of the processes in place in the Energy Management area, related to Real Time (granularity of data per minute), switching to a standard tool already used by several market operators.

From an infrastructural point of view, the project for the modernisation of perimeter security devices was completed. The initiative, which not only ensured more modern and efficient devices, led to an annual saving of around 55% compared to the provisions of the agreement of the 2014-2016 three-year period.

As regards telephony, a contract was signed in 2016 for the new reloadable plan for businesses. The main change introduced by the plan is the disposal of the BlackBerry platform and use of Android terminals.

**Obligations regarding Legislative Decree no. 231/01**



By means of Board of Directors resolution dated April 24, 2015, the new Chairman of the Supervisory Board was appointed, following the resignation of the previous Chairman in its meeting of March 25, 2015. At present, the Supervisory Board is composed of an internal member (responsible for Company's legal department) and two external members.

The MOG (organisation and management model) was updated in 2016 with the insertion of a special section relating to eco-crimes, the offence of self-laundering and the revision of the information flows required by the Model in order to adjust them into line with the new organisational macro-structure. The latter activity, together with the revision of the Company's Code of Ethics was approved by the Board of Directors at the meeting on June 22, 2016. This led to a temporary deferment of the half-yearly flows. The analysis of the flows of the second half of 2016 will actually be concluded in February 2017.

In any case, based on the flows relating to the first half of 2016, the Supervisory Board reported positively to the Board of Directors on the effectiveness of the Model for the prevention of offences.

**Operating performance during the year**

The chart below shows, in line with ESMA Recommendation on Guidelines on Alternative Performance Measures, the criteria used for the construction of the reclassified statements that contain alternative performance indicators with respect to those obtained directly from the financial statements:

***Gross operating profit***: an operating performance indicator, calculated as “Operating income” plus “Depreciation, amortisation and write-downs” and “Provisions”.

***EBITDA***: an operating performance indicator, calculated as “Operating income” plus “Depreciation/amortisation and write-downs”

***Net fixed assets***: calculated as the difference between the “Non-current assets” and “Non-current liabilities” with the exception of:

“Payables for loans”;

“Provisions for risks and charges”;

“Post-employment and other employee benefits”;

“Liabilities for deferred taxes”.

***Net working capital***: defined as the difference between “Current assets” and “Current liabilities” with the exception of:

“Payables for loans”;

“Cash and cash equivalents”;

“Provisions for risks and charges”;

the bank current account advances and bank current account debt exposures included in “Other current financial liabilities”.

***Net capital employed***: calculated as the algebraic sum of “Net current assets”, “Net working capital” and provisions.

***Net financial debt***: defined as the sum of “Payables for loans”, bank c/a advances and debt exposures on bank current accounts included in “Other current liabilities”, net of “Cash and cash equivalents” not previously considered in the definition of other balance sheet indicators.

***Return on Investment (ROI)***: defined as the ratio between operating profit and net average capital employed (opening and closing).

***Return on Sales (ROS)***: defined as the ratio of operating profit to total revenues.

***Equity yield***: defined as the ratio between the net profit and the share capital plus the share premium reserve.

***Unit revenue from energy sales (€/MWh)***: calculated as the ratio between revenues from energy sales for the period and energy sales in the period.

***Incidence of financial expenses on total revenues***: defined as the percentage ratio between the financial expenses in the period and the total revenue for the period.

### Reclassified Income Statement

The values of the reclassified income statement are reported in Euros, without decimals. For a better disclosure, comments on the individual items are expressed in thousands of Euro.

| (Euro) | 12.31.2016 | 12.31.2015 | difference |
|---|---|---|---|
| Revenues | 738,479,690 | 425,417,168 | 313,062,522 |
| Other revenues | 10,261,641 | 14,690,950 | (4,429,309) |
| **Total revenues** | **748,741,331** | **440,108,118** | **308,633,213** |
| Own work capitalised | 286,282 | 230,812 | 55,469 |
| Consumption of raw materials | (627,580,581) | (355,999,650) | (271,580,931) |
| Personnel costs | (23,750,309) | (27,019,090) | 3,268,780 |
| Service costs | (23,156,521) | (29,099,955) | 5,943,434 |
| Other costs | (19,838,318) | (28,000,270) | 8,161,952 |
| **Total costs** | **(694,039,447)** | **(439,888,152)** | **(254,151,295)** |
| **Gross operating profit** | **54,701,884** | **219,966** | **54,481,918** |
| Provisions | (32,904,393) | (9,004,432) | (23,899,961) |
| **EBITDA** | **21,797,491** | **(8,784,466)** | **30,581,957** |
| Amortisation, depreciation and write-downs | (59,976,249) | (57,680,191) | (2,296,058) |
| **EBIT** | **(38,178,758)** | **(66,464,658)** | **28,285,899** |
| Financial expenses | (20,937,621) | (12,013,161) | (8,924,460) |
| Financial income | 426,641 | 87,001,360 | (86,574,719) |
| **Pre-tax profit** | **(58,689,739)** | **8,523,542** | **(67,213,281)** |
| Taxes | - | 5,366,833 | (5,366,833) |
| **Net income for the period** | **(58,689,739)** | **13,890,376** | **(72,580,114)** |



**Electricity** sold in 2016 totaled 14,317 GWh, an increase of 7,931 GWh compared to the previous year.

Energy sold in the open market amounted to 7,390 GWh (of which 4,849 GWh contractualised with Edison to cover gas purchases), marking an increase of 4,302 GWh, while energy sold on the Power Exchange recorded an increase of 3,629 GWh.

The energy balance is presented below with a reconciliation of the quantity of energy purchased and unbalanced that makes it possible to reconcile the volumes sold with the actual energy injected to the grid.

| Energy injected, purchased and sold (GWh) | 12.31.2016 | 12.31.2015 | Diff. |
|---|---|---|---|
| **Energy injected** | **5,541** | **2,940** | ***2,601*** |
| **Energy purchased** | **8,812** | **3,498** | ***5,314*** |
| **Energy sold** | **14,317** | **6,386** | ***7,931*** |
| *-on free market* | 7,390 | *3,087* | *4,302* |
| *-on Power Exchange* | 6,927 | *3,299* | *3,629* |
| **Imbalances** | **(37)** | **(52)** | ***15*** |

**Revenues** amounted to Euro 738,480 thousand, an increase of Euro 313,063 thousand compared to the previous year (+73.6%).

| Revenues - (thousands of Euro) | 12.31.2016 | 12.31.2015 | Diff. |
|---|---|---|---|
| Free Market | 333,433 | 161,216 | *172,217* |
| Power Exchange | 404,906 | 263,120 | *141,786* |
| Other | 140 | 1,081 | *(941)* |
| **TOTAL** | **738,480** | **425,417** | ***313,063*** |



The increase relates to the higher sales volumes attributable to the trading in the Dispatching Services Market, thanks to the excellent performances of the NA4 and TV5 units and greater sales volumes in the day-ahead market as a result of the higher PUN level recorded in the last few months of the year, coinciding with the shutdowns of a number of French nuclear power plants for maintenance.

The item "Other" refers, as at December 31, 2016, mainly to the sale to third parties of warehouse materials, while in 2015 the item referred essentially to the insurance reimbursement for the damage suffered by the VL5 transformer.

**Other revenues** amounted to Euro 10,262 thousand, compared to Euro 14,691 thousand in 2015 and mainly refer to:

- for Euro 9,975 thousand due to the recognition of contingent assets attributable mainly to:
  - ✓ the adjustment by Terna of the recalculation of 2012-2014 imbalance charges of Euro 5,229 thousand;
  - ✓ adjustments to energy items of previous years for Euro 1,551 thousand, mainly due to the definition by Terna of the adjustment of the second component of the 2011 capacity payment (Euro 1,121 thousand);
  - ✓ reduction in liabilities to employees for bonuses and welfare for the years 2013 and 2015 (Euro 1,255 thousand);

  - ✓ transfer of provisions for risks for Euro 967 thousand, mainly due to the partial repayment of the Escrow security deposit of Tirreno Solar for Euro 300 thousand, adjustment of the redundancy provision for Euro 311 thousand plus the adjustment, amounting to Euro 290 thousand, of charges for legal expenses and ongoing disputes of the disputes and litigation provision;

- for Euro 113 thousand due to the recognition of other revenues and rental income.

In 2015, other revenues mainly referred to the sale of self-produced green certificates (Euro 5,459 thousand), to the recognition of contingent assets (Euro 8,604 thousand), attributable to the adjustment of energy items of previous years (Euro 4,758 thousand), to the recognition of the all-inclusive tariff for the Strinabecco hydroelectric plant from 2012 (Euro 2,369 thousand) and to the transfer of the provisions for risks (Euro 1,570 thousand).

The **cost of raw materials consumption** amounted to Euro 627,581 thousand, an increase of Euro 271,581 thousand compared to the previous year.

The cost of fuel consumed in the period amounted to Euro 231,093 thousand, up by Euro 69,580 thousand compared to the cost incurred in 2015. The volume effect of the greater production of CCGT (gas consumption rose by around by about 92.2%) was partially offset by the positive effect of the gas price (the PMP - weighted average price - fell by around 26.0%).

Charges related to the purchase of energy and operation of the power exchange amounted to Euro 393,619 thousand, an increase of Euro 201,750 thousand compared to 2015. A significant increase of Euro 170,093 thousand was recorded in purchases of energy on the power exchange, made to cover contractually agreed sales.



Purchases in the Dispatching Services Market (Euro 27,390 thousand) recorded a sizeable increase of Euro 24,477 thousand compared to the previous year, due to more trading on said market.

Energy purchases for imbalances stood at a negative Euro 4,867 thousand, up by Euro 7,142 thousand compared to 2015 (a positive Euro 2,275 thousand), due primarily to higher imbalance volumes (as a result of greater production) and higher unit imbalance costs which, due to a higher PUN value and prices on the DSM in particular, rose by over 160%.

**Personnel costs** amounted to Euro 23,750 thousand, a decrease of Euro 3,269 thousand compared to the figure recorded in 2015.

The decrease is mainly attributable to the recognition of performance-related pay under allocations (amounting to Euro 1,736 thousand), given that, as of today, a trade union agreement has still not been signed by the parties which defines the criteria and base value to be allocated to company bonuses for the year. The estimate was made for executives and middle managers on the basis of the MBOs assigned for 2016, and for employees and workers, using the amounts from the previous agreement signed (2015 bonuses).

The further drop of Euro 1,533 thousand compared to the previous year is mainly due to the decrease in other expenses other than personnel costs relating to the redundancy incentives contractualised in the year, as well as the drop in the average amounts compared to 2015, down from 387.4 in 2015 to 382.7 in 2016.

| Average amount | 12.31.2016 | 12.31.2015 | Diff. |
|---|---|---|---|
| Executives and Middle Managers | 43.5 | 46.0 | *(2.5)* |
| Employees | 226.1 | 223.4 | *2.6* |
| Workers | 113.2 | 117.9 | *(4.8)* |
| **TOTAL** | **382.7** | **387.4** | ***(4.6)*** |

The headcount at December 31, 2016 was 371 employees, compared to 386 employees at December 31, 2015.

**Service costs** for the period totalled Euro 23,157 thousand, a decrease of Euro 5,943 thousand compared to the previous year, essentially due to the decrease in technical and professional services linked to the 2015 debt restructuring process.

Additional savings have also been made possible by a thorough analysis of all the contracts in place, with subsequent initiatives involving new contracts and efficiency drives.



**Other costs** amounted to Euro 19,838 thousand, a decrease of Euro 8,162 thousand compared to the previous year.

In particular, higher expenses were recorded for emissions rights (Euro 3,435 thousand) as a result of higher emissions in the period (approx. 1,053 Kton). This increase was offset by lower expenses for Green Certificates of Euro 8,058 thousand, due to the end of the obligation in 2015.

In addition, IMU (single municipal tax) fell by Euro 3,607 compared to 2015, due to the recalculation of the tax based on the exclusion of the so-called "imbullonati" (machinery or plants fixed to the ground or incorporated in the construction but which, at the same time, can be dismantled and transferred from one site to another) from cadastral rents.

**EBITDA** was a positive Euro 54,702 thousand, compared to Euro 220 thousand realised in 2015.

**Provisions** amounted to Euro 32,904 thousand, mainly related to:

- the adjustment to the personnel redundancy provision (Euro 20,229 thousand) based on the estimated effects of the agreement signed on December 2, 2016 by the Company with the social parties, as detailed in full earlier in the section "Organisational Development and Industrial Relations";
- the adjustment to the provision for risks and charges (Euro 5,055 thousand) deriving from Terna's adjustment of the recalculation of 2012-2014 imbalance charges, already accounted for under other revenues, as highlighted in the relevant section. This

provision was made to cover the risk, deemed likely, of having to repay the amount to Terna as a result of a number of appeals filed by the other operators;

- for Euro 3,518 thousand for the adjustment of the estimate of the provision for expenses for the dismantling of the coal-powered units of the Vado Ligure plant, of which Euro 380 thousand connected with segmentation expenses;
- for Euro 1,736 thousand for the allocation to the provision for risks and charges as a result of the estimate of productivity incentives and bonuses connected with the company's 2016 results;
- for Euro 630 thousand for the adjustment to the provision for risks and charges deriving from the estimate relating to the IMU due for previous years, mainly attributable to the hydroelectric plants;
- for Euro 486 thousand for the adjustment to the market prices of fuel stocks;
- for Euro 397 thousand for the adjustment to the provision for risks and charges deriving from the damages suffered by the Millesimo hydroelectric plants as a result of the flood on November 24, 2016.

**EBITDA** amounted to a positive Euro 21,797 thousand compared with a negative Euro 8,784 thousand in the previous year. The improvement is primarily due to higher market margins and the notable savings in service and other costs, as outlined in the previous sections.

**Depreciation/amortisation and write-downs** (Euro 59,976 thousand) rose by Euro 2,296 thousand.



In particular, the increase in depreciation/amortisation is attributable to the capitalised maintenance of the VL5 unit.

In 2016, no write-downs were registered on tangible and intangible fixed assets, while plants connected to the coal-powered units were written down by Euro 578 thousand in the previous year.

The **operating result** was therefore negative by Euro 38,179 thousand, compared to a negative operating result recorded in the previous year amounting to Euro 66,465 thousand.

In 2016, **financial expenses** of Euro 20,938 thousand, an increase of Euro 8,924 thousand compared to the previous year.

The variation is primarily attributable to the higher average cost of debt relating to the credit lines set out in the debt Restructuring Agreement reached with banks last year (average interest rate of 2.63%), compared to those of 2015 relating to the previous loan agreement (stipulated in 2007, with an average interest rate of 0.45%).

**Financial income** amounted to Euro 427 thousand, compared to Euro 87,001 thousand in 2015.

The decrease of Euro 86,575 thousand is attributable mainly to the recognition, in the previous year, of income achieved in relation to the Debt Restructuring Agreement, i.e.:

- for Euro 80,387 thousand, at the lower value of fair value of the Participating Financial Instruments (PFI), determined on the basis of the report of an external expert as required in ADR, compared to the nominal value of these PFIs resulting from their issue resolved by the Extraordinary Shareholders' Meeting on December 16, 2015 and signed by the financial institutions, as set forth in the Debt Restructuring Agreement;
- for 55% of the Euro 5,430 thousand to the balance of the total value of financial liabilities for interest expense on hedging contracts of previous years, as set out in the Debt Restructuring Agreement.

The **Net loss** for the year amounted to Euro 58,690 thousand, compared to a net profit of Euro 13,890 thousand in the previous year.

During the year, no **taxes** pertaining to the year were recorded, given that the Company closed 2016 with a tax loss, whereas in the previous year, positive adjustments of Euro 5,367 thousand had been registered, essentially resulting from the adjustment of deferred taxes to take account of the effects of the IRES reduction from 27.5% to 24% from 2017 set forth in the Stability Law in 2016.

## Analysis of the capital structure

### Reclassified Balance Sheet

The values of the reclassified income statement are reported in Euros, without decimals.  For a better disclosure, comments on the individual items are expressed in thousands of Euro.

| (Euro) | 12.31.2016 | | 12.31.2015 | | difference |
|---|---|---|---|---|---|
| **Net fixed assets** | | | | | |
| Tangible and intangible assets | 755,470,182 | | 776,480,901 | | (21,010,720) |
| *- of which green certificates and CO2 rights* | *7,724,367* | | *9,853,130* | | *(2,128,764)* |
| Other net non-current assets/(liabilities) | 56,520,582 | | 69,013,441 | | (12,492,859) |
| **Total** | **811,990,763** | | **845,494,343** | | **(33,503,579)** |
| **Net working capital** | | | | | |
| Inventories | 21,292,759 | | 23,035,334 | | (1,742,575) |
| Trade receivables | 164,743,553 | | 105,703,205 | | 59,040,348 |
| Trade payables | (154,363,851) | | (85,252,708) | | (69,111,143) |
| Other net current assets/(liabilities) | 25,811,408 | | 61,962,329 | | (36,150,921) |
| **Total** | **57,483,869** | | **105,448,160** | | **(47,964,291)** |
| **Gross capital employed** | **869,474,633** | | **950,942,503** | | **(81,467,870)** |
| **Other provisions** | | | | | |
| Provisions for risks and charges | (101,797,548) | | (72,175,793) | | (29,621,755) |
| Post-employment benefits and other employee benefits | (17,136,349) | | (17,187,233) | | 50,884 |
| Deferred tax liabilities | (37,389,448) | | (38,588,472) | | 1,199,024 |
| **Total** | **(156,323,345)** | | **(127,951,499)** | | **(28,371,847)** |
| **Net capital employed** | **713,151,288** | **100%** | **822,991,004** | **100%** | **(109,839,717)** |
| **Shareholders' equity** | **198,724,823** | **28%** | **257,888,847** | **31%** | **(59,164,024)** |
| **Net financial debt** | **514,426,465** | **72%** | **565,102,158** | **69%** | **(50,675,693)** |

**Tangible and intangible fixed assets** recorded a decrease of Euro 21,011 thousand, due to the depreciation/amortisation for the period of Euro 59,976 thousand exceeding investments of Euro 40,833 thousand, net of $CO_2$ emissions rights mainly attributable to the Major Inspections of the VL5 combined cycle unit (Euro 20,017 thousand) and the early shutdown of the Napoli Levante power plant for the Major Inspections for a total of Euro 6,808 thousand, and the shutdown of the TV6 combined cycle unit (Euro 7,015 thousand).

The lower value of the emission rights and green certificate quotas acquired under consideration amounted to Euro 2,129 thousand.

**Other net non-current assets/(liabilities)** recorded a decrease of Euro 12,493 thousand, due to the decrease in VAT credits following the collection of the 2014 annual amount (Euro 13,500 thousand) during the year.

**Inventories** recorded a decrease of Euro 1,743 thousand compared to December 31, 2015, due to the adjustment of the market prices of stocks of combustible oil and coal, as well as the sale of around 77 kton of coal in the period.

As at December 31, 2016, there were no coal stocks at the Vado Ligure plant.

**Trade receivables** rose by Euro 59,040 thousand as a result, in particular, of higher bilateral revenues in December 2016 compared to the same period of 2015. An increase of Euro 15,065 thousand in receivables due from the GME was also recorded. The effect of the start of the weekly settlement with the GME from December 1, 2016, was more than offset by higher revenues from the sale of energy on the Power Exchange in the months of November and December 2016, compared to the same period of 2015.

The balance of **Trade payables** was Euro 69,111 thousand higher than at December 31, 2015.

This variation is attributable to:

- higher payables due to the GME for the purchase of energy on the Power Exchange (Euro 44,186 thousand). The effect of the start of the weekly settlement with the GME from December 1, 2016, was more than offset by higher revenues from the sale of energy on the Power Exchange in the months of November and December 2016, compared to the same period of 2015.
- higher payables for gas purchase (amounting to Euro 11,676 thousand);
- higher payables due to Terna for the purchase of energy (Euro 10,751 thousand), as a result of greater trading on the Dispatching Services Market from high to low.



**Other net current assets/(liabilities)** registered a decrease of Euro 36,151 thousand compared to December 31, 2015. This variation derives primarily from the decrease in VAT credits as a result of the collections in the year, i.e.:

- the annual 2013 VAT credit transferred to Banca Sistema of Euro 33,102 thousand,
- VAT credit for the 2nd and 3rd quarters of 2014 totalling Euro 14,712 thousand.

The **Provision for risks and charges** increased by Euro 29,622 thousand as a result of increases and uses, as described in detail in the notes.

The **Net capital employed** therefore amounted to Euro 713,151 thousand (Euro 822,991 thousand at December 31, 2015).

**Shareholders' equity** stood at a positive Euro 198,725 thousand, which changed when compared to December 31, 2015, due to the loss in the period, amounting to Euro 58,690 thousand, as well as the effect of the reduction in the reserve that includes the gains and losses from discounting as required by IAS 19 revised (Euro 474 thousand).

**Net financial debt** amounted to Euro 514,426 thousand, related primarily to the bank loan renegotiated in 2015 as a result of the debt restructuring agreement reached with the banks. For more details, please refer to the explanatory notes.

### Research and Development Activities

The Company did not carry out research and development in 2016 nor are there, as at December 31, 2016, deferred costs related to this type of activity.

### Own shares and shares of the parent

At the date of the financial statements, the Company does not own treasury shares or shares of parent companies, either direct or indirect.

### Relationships with subsidiaries, affiliates, parent companies and companies controlled by the latter

No significant transactions were carried out in 2016 with related parties. For more details, please refer to the notes to the financial statements.

### Financial instruments and risks

Please refer to the notes to the financial statements.

### Business outlook

After a 2016 characterised by an increase of approximately 0.9% in Italian GDP, in its last monthly bulletin, the Bank of Italy predicted GDP growth of around 0.9% also in the current year, and 1.1% in both 2018 and 2019.

The demand for electricity, which grew by 1.5% in 2015 compared to 2014, after three consecutive years of decline, fell again in 2016 when compared to the previous year (-2.1%).

In January 2017, electricity demand in Italy stood at 27.9 billion kWh, an increase of 4.9% compared to the same month in the previous year.

One year on from the closing of the process of restructuring of financial debt and simultaneous significant recapitalisation of the company, in a consistently competitive market context, management’s activities are targeted at protecting profitability through the constant focus on seizing all the opportunities in the electricity market, the maintenance of an adequate level of operational efficiency of the plants and meticulous reduction of business costs.

The above activities form part of ongoing actions to optimise the Company's cash flow.

The performance in the first two months of 2017 is better than the Company's forecasts.

### Significant events after the close of the period



On February 6, 2017, the Company arranged for the early repayment of Tranche A, amounting to Euro 3,017 thousand, in application of the so-called Cash Sweep mechanism.

In fact, the Restated Facilities Agreement requires, at the end of each half, the cash and cash equivalents exceeding Euro 50,000 thousand, to be used for the early repayment of the credit lines, starting with Tranche A and on a pro-rata basis on the expiries of the repayment plan, together with interest capitalised on the principal portion repaid early.

As at December 31, 2016, given cash and cash equivalents totalled Euro 53,017 thousand, the Company arranged for the early payment of excess cash totalling Euro 3,017 thousand. In particular, the principal portion of Tranche A was repaid (Euro 2,956 thousand), and the associated interest capitalised on the principal portion repaid (Euro 61 thousand).

## PROPOSALS OF THE BOARD OF DIRECTORS

Dear Shareholders,

We invite you to approve the financial statements at December 31, 2016, both as a whole and the individual items.

As illustrated, the financial statements of Tirreno Power S.p.A. reported a net loss of Euro 58,689,739.

In relation to the provisions of the Company's Articles of Association, and taking into account the available reserves present under shareholders' equity items, it is proposed that the net loss be covered in full as shown below:

1. Euro 13,195,857 through the use of the retained earnings reserve;
2. Euro 45,493,882 through the use of the available reserve for the coverage of losses.

Rome, March 22, 2017

*For the Board of Directors*

*(Chairman)*

*Naples Power Plant*

# Financial Statements Schedules

## Balance Sheet

| (Euro) | Note | 12.31.2016 | 12.31.2015 |
|---|---|---|---|
| **Assets** | | | |
| Property, plant and equipment | 1 | 746.879.007 | 765.458.203 |
| Intangible assets | 2 | 8.591.174 | 11.022.698 |
| Non-current financial assets | 3 | 17.586.093 | 7.542.690 |
| Deferred tax assets | 4 | 1.068.676 | 2.117.925 |
| Other non-current assets | 5 | 40.982.329 | 62.767.128 |
| **Total non-current assets** | | **815.107.280** | **848.908.646** |
| Inventories | | 21.292.759 | 23.035.334 |
| Trade receivables | | 164.743.553 | 105.703.205 |
| Other current assets | | 38.463.708 | 78.217.988 |
| Other current financial assets | | 2.562.044 | 2.749.772 |
| Cash and cash equivalents | | 53.017.128 | 68.638.179 |
| **Total current assets** | **6** | **280.079.192** | **278.344.479** |
| **Total assets** | | **1.095.186.472** | **1.127.253.123** |
| **Liabilities** | | | |
| Share capital | | 60.516.142 | 60.516.142 |
| Other reserves | | 183.702.563 | 183.482.329 |
| Accrued gains (losses) | | 13.195.857 | - |
| Profit (losses) for the period | | (58.689.739) | 13.890.376 |
| **Shareholders' equity** | **7** | **198.724.823** | **257.888.847** |
| Payables for loans | 8 | 559.337.123 | 602.660.439 |
| Provisions for risks and charges | 9 | 74.124.221 | 65.750.096 |
| Post-employment benefits and other er | 10 | 17.136.349 | 17.187.233 |
| Deferred tax liabilities | 11 | 37.389.448 | 38.588.472 |
| Other non-current liabilities | 12 | 3.116.516 | 3.414.302 |
| **Total non-current liabilities** | | **691.103.658** | **727.600.543** |
| Payables for loans | 8 | 8.083.316 | - |
| Provisions for risks and charges | 9 | 27.673.327 | 6.425.697 |
| Trade payables | | 154.363.851 | 85.252.708 |
| Other current liabilities | | 15.214.344 | 18.995.867 |
| Other short-term financial liabilities | | 23.154 | 31.089.462 |
| **Total current liabilities** | **13** | **205.357.991** | **141.763.734** |
| **Total shareholders' equity and liabilities** | | **1.095.186.472** | **1.127.253.123** |



## Income Statement

| (Euro) | Note | 12.31.2016 | 12.31.2015 |
|---|---|---|---|
| Revenues | 14 | 738.479.690 | 425.417.168 |
| Other revenues | 15 | 10.261.641 | 14.690.950 |
| **Total revenues** | | **748.741.331** | **440.108.118** |
| Own work capitalised | 16 | 286.282 | 230.812 |
| Consumption of raw materials | 17 | (627.580.581) | (355.999.650) |
| Personnel costs | 18 | (23.750.309) | (27.019.090) |
| Service costs | 19 | (23.156.521) | (29.099.955) |
| Other operating costs | 20 | (52.742.711) | (37.004.702) |
| Amortisation, depreciation and write-downs | 21 | (59.976.249) | (57.680.191) |
| **EBIT** | | **(38.178.758)** | **(66.464.658)** |
| Financial expenses | 22 | (20.937.621) | (12.013.161) |
| Financial income | 23 | 426.641 | 87.001.360 |
| **Pre-tax profit** | | **(58.689.739)** | **8.523.542** |
| Taxes | 24 | - | 5.366.833 |
| **Net income** | | **(58.689.739)** | **13.890.376** |
| **Earnings per share - basic and diluted** | **25** | **-0,97** | **0,23** |



## Statement of Comprehensive Income / (loss)

| (Euro) | Note | 2016 | 2015 |
|---|---|---|---|
| **Net income for the period** | | **(58.689.739)** | **13.890.376** |
| **Other components of comprehensive income:** | | | |
| Change in fair value IAS 19 - Post-employment and other benefits | 10 | (474.285) | 17.355 |
| **Total other components of comprehensive income** | | **(474.285)** | **17.355** |
| **Total comprehensive income** | | **(59.164.024)** | **13.907.731** |

## Cash flow statement of cash and cash equivalents

| (Euro) | Note Ref. | 12.31.2016 | 12.31.2015 |
|---|---|---|---|
| **OPERATING ACTIVITIES** | | | |
| Statutory result | | (58,689,739) | 13,890,376 |
| Amortisation, depreciation and write-downs | 21 | 59,976,249 | 57,680,191 |
| Net provisions for deferred taxes and other provisions | | 28,371,847 | (11,674,901) |
| (Purchase) repayment of GC and CO2 quotas | | 2,128,764 | 9,668,187 |
| Increase (decrease) in CF hedge reserve and IAS 19 | | (474,285) | 862,420 |
| Other non-monetary changes | | (260,865) | (19,083,045) |
| Change in other non-current assets and liabilities | | 12,492,859 | 56,818,294 |
| Change in other current assets and liabilities | | 47,964,291 | (144,697,955) |
| **Cash flow from operating activities** | | **91,509,120** | **(36,536,434)** |
| of which: | | | |
| *- Interest income collected* | | *-* | *-* |
| *- Interest expenses paid* | | *(905,036)* | *(298,199)* |
| *- Income taxes paid* | | *-* | *-* |
| **INVESTMENT ACTIVITIES** | | | |
| Investments in tangible assets | | (40,551,645) | (4,573,000) |
| Investments in intangible assets | | (281,783) | (354,876) |
| **Cash flow from investment activities** | | **(40,833,428)** | **(4,927,876)** |
| **FINANCING ACTIVITIES** | | | |
| Increase in share capital | | - | 36,800,000 |
| Increase in payables for non-current loans | | 14,760,000 | 602,660,439 |
| Increase in payables for current loans | | (50,000,000) | (888,025,406) |
| Equity instruments | | | 284,400,000 |
| Changes in other short-term financial liabilities | | (31,056,744) | 27,920,000 |
| **Cash flow from financing activities** | | **(66,296,744)** | **63,755,033** |
| **Increase (decrease) in cash and cash** | | **(15,621,051)** | **22,290,722** |
| **Opening cash and cash equivalents** | | **68,638,179** | **46,347,457** |
| **Closing cash and cash equivalents** | | **53,017,128** | **68,638,179** |

## Statement of changes in Shareholders' Equity

| (Euro) | Note | Share capital (a) | Other reserves (b) | Accumulated gains (losses) (c) | Profit (loss) for the period (d) | Total (a+b+c+d)=e |
|---|---|---|---|---|---|---|
| **Balance at January 1, 2015** | | **91.130.000** | **105.052.497** | **(147.540.164)** | **(109.506.283)** | **(60.863.949)** |
| Allocation of profit for 2014 | | | | (109.506.283) | 109.506.283 | - |
| *elimination of S.E. for coverage of losses* | | (91.130.000) | (105.052.497) | 196.182.497 | | |
| *increase in share capital* | | 60.516.142 | 39.483.858 | | | 100.000.000 |
| *issuing of participating financial instruments (Junior PFI)* | | | 284.386.754 | | | 284.386.754 |
| *Fair value measurement of Junior PFI and coverage of residual losses* | | | (140.405.638) | 60.863.949 | | (79.541.689) |
| Comprehensive income/loss - December 2015 | | | 17.355 | | 13.890.376 | 13.907.731 |
| *of which:* | | | | | | |
| *Income/losses booked directly to shareholders' equity* | *7* | | *17.355* | | | 17.355 |
| *Income/loss - DECEMBER 2015* | | | | | *13.890.376* | *13.890.376* |
| **Balance at January 1, 2016** | | **60.516.142** | **183.482.329** | | **13.890.376** | **257.888.847** |
| Allocation of profit for 2015 | | | 694.519 | 13.195.857 | (13.890.376) | - |
| Comprehensive income/loss - December 2016 | | | (474.285) | | (58.689.739) | (59.164.024) |
| *of which:* | | | | | | |
| *Income/losses booked directly to shareholders' equity* | *7* | | *(474.285)* | | | (474.285) |
| *Income/losses for the year - December 2016* | | | | | *(58.689.739)* | *(58.689.739)* |
| **As at December 31, 2016** | | **60.516.142** | **183.702.563** | **13.195.857** | **(58.689.739)** | **198.724.823** |

*Torrevaldaliga Sud Power Plant*

# Explanatory Notes

## Declaration of conformity

This Report is prepared in accordance with IFRS international accounting standards and provides complete information on the basis of IAS 1.

IFRS means all the "International Financial Reporting Standards", all International Accounting Standards ("IAS"), all of the interpretations of the International Financial Reporting Standards Committee ("IFRIC"), all the interpretations of the Standing Interpretations Committee ("SIC"), adopted today by the European Union and contained in the EU Regulations published on G.U.C.E. up to today's date, in which the Board of Directors of Tirreno Power S.p.A. It authorised the publication of these financial statements. Still on the subject of interpretation, finally, was also taken into account the documents on IAS / IFRS in Italy prepared by the Italian Accounting Board (OIC).

## Structure and content of financial statements

These financial statements consist of the Balance Sheet, Income Statement, Statement of / total loss, cash flow statement, statement of changes in shareholders' equity, as well as the explanatory notes.



As for the financial statements that the Company has chosen to adopt it should be noted:

- In the "balance sheet" assets and liabilities are sorted by due date, separating current and non-current items by expiry, respectively, within or after 12 months;
- The "income statement" is presented in a scalar form by nature;
- The "cash flow statement" is prepared using the indirect method, as allowed by IAS 7;
- The "statement of comprehensive income / loss" is prepared separately in accordance with IAS 1 Revised.
- The "Statement of Changes in Shareholders' equity" is prepared in accordance with IAS 1 Revised.

The functional currency used for the presentation of financial statements is the euro and all amounts are expressed in thousands of Euros unless indicated otherwise. For disclosure purposes, the values are reported without decimals.

This document is subject to auditing by the auditing firm EY S.p.A., a company which was also entrusted with the legal auditing of accounts.

### Assessment of the going concern assumption

Tirreno Power closed the year ended as at December 31, 2016, with a loss of Euro 58,690 thousand, impacted significantly, inter alia, by the provision made for the estimated expenses, amounting to Euro 20,229 thousand, deriving from the signing of the trade union agreement on December 2, 2016, as well as a positive Gross operating profit of Euro 54,702 thousand, compared to Euro 220 thousand achieved in 2015. However, at operating level, the result achieved was still negative, amounting to Euro 38,178 thousand, albeit a significant improvement compared to the previous year (a negative Euro 66,465 thousand in 2015), also taking into account the effect of the aforementioned allocation under provisions for risks and charges.

These results highlight a better operating performance, also in 2016, than the expectations included in the Business and Financial Plan definitively approved by the Board of Directors on July 8, 2015 (hereinafter the “Plan”), forming the basis of the Restructuring Agreement, and are attributable to the considerably higher than expected values of production and excellent results achieved on the Dispatching Services Market, as a result of the favourable pricing opportunities seized in certain months of the year. These results were achieved despite the continued productive shutdown of the coal-fired units at the Vado Ligure site, subject to the preventive seizure order of the preliminary Judge of the Court of Savona effective from March 11, 2014 as part of the criminal proceedings initiated by the Prosecutor of Savona, as better described in the section on the Operating structure, a situation that involved the Board of Directors’ acknowledgement, on June 6, 2016, that the conditions did not exist to allow a future return to service of coal-fired units 3 and 4 of the Vado Ligure plant. In this regard, it should be noted that, on December 23, 2016, the Company obtained a favourable opinion from the Ministry of Economic Development for definitively putting coal-powered units out of service.



The critical financial and equity situation of the Company, as highlighted in the previous financial statements, had implied the need for the Company to reach a Restructuring Agreement in 2015 with the main creditors (the Lenders) for payables pursuant to art. 182-bis of the Bankruptcy Law, aimed at structurally resolving the existing financial and equity imbalances.

In this regard it should be noted that on July 9, 2015, the Restructuring Agreement (ADR) between the Company, its shareholders and the financial institutions was signed and, the next day, July 10, the Agreement was filed with the Rome Register of Companies, and the Company filed an application with the Court of Rome - Bankruptcy Section -, pursuant to art. 182-bis of the Bankruptcy Law, for the approval of the same, achieving the purposes of art. 182-sexies of the Bankruptcy Law. The Debt Restructuring Agreement and the financial manoeuvre agreed with the lenders based on the Company Financial and Business Plan, finally approved by the Board of Directors on July 8, 2015, attached to and an integral part of the Restructuring Agreement; on the same date, Enrico Laghi, as an independent expert, meeting the requirements of Art. 67, third paragraph, letter d) of the Bankruptcy Law, issued the certification on the authenticity of company data and the feasibility of the Financial and Business Plan and the Restructuring Agreement (ADR, signed by the Company, its shareholders and lenders) with particular reference to its suitability to ensure full payment of the external creditors, under art. 182-bis, first paragraph of the Bankruptcy Law. The Court of Rome - Bankruptcy Section by Decree of November 18, 2015, filed with the Registrar of the Court and with the Register of Companies on November 20, 2015, approved the Restructuring Agreement. Said decree became final on December 7, 2015 due to the absence of complaints.

The Plan was prepared on the basis of the results of a study of the market and of forecast dispatching commissioned to a leading company in econometric studies in the electricity sector in Italy, and incorporates the management's best estimates, at the plan drafting date, in relation to the main assumptions underlying the company's operations. This plan assumes from 2015 and in the following three years (2016-2018) modest profitability, because the electricity market will continue to be characterised by overcapacity on the production side, by weak demand and a growing supply of energy from renewable sources, likely to increasingly reduce both achievable volumes on the market and the difference between Peak and Off-Peak prices. The plan also made provision for the introduction of the Capacity Market from 2018 and the recovery of electricity demand which will enable a gradual return to higher profit margins. In addition, the Plan already prudentially assumes the non-reactivation of coal units VL3 and VL4 due to the rejection of the application for release from seizure and/or confirmation of the AIA (integrated environmental authorisation) suspension measure, and simultaneous failure to obtain a new authorisation as a result of the application for the early renewal of the AIA submitted by the company on May 6, 2014, as well as the effects of a plan for increasing resource efficiency.

In this regard, the staff reduction plan set out in the Business and Financial Plan was implemented through the signing of the trade union agreement of December 2, 2016: despite this agreement entailing higher expenses for the Company than forecast in the Plan, in terms of redundancy incentives, personnel costs on completion of the procedures set forth in the agreement were essentially in line with those envisaged in the Plan. With reference to this aspect, which was the only event to take place in 2016 according to different methods with respect to those set out in the Business and Financial Plan, the Company requested an opinion from Mr. Enrico Laghi who reached the conclusion that the proposed trade union agreement does not constitute a substantial change to the Plan as such to compromise the feasibility of the agreement, given that the higher outflows deriving from any implementation of the trade union agreement are offset by the higher inflows stemming from the better results achieved.



It should be noted that the Restructuring Agreement and the related financial measures are targeted at refinancing, in 2015, the total amount of Euro 886,696 thousand, and at recapitalisation of the Company, according to the methods described below:

- for Euro 300,000 thousand as the "term loan A", to be repaid according to the amortisation plan starting from June 30, 2017, remunerated at the Euribor rate of + 2.07%, maturity in December 2022 (+ optional extension for a further 2 years );
- for Euro 50,000 thousand as "revolving credit facility", remunerated at the Euribor rate + 2% with the possibility of repayment and drawdown up to the maturity date in December 2022 (+ optional extension for a further 2 years);
- for Euro 250,000 thousand in the form of a "mandatory convertible bond", remunerated at a rate of 3.42% (PIK), maturity in December 2024 (with the possibility of optional extension for a further 2 years);
- for Euro 2,309 thousand as the Hedging Credit Facility to be repaid according to the amortisation plan incorporating 6 half-yearly instalments starting from June 30, 2017, remunerated at the Euribor rate of + 2%;
- for Euro 284,387 thousand in the form of equity instruments (PFIs) in accordance with art. 2346, paragraph 6, of the Italian Civil Code, whose fair value at the issue date, equal to Euro 204,000 thousand, has been accounted as a shareholders' equity reserve, with a positive effect of Euro 80,387 thousand recorded at December 31, 2015 under financial income.;

On December 16, 2015 the Extraordinary Shareholders’ Meeting approved the share capital increase of Euro 100 million set out in the Debt Restructuring Agreement, of which Euro 60,516 thousand as share capital and Euro 39,484 thousand as share premium reserve - subscribed and fully paid in as set out below. With the aim of capitalising the Company, the Shareholders' Meeting has also issued the equity instruments, without voting rights, called “Junior PFIs”, in the manner prescribed in the ADR and the total nominal amount indicated above, in fact, transforming part of the debt into shareholders’ equity.

On completion of all the actions contained in the DRA, the shareholders’ equity of the Company - which at December 31, 2014 was a negative Euro 60,864 thousand - was a positive Euro 257,889 thousand at as December 31, 2015. As at the date of these financial statements, based on the results achieved, the shareholders’ equity came to Euro 198,725, deemed suitable by the Directors to ensure adequate capitalisation of the Company with respect to the objectives set out in the Plan.

It should also be noted that the results achieved in the 2016, like those registered in 2015, were better than those forecast in the Business and Financial Plan, confirming the reasonableness of the assumptions used in preparing the Plan and consequently instilling confidence in the Company’s Board of Directors as regards its ability to achieve the results forecast in the plan also in future years, despite being fully aware that these results may only be achieved if future events occur - the assumptions and actions set out in the plan connected primarily with market trends, regulatory developments and resource efficiency drives - which are subject, owing to their nature, to uncertainties in terms of the methods and timing of implementation.

Therefore, the Directors have prepared these financial statements based on the going concern assumption, without prejudice to the fact that this business continuity is subject, as necessary, to the realisation of the assumptions set out in the Plan, according to the assumed methods and timing of implementation.

**Accounting policies and valuation criteria**

The accounting policies and valuation criteria adopted are summarised below. The accounting policies are adopted on a going concern basis as described above and with the principles of competence, relevance and materiality of accounting information and the prevalence of substance over form.

The general principle used in preparing these financial statements is the cost method with the exception of any derivatives for which IAS 39 requires the fair value measurement.

**Use of estimates**

The preparation of financial statements and related notes requires the application of accounting principles and methods that sometimes are based on complex judgments and estimates, linked to historical experience, and assumptions that are from time to time considered reasonable and realistic based on the associated circumstances. The application of these estimates and assumptions affects the information provided and the amounts reported in the balance sheet, income statement and cash flow statement, and consequently in the statement of changes in equity. The final values of the budget for which has been the basis of estimates and assumptions, may differ from those reported in this document due to the uncertainty that characterizes the assumptions and conditions upon which the estimates are based.

A change in the assumptions underlying conditions used could have a potentially significant impact on the financial statements, on recoverability and on depreciation and amortisation of non-current assets, risk provisions, some regulatory credits, the fair value of financial instruments; particularly the recoverability assessments of major asset items, such as tangible and intangible assets and deferred tax assets, are based on significant estimates related to the determination of future cash flows and taxable income. Estimates and assumptions are reviewed periodically and the effects of each change are simultaneously recognised in the income statement. In connection with the use of estimates, please refer to the "Evaluation of the going concern assumption" and the note no. 1.



**Translation of foreign currency items**

The functional and presentation currency is the euro.

Foreign currency transactions are recorded at the exchange rate prevailing at the transaction date. Monetary assets and liabilities in currencies other than the functional currency are subsequently adjusted at the exchange rate prevailing at the balance sheet date. Exchange differences arising from the conversion operations are reflected in the income statement and recorded under financial income and expenses. Non-monetary assets and liabilities denominated in foreign currencies and valued at cost are translated at the exchange rate prevailing at the date of initial transaction.

**Tangible assets**

Property, plant and equipment are stated at acquisition or production cost, less accumulated depreciation and any impairment losses. The cost includes expenditure directly incurred to prepare the assets for use, as well as any charges for dismantlement and removal (as provided by IAS 37), recorded at the present value of the future is estimated to support. The cost also includes any interest paid on the purchase or construction of property, plant and equipment incurred to bring exercise thereof.

Also included are the costs for the strategic spare parts of the plants.

Amortisation commences when the asset is available for use and is recognised systematically over the remaining useful life of the same, i.e. on the basis of the estimated useful life.

The useful life of property, plant and equipment and their residual value are reviewed and adjusted if appropriate, at least at the end of each year. The presumed realisable value which is deemed recoverable at the end of its useful life, if determined, is not amortised.

Where the asset subject to depreciation is composed of separately identifiable elements whose useful life differs significantly from that of the other parts that make up the asset, depreciation is calculated separately for each of these parts, in application of the component approach.

Ordinary maintenance costs are fully expensed in the year they are incurred.

The costs incurred for the maintenance performed at regular intervals (so-called Major Inspection) are recorded as assets in the balance sheet and are amortised on the basis of the intervention cycle, as planned by management.

The depreciation of freely transferable assets outside the scope of IFRIC 12 is calculated on a straight-line basis over the shorter of the remaining life of the concession and the estimated useful life of the same.

Land, whether free of constructions or annexed to civil and industrial buildings are not depreciated as it has an unlimited useful life.



The estimated useful lives of property, plant and equipment is as follows:

| | |
|---|---|
| Buildings | 25/40 years |
| Equipment; steam generators; Mechanical Equipment; Hydraulic works | 20 years |
| Combined cycle plants | 30 years |
| Maintenance | 2-8 years |
| Computers; Office machines; IT equipment | 5 years |
| Transport lines | 35 years |
| Television transmission systems and Industrial equipment | 10 years |

If there are signs of deterioration, tangible assets are subject to a recoverability test (so-called “impairment test”) which is illustrated in the following paragraph “Impairment of Assets”.

**Intangible assets**

An intangible asset is an identifiable non-monetary, identifiable and without physical substance, controllable and capable of generating future economic benefits. They are carried at cost of purchase and / or production cost, including directly attributable costs of preparing the asset for use, net of accumulated amortisation, in cases where there is an amortisation process, and any impairment.

Amortisation commences when the asset is available for use and is recognised systematically over the remaining useful life of the same, i.e. on the basis of the estimated useful life.

Research costs are expensed in the year they accrue. Development costs are capitalised if the cost can be measured reliably and it is shown that the asset is able to generate future economic benefits.

With regard to so-called emission rights as well as economic situations similar to them, following the IASB's non-approval of IFRIC 3 (Emission Rights) and then its subsequent withdrawal, there is currently no specific international accounting standard on the issue. Until a new principle Tirreno Power, given that it procures the above environmental bonds to meet its own requirements in the performance of its industrial activities (so-called own use), it has decided to adopt, on the basis of market benchmarks, the gross method, which involves booking the emission rights as intangible assets at their fair value, which is equal to the historical cost, and registration of emission rights to be delivered as a liability. Quotas allocated freely shall be entered at a zero value. This item is not amortised, but tested for impairment. Costs incurred for purchase on the market (or, nonetheless, with consideration) of the green certificates and missing CO2 quotas to fulfill the obligation of the reporting period are recognised in the income statement on an accrual basis, under other operating expenses, given that expenses represent the fulfilment of a legal obligation.

**Impairment of Assets**

At each balance sheet date, property, plant and equipment and intangible assets with indefinite lives are tested in order to establish whether there are indicators of impairment. When the presence of these indicators is identified, the recoverable amount of the assets is estimated and any impairment loss recognised in the income statement. The recoverable amount of an asset is the higher of its fair value less costs to sell and its value in use, where the latter is the present value of estimated future cash flows of the asset. In determining the value in use, future cash flows are discounted with a discount rate before tax that reflects the assessment of the cost of money for the company, the time value and the specific risks. An impairment loss is recognised in the income statement when the asset's carrying amount exceeds its recoverable amount.



In the case of goodwill and other intangible assets with indefinite useful life or assets not available for use, this test is performed at least annually.

For tangible and intangible assets (but not for goodwill), should the reasons for a write-down effected previously no longer exist, the carrying value is reinstated by an entry in the income statement, in accordance with the limits of the net book value that the asset would have had if it had not been written down and depreciation had been charged.

**Inventories**

Raw materials, consumables and supplies are valued at the lower of cost determined using the weighted average method, and net realisable value based on market trends.

The purchase cost is determined for the reference period, in respect of each inventory item. The weighted average cost includes the relevant accessory charges relating to purchases in the period.

The value of obsolete and slow-moving inventory is written down in relation to the possibility of use or realisation, through provision of a specific materials obsolescence allowance.

**Financial instruments**

Financial instruments include financial assets and liabilities whose classification is determined at the time of their initial recognition, depending on the purpose for which they were purchased. Purchases and sales of financial instruments are recognised on the trade date.

The financial instruments include not only investments available for sale, but other non-current financial assets, receivables and non-current loans, trade receivables, other receivables originated by the enterprise as well as other current financial assets such as cash and equivalents or bank deposits and financial receivables due within three months. Fall also under financial instruments, financial liabilities, trade payables, other payables and other financial liabilities and derivative instruments.

Their initial assessment takes into account the transaction costs directly attributable to the acquisition or the issuance costs that are included in the initial measurement of financial instruments. The fair value of instruments quoted on public markets is determined with reference to quoted prices (bid price) at the balance sheet date. The fair value of unquoted instruments, including those related to electricity, is instead measured with reference to the financial valuation techniques or using major financial counterparties. In particular, the fair value of interest rate swaps is measured by discounting the expected cash flows, the fair value of foreign exchange forwards is determined on the basis of market exchange rates at the balance sheet date and the rate differentials between the relevant currencies, while the fair values of derivatives related to commodities are calculated using models based on industry best practices.

In general, in applying those models, market data are used rather than internal company data.

**Trade receivables**



Trade receivables which accrue within the normal commercial terms are not discounted and are recognised at cost (identified by their nominal value) net of related impairment losses.

Whenever there is objective evidence of impairment, the asset's value is reduced to such an extent as to be equal to the discounted value of future cash flows: the losses in value in the impairment test are recognised in the income statement. Significant financial difficulties of the debtor, probability that the debtor is subject to insolvency proceedings, or the natural delay in meeting payments (amounting to at least 30 days) are indicators of impairment. If in subsequent periods, the reasons for the write-down no longer apply, the value of the assets is restored up to the value that would have resulted from the amortised cost if the impairment had not been effected. As for trade receivables and, in general, the assets and liabilities with a residual term not exceeding 12 months, the fair value is reasonably assumed to approximate their book value.

**Cash and cash equivalents**

Cash and cash equivalents include cash, i.e. assets that meet the requirements of availability on demand or at short notice, successful outcome and absence of collection expenses and are measured at fair value.

**Cancellation (derecognition) of financial assets**

Financial assets are derecognised when the rights to receive cash flows from the instrument expires and the entity has transferred substantially all the risks and rewards relating to the instrument and the relative control.

**Trade payables**

The trade payables which accrue within the normal commercial terms are not discounted and are recognised at cost (identified by their nominal value).

**Financial liabilities**

Financial liabilities, including borrowings, trade payables and other payment obligations, are initially recognised at cost corresponding to the fair value of the liability net of costs incurred to secure loans (transaction costs). Following initial recognition, financial liabilities are measured at amortised cost using the effective interest rate. They are consequently restated net financial charges on the basis of the effective interest rate method.

If there is a change in expected cash flows and the possibility exists to reliably estimate the value of the loans is recalculated to reflect this change on the basis of the present value of expected future cash flows and the internal rate of return originally determined. Financial liabilities are classified as current liabilities unless the entity has an unconditional right to defer settlement for at least 12 months after the balance sheet date.



Financial liabilities are removed from the balance sheet when the specific contractual obligation is extinguished.

**Derivative financial instruments**

Derivatives are recognised on the trade date at fair value and accounted for as hedging instruments when the relationship between the derivative and the hedged item is formally documented and the hedge effectiveness, verified periodically, is high.

When derivative financial instruments accounted for as hedges hedge the risk of changes in the cash flows of the hedged item (cash flow hedge), the changes in fair value are recognised in equity under reserves while the ineffective portion is recognised in the income statement. The items whose cash flows are subject to a cash flow hedge are measured at amortised cost. The company will prospectively suspend accounting using the cash flow hedge method from the moment the requirements are no longer met. Subsequent changes in fair value in this case are charged to the income statement. The residual cash flow hedge reserve recognised directly in equity until the hedge is no longer considered effective must be recorded in the income statement when the transaction or transactions take place, to which it/they refer(s).

If derivatives are defined in accordance with IAS 39 as the price risk hedges (fair value hedges), they are recorded in the balance sheet and are measured at fair value and the gains or losses determined are recognised in the income statement; the corresponding items hedged with derivatives are measured at fair value.

Changes in the fair value of derivative financial instruments put in place by each company that does not meet the requirements for recognition as hedging instruments (hedge accounting), measured subsequent to initial recognition, are treated as positive or negative components of the economic result for the year.

To ensure the correct recognition, classification, representation in the financial statements and subsequent measurement, the derivative finance transactions in place can be divided as follows:

- *Transactions considered hedges under IAS 39*: these are transactions to hedge cash flows (cash flow hedge). In the case of cash flow hedges, the accrued result is included in profit or loss when realised, whereas the prospective value is recognised in equity.
- *Transactions not considered accounting hedges pursuant to IAS 39*, albeit for hedging purposes: the Company may hold derivative instruments to hedge its exposure against fluctuations in selling prices of electricity and purchase of fuels. In line with the chosen strategy, Tirreno Power does not enter into derivative transactions for speculative purposes. When such operations are not classified as hedges pursuant to IAS 39, the accrued result and prospective value are included in the operating result.

**Embedded derivatives**

Embedded derivatives included in other financial instruments or in other contracts are treated as separate derivatives when their risks and characteristics are not closely related to those of the host contracts and the latter are not stated at fair value with recognition of gains and losses in the income statement. The Company verifies the existence of any embedded derivatives, analysing the facts and circumstances which could have originated them, including, for example, any contracts regarding the receipt or sale of “non-monetary” assets according to specific company purchase, use or sale requirements.



**Employee Benefits**

The short-term benefits are recognised in the income statement in the period in which the working activity is performed.

It is noted that, in connection with the pension reform of 2007, the provision for Post-employment benefits was restated, by adopting the new methodological approach, or considering that the amounts accrued as of January 1, 2007 are a defined contribution benefit and, therefore, not included in the calculation of liabilities. Where the provision accrued at December 31, 2006 is treated as a defined benefit plan, the benefits granted to employees are recognised over the vesting period, as well as other long-term benefits (Additional months' salaries, Tariff Incentives and Loyalty Bonuses).

The cost of providing benefits under the various plans is determined separately for each plan, using actuarial assumptions to estimate the amount of future benefits that employees have accrued at the reporting date.

The obligation in question is determined on the basis of independent actuarial assumptions. Gains and losses resulting from actuarial calculations are recognised in the income statement.

For defined contribution plans, contributions are only recorded when the employees have provided their activities and then those contributions are accrued. In the latter case Tirreno Power pays fixed contributions into a separate entity (e.g. A fund) and will have no legal or constructive obligation to pay further contributions if the fund is not solvent.

Lastly, the IASB has issued a number of amendments to IAS 19. The new standard requires all actuarial gains / losses accrued at the reporting date to be recognised in the "Statement of Comprehensive Income" (OCI). Thus it eliminated the possibility of deferral through the corridor method (no longer present), as well as their possible recognition in the income statement.

**Provisions for risks and charges**

Provisions are recorded to cover losses and charges of a specific nature, certain or probable, in respect of which, however, the amount and/or date of occurrence cannot be determined.

Provisions for risks and charges are recognised when, at the reporting date, in the presence of a present obligation (legal or constructive) to third parties arising from a past event, it is likely that, to fulfil the obligation, an outflow of resources whose amount can be estimated reliably will be required.

When the financial effect of time is significant, the provision is discounted using a yield curve that reflects the time value of money expressed by the market and the risks associated with the liability.

If the provision is estimated taking into account the discounting process, the increase in provisions, due to the passage of time is recognised in the income statement as a financial charge. If the liability relates to tangible assets (e.g. dismantling and restoration of sites), the provision is recorded against the asset to which it relates; the expense is recognised in the income statement occurs through the depreciation of the tangible fixed asset to which the expense relates, as well as through the measurement of the financial expenses of the revaluation of the liability.



The allocation of restructuring expenses takes place when the general criteria for allocation of a provision are respected. The Company has an implicit obligation when a detailed and formalised plan identifies the business unit concerned, the location and number of employees forming the object of the restructuring, the detailed estimate of costs and the implementation timescales. In addition, the personnel concerned must be informed of the main characteristics of the restructuring plan.

**Revenue recognition**

Revenue is recognised to the extent that it is possible to reliably determine its value (fair value) and it is probable that the associated economic benefits will be enjoyed by taking into account any discounts and reductions linked to quantities.

Revenues related to the sale of electricity are recognised at the time of delivery of supply, even if not invoiced, based on the actual sales prices on the Power Exchange or the conditions set forth contractually, taking into account the existing legislation.

Revenues from services are recognised when they can be reliably estimated, on the basis of the percentage of completion method.

Other revenues are determined according to the terms and conditions which take account of the risks and benefits transferred.

**Recognition of costs**

Costs are recognised in the periods in which the related revenues are recorded and, in general, in accordance with the accrual principle. Costs that cannot be associated with revenues are immediately recognised in the income statement. For the criteria for recognition and measurement of specific costs, the Company considers their nature and the reference accounting legislation.

**Financial income and expenses**

The financial income and expenses are recognised according to the accrual method, based on the interest accrued on the amount of the related financial assets and liabilities using the effective interest rate.

**Dividends**

Dividends distributed to shareholders are reported as changes in shareholders' equity on the date on which they are approved by the shareholders' meeting.

**Government grants**

Government grants, in the presence of a formal resolution by the disbursing entity, are recognised on an accruals basis in direct correlation with the costs incurred. In particular, the operating grants are credited to the income statement under "Other income", while public capital grants that relate to property, plant and equipment are recorded as deferred revenue in balance sheet liabilities. The deferred income is recognised in the income statement as income on a straight-line basis over the useful life of the asset to which it directly relates.



**Income tax**

Current income taxes are recognised as tax payables and calculated based on the estimated taxable income determined in accordance with the provisions in force at the reporting date.

Deferred taxes are calculated on temporary differences between the carrying amounts and the corresponding amounts recognised for tax purposes applying tax rates that are expected to apply in the period when the asset is realised or the liability settled.

Deferred tax liabilities are recognised without exception for all taxable temporary differences. Deferred tax assets are only recognised if it is likely that, within a reasonable timeframe, taxable income emerges of a sufficient amount to absorb the deductible temporary differences and the underlying IRES losses to such deferred taxes.

Current and deferred taxes are recognised in the income statement, except those relating to items charged or credited directly to equity; in which case, the tax effect is recognised as a separate item in equity.

Income taxes include the effects, better described in the explanatory notes on deferred tax assets and liabilities, of Law no. 208 of December 28, 2015, (2016 Stability Law) regarding the reduction in the IRES rate from 27.50% to 24% from tax year 2017.

**Changes in International Accounting Standards**

With reference to the description of recently issued accounting standards, in addition to what is stated in the financial statements at December 31, 2015, to which reference should be made, the international accounting standards that became applicable from January 1, 2016, given adopted by the EU, are reported below:

Amendments to IAS 19. Defined contribution plan: employee contributions.

Amendments to IAS 16 and IAS 38. Clarification of acceptable methods of depreciation and amortisation.

Amendments to IAS 24. Related party disclosures

Amendments to IAS 1. Disclosure initiative.

The application of the amendments to the existing standards have had no effect on the Company's financial statements.

## Type of risks and management of hedging activities

For Tirreno Power S.p.A., in general, risk-taking is limited, in nature and extent, to those which, according to principles of sound and prudent management, are the risks considered ordinary. The principal risks identified, monitored and managed are as follows:

- Operational risk
- Market Risk
- Credit risk
- Liquidity Risk
- Risk of interest rate on cash flows.

The different types of risk are monitored in order to assess the potential adverse effects and take the appropriate actions to mitigate them. The optimisation and the reduction of the level of risk is pursued through an adequate organisational structure, the adoption of rules and procedures, the implementation of certain trade and procurement policies, the use of insurance coverage and derivative financial instruments.

In performing the electricity generation activities, the company is exposed to risks that are constantly monitored by management in accordance with the provisions of its own risk management manual. The role of risk owners, as head of risk management, is entrusted to the General Manager, who is assisted by the Risk Management Committee appointed by the Board of Directors. In identifying, measuring, monitoring, controlling and reporting the Risk Owner is supported by the Risk Control Department.



### Operational risk

Operational risk refers to the risk of direct or indirect loss resulting from inadequate procedures, human resources, legal aspects and internal systems, or from external events. This type of risk involves a number of competences and management systems within the company and can be traced, to four categories of reasons:

1. human resources: losses arising from staff conduct such as errors, fraud, non-compliance with internal rules and procedures, incompetence or negligence, etc .;
2. processes: failure of internal procedures or, something which is very common, deficiencies in the control system;
3. external factors: environmental threats, criminal activity committed by external parties, political or military events, changes in the regulatory and tax context, etc .;
4. technology: all things related to ICT, to systems, etc..

Owing to the nature of its business, the company is constantly subject to operational risks which, if not managed properly, can lead to economic and financial losses, damage to the company or to third parties. Risks of loss or damage can arise both from accidental events during the construction of the plants and from sudden unavailability of one or more machines critical to the production processes.

Prevention and control activities, aimed at reducing the frequency of these events, or to reduce their impact, provide high safety standards and frequent revision and maintenance plans. To this end, Tirreno Power is constantly engaged in the critical analysis of key business processes; the primary objective of this analysis is the continuous improvement of its internal procedures.

When appropriate, effective risk management policies and specific insurance policies in the business domain minimise the possible consequences of such damages.

An important source of risk is represented by the continuous evolution of the reference legislative, tax, regulatory, and environmental context. The company is committed to monitoring activity in order to promptly acknowledge the changes that have occurred by minimising the resulting economic impact.

Special attention is given to information systems that support business operations concerning, in particular, the technical, commercial and administrative aspects. In order to limit the risk of business interruption caused by system malfunctions, the company has hardware and software architectures boasting a highly reliable configuration for those applications that support critical activities. In addition, as part of the services provided by external suppliers, the service for the monitoring of the backup and any “restore” activities is structured to ensure quick recovery times.



**Market Risk**

Market risk is the risk that the value of a financial instrument, as defined by IAS 32, will fluctuate because of changes in market prices or exchange rates.

Owing to the nature of its business, the Company is exposed to changes in the prices of electricity, fuel and environmental costs ($CO_2$ Rights) that can significantly influence the financial results.

To mitigate this exposure, it has developed a strategy of stabilising margins by means of the early negotiation of fuel supply. Through formulas or indexing, the company pursues, as far as possible, a policy of standardisation between sources and physical uses.

The Company has also implemented a formal procedure that provides for the measurement of the residual commodity risk and the implementation of a hedging strategy using derivatives. Hedging transactions may have the objective of stabilising the margin on an individual transaction or a group of similar transactions, or to limit overall exposure to price risk. Tirreno Power does not adopt speculative positions in financial instruments.

In the course of 2016, the Company has not had access to the credit lines needed to be able to implement its hedging strategy through financial instruments; as at December 31, 2016, in fact, there were no hedging instruments in place.

**Credit risk**

Credit risk represents the Company's exposure to potential losses arising from the default of a counterparty.

Credit risk is limited due to the characteristics and the creditworthiness of the customers served. The portfolio of accounts receivable is constantly monitored by the relevant departments. Tirreno Power also pays particular attention to the selection of prime counterparties (both commercial and financial), the evaluation of supplier references in terms of the customers served and respect for supply/service obligations, in the definition of contractual penalties in cases where the non-fulfillment of the obligation by the third party may have economic consequences for the company in the issue and request for guarantees, especially financial, for entering into derivative contracts according to ISDA standards.

As for the payment terms applied by most customers, deadlines are mostly concentrated within thirty or sixty days from billing, normally monthly and is carried out within the month following the month of the supply.

The table below shows that, at the reporting date, the credit risk is reduced given that the trade receivables relate either to counterparties with a high credit rating, or other operators with whom supply contracts are also in place that generate net positions to essentially cover the credit risks.

| Information on counterparty quality (Thousands of Euro) | 12.31.2016 | % | 12.31.2015 | % |
|---|---|---|---|---|
| **Receivables for sale of energy** | | | | |
| State-owned company [1] | 83,991 | 51% | 83,750 | *79%* |
| Related parties | - | 0% | - | *0%* |
| - Other operators | 75,746 | 46% | 20,809 | *20%* |
| **Total receivables for sale of energy** | **159,737** | **97%** | **104,559** | ***99%*** |
| Other counterparties | 5,007 | 3% | 1,143 | *1%* |
| **Total trade receivables** | **164,744** | **100%** | **105,702** | ***100%*** |

(1) Gestore del Mercato Elettrico S.p.A. (GME) and Terna S.p.A.



**Liquidity Risk**

The liquidity risk is related to the possibility that the Company is in a situation of difficulty in meeting the financial obligations arising from contractual commitments and, more generally, from its financial liabilities.

This risk is closely linked to the phase of refinancing that the Company is currently engaged in, as described in note 8 “Payables for loans”.

The following table summarises the contractual expiry date for the financial and trade assets and liabilities at the date of these financial statements.

| Expiry of financial assets and liabilities (Thousands of Euro) | Within 1 year | Between 1 and 2 years | Between 2 and 5 years | After 5 years | Total |
|---|---|---|---|---|---|
| Cash and cash equivalents | 53,017 | | | | 53,017 |
| Trade receivables and other assets | 205,769 | 58,568 | | | 264,338 |
| **Total financial assets** | **258,786** | **58,568** | **-** | **-** | **317,355** |
| Trade payables | 8,106 | 35,463 | 144,957 | 378,917 | 567,444 |
| Trade payables and other liabilities | 169,578 | 1,693 | 1,423 | - | 172,695 |
| **Total financial liabilities** | **177,685** | **37,156** | **146,380** | **378,917** | **740,138** |
| **Total net exposure** | **81,102** | **21,412** | **(146,380)** | **(378,917)** | **(422,783)** |

**Interest rate risk on cash flows**

The exposure to risk of changes in the Company's interest rate is linked primarily to the financial debt, 55% of which is at floating rate. The Company, taking into account the contractual obligations, regularly assesses its exposure to the risk of changes in interest rates and manages these risks through the use of non-speculative derivative financial instruments.

The Hedging policy aims to stabilise cash outflows relating to financial expenses, reducing the effects of increases in interest rates and at the same time retaining some of the benefits associated with a reduction of the same through a combination of debt between fixed and floating rate.



As at December 31, 2016 there were no interest rate hedging instruments.

## Notes to the Balance Sheet

## ASSETS

### Non-current assets

### 1. PROPERTY, PLANT AND EQUIPMENT

Details of tangible fixed assets are provided below, by individual category, along with the changes in the period:

| (Thousands of Euro) | FIXED ASSETS IN OPERATION | | | | FIXED ASSETS IN PROGRESS AND ADVANCES | BOOK VALUE |
|---|---|---|---|---|---|---|
| | Land and buildings | Plant and equipment | Industrial and commercial equipment | Other assets | | |
| -historical cost at 12.31.2015 | 226,105 | 1,968,677 | 10,416 | 4,124 | 17,764 | 2,227,085 |
| -write-downs (-) at 12.31.2015 | (21) | (113,968) | | | (10,823) | (124,812) |
| -accumulated depreciation (-) at 12.31.2015 | (119,683) | (1,204,287) | (9,490) | (3,355) | | (1,336,815) |
| **Opening values at 01.01.2016** | **106,401** | **650,422** | **926** | **769** | **6,941** | **765,458** |
| Changes at 12.31.2016 | | | | | | |
| -acquisitions | 215 | 24,522 | 95 | 110 | 15,610 | 40,552 |
| -disposals (-) | | | | | | |
| of which: | | | | | | |
| *-historical cost* | (99) | (5,636) | | | | (5,735) |
| *accumulated depreciation* | 79 | 5,406 | | | | 5,484 |
| *use of the write-down provision* | 21 | 231 | | | | 252 |
| -depreciation | (7,674) | (51,263) | (198) | (256) | | (59,390) |
| -commissioning | 76 | 5,432 | | 61 | (5,570) | (2) |
| -other changes | | | | | | |
| of which: | | | | | | |
| -historical cost | | | | (2) | 261 | 260 |
| accumulated depreciation | | | | | | |
| **Total changes (B)** | **(7,382)** | **(21,308)** | **(103)** | **(86)** | **10,301** | **(18,579)** |
| **Changes at 12.31.2016** | **99,018** | **629,113** | **823** | **683** | **17,242** | **746,879** |
| Of which | | | | | | |
| -historical cost | 226,296 | 1,992,995 | 10,510 | 4,294 | 27,804 | 2,261,900 |
| -write-downs (-) | 0 | (113,738) | | | (10,562) | (124,300) |
| -accumulated depreciation (-) | (127,278) | (1,250,144) | (9,687) | (3,611) | | (1,390,721) |
| **Net value** | **99,018** | **629,113** | **823** | **683** | **17,242** | **746,879** |

As of December 31, 2016 the value of property, plant and equipment amounted to Euro 746,879 thousand. During the year, the Company reported investments totaling Euro 40,552 thousand, of which Euro 15,610 thousand related to "fixed assets in progress and advances" and Euro 24,942 thousand relating to the "fixed assets in operation".

**Investments** relating to fixed assets in operations primarily concerned:

- the Major Inspections of the VL5 combined cycle unit (Euro 24,140 thousand), of which Euro 20,017 thousand for costs incurred in 2016 and the remainder relates to the commissioning of fixed assets in progress as at December 31, 2015;
- Euro 1,717 thousand relating to the Naples Plant, linked to the LTSA maintenance contract;
- Euro 1,030 thousand for works performed at the hydroelectric plants, such as the channel restoration at the Argentina (Euro 374 thousand) and Chiesuola (Euro 356 thousand) plants, the review of the turbine and alternator of the Cairo Montenotte Plant (Euro 238 thousand);
- Euro 638 thousand for the repair to a 300 MVA 20/420Kv transformer in the strategic stockpile at the VL5 combined cycle unit;
- Euro 385 for safety and environmental adaptation measures of the Vado Ligure plant;
- Euro 266 thousand for works to restore the low pressure rotor coming from unit VL4 and intended for TV6.

By contrast, as regards investments in fixed assets in progress and advances, amounting to Euro 15,610 thousand, note should be taken not only of those relating to the Major Inspections of the VL5 unit mentioned above, but Euro 7,015 thousand for the progress of the Major Inspection works at unit TV6, Euro 6,808 thousand for the purchase of the necessary materials for the Major Inspection at the Naples Plant planned for the summer of 2017, as well as Euro 597 thousand for the environmental adaptation and safety works at the hydroelectric plants.

**Disposals** refer to the dismantling of the plants and buildings of the former Napoli Vigliena Plant, fully written down in previous years.



Lastly, it should be noted that the overall write-down of coal-powered plants currently amounts to Euro 67,799 thousand, net of depreciation accrued as at December 31, 2016.

As indicated in the annual financial statements of the previous year, the impairment test performed as at December 31, 2015 on the sole Tirreno Power CGU, using the cash flows relating to the 2016-2039 period, extracted from the Business Plan forming the basis of the Restructuring Agreement definitively approved by the Board of Directors on June 25, 2015 and updated with the estimates from the 2016 budget, did not highlight the need for further write-downs of company assets. In fact, the estimated recoverable value, amounting to Euro 1,166 million, is significantly higher than the company's carrying amount, equal to Euro 840 million, leading to the recording of headroom of roughly Euro 326 million.

As at December 31, 2016, as required by IAS 36, the Company conducted an analysis of the existence of potential indicators of impairment, both external and internal.

On the back of the analyses conducted, which take into consideration, on the one hand, the results obtained in the first two years of the Plan, and the first few months of 2017, results that greatly exceeded the best expectations with respect to those envisaged in the Plan and, on the other, the short-term market scenarios which would generate economic and financial effects for the company essentially in line with those set out in the Business Plan, as well as the absence of any deterioration in the elements incorporated in the rate applied to discount expected future flows, management did not identify the presence of any impairment indicators as such to require the preparation of a new impairment test as at December 31, 2016.

The **Depreciation** of tangible fixed assets charged to the period mainly affected the combined cycle thermoelectric production sites (Euro 46,574 thousand), the relevant Major Inspections (Euro 8,607 thousand) and restoration costs (Euro 441 thousand), and are calculated using the economic-technical rates representative of the useful life of each component.

As for freely transferable assets, depreciation is proportional to the duration of the associated concession if shorter than the useful life.

Tangible fixed assets at December 31, 2016, classified according to their use, are divided as follows:

| Plant types | Original cost | Accumulated depreciation | Net value | Write-down provision | Net reported value |
|---|---|---|---|---|---|
| Production plants | | | | | |
| Thermoelectric plants | 2,094,716 | (1,321,535) | 773,181 | (113,738) | 659,443 |
| Freely transferable assets | 2,132 | (2,124) | 8 | | 8 |
| **Total** | **2,096,848** | **(1,323,659)** | **773,189** | **(113,738)** | **659,451** |
| Renewable energy plants | 85,549 | (36,481) | 49,068 | | 49,068 |
| Freely transferable assets | 29,645 | (12,747) | 16,898 | | 16,898 |
| **Total** | **115,194** | **(49,228)** | **65,966** | | **65,966** |
| **Total production plants** | **2,212,042** | **(1,372,887)** | **839,155** | **(113,738)** | **725,417** |
| Other plants and machinery, | 22,054 | (17,834) | 4,220 | | 4,220 |
| **Total operating assets** | **2,234,096** | **(1,390,721)** | **843,375** | **(113,738)** | **729,638** |
| Fixed assets in progress and advances | 27,804 | | 27,804 | (10,562) | 17,242 |
| **Total** | **2,261,900** | **(1,390,721)** | **871,179** | **(124,300)** | **746,879** |

As at December 31, 2016 there are no tangible fixed assets for which any collateral securities have been granted to third parties.

## 2. INTANGIBLE ASSETS

A table is provided below, which details the original values and changes:

| (Thousands of Euro) | Industrial patents and software applications | Concessions licences | Fixed assets in progress and advances | BOOK VALUE |
|---|---|---|---|---|
| -historical cost at 12.31.2015 | 8,319 | 9,897 | 76 | 18,292 |
| -accumulated amortisation (-) at 12.31.2015 | (7,239) | (30) | | (7,269) |
| *Opening values at 01/01/2016(A)* | *1,080* | *9,867* | *76* | *11,023* |
| Changes at 12.31.2016 | | | | |
| -acquisitions | 232 | 10,831 | 4,848 | 15,911 |
| -reclassifications | 77 | | (76) | 2 |
| -amortisation (-) | (585) | (1) | | (586) |
| -write-downs (-) | | | | |
| -other changes | | (17,758) | | (17,758) |
| **Total changes (B)** | **(276)** | **(6,928)** | **4,772** | **(2,431)** |
| *Values at 12.31.2016 (A+B)* | *804* | *2,939* | *4,848* | *8,591* |
| Of which | | | | |
| -historical cost | 8,628 | 2,970 | 4,848 | 16,446 |
| -write-downs (-) | | | | |
| -amortisation (-) | (7,824) | (31) | | (7,855) |
| **Net value** | *804* | *2,939* | *4,848* | *8,591* |



The item refers mainly to 518,721 $CO_2$ emission rights for an amount of Euro 2,926 thousand, as well as to advances of Euro 4,798 thousand for purchases of $CO_2$ with delivery in 2017.

Both the $CO_2$ rights that the Company holds in its portfolio as at December 31, 2016 and those for which delivery is deferred are purchased in order to comply with the obligations set forth for the year 2016.

The acquisitions for the period relate essentially to the purchase of 1,620,000 $CO_2$ emission rights for a total of Euro 9,052 thousand, as well as to the purchase, for Euro 1,779 thousand, of the green certificates needed for compliance with the redelivery obligations for 2015.

Other changes relate mainly to the sale of 1,000,000 emission rights for Euro 4,800 thousand and the delivery - in accordance with the Company's obligations for 2015 - of 1,123,286 $CO_2$ certificates, amounting to Euro 7,617 thousand, as well as 110,151 green certificates, amounting to Euro 4,335 thousand.

### 3. NON-CURRENT FINANCIAL ASSETS

This item refers to financial receivables due after 12 months.

| (in thousands of euro) | 12.31.2016 | 12.31.2015 | CHANGES |
|---|---|---|---|
| - loans to personnel | 649 | 760 | (111) |
| - security deposits | 16,937 | 6,783 | 10,154 |
| **Total non-current financial assets** | **17,586** | **7,543** | **10,043** |

Security deposits include, for Euro 10,495 thousand, the part of the credit relating to the free emission quotas set forth in the second period of the Emission Trading System for the Naples Plant paid by the Ministry of Economic Development in December 2016 to Intesa Sanpaolo S.p.A., as assignee of the aforementioned credit transferred by the Company during the phase of refinancing as collateral to the committed credit line for guarantees. The item also includes the deposit in favour of Terna SpA for the dispatching contract for the injection and withdrawal points issued in 2015 (Euro 6,056 thousand).

It should be noted that "loans to employees", remunerated at current market rates and guaranteed by TFR (post-employment benefits), were granted for the purchase of a first home or to meet important family needs.

As at December 31, 2016, there were no financial assets carried at a value greater than their fair value.



### 4. DEFERRED TAX ASSETS

This item includes deferred tax assets whose composition is as follows:

| (in thousands of euro) | SITUATION AT 12.31.2015 | SITUATION AT 12.31.2016 | | | |
|---|---|---|---|---|---|
| | Balance | Provisions | Uses | Other changes | Balance |
| **Deferred tax assets** | | | | | |
| Provisions for risks and charges and other write-downs | 5.474 | | (1.199) | | 4.275 |
| Reduction in value from estimate of recoverability | (3.796) | | | | (3.796) |
| **Total** | **1.678** | | **(1.199)** | | **479** |
| FV IAS 19 to Shareholders' equity reserve | 440 | 150 | | | 590 |
| **Total deferred tax assets** | **2.118** | **150** | **(1.199)** | | **1.069** |

The recoverability of deferred tax assets has been verified on the basis of the Business plan, considering a reduced observation period, based on a conservative approach, with respect to the time horizon of the plan itself. Following this analysis, similar to what was already done in the previous year, the Company decided not to proceed with the registration of additional deferred tax assets accrued during the year for Euro 19,896 thousand, mainly relating to the tax loss and provisions for risks, charges and redundancy incentives of the year.

Therefore, also considering the amounts not allocated in the 2013, 2014 and 2015 financial statements, deferred tax assets not recognised in the balance sheet amount to Euro 96,671 thousand.

### 5. OTHER NON-CURRENT ASSETS

The item, amounting to Euro 40,982 thousand, essentially includes:

- the tax credit for which a refund was requested, resulting from the 2016 tax return (Euro 23,000 thousand);
- the residual credit (Euro 17,928 thousand) for ETS allowances payable for the years 2010 to 2012 to the new plant owners, who were not satisfied with in so-called 'new entrants reserve'.

The latter amount is accounted for on the basis of criteria developed in accordance with Resolutions ARG/elt 77/08 and ARG/elt 117/10 of the AEEG and Decree Law no. 72 of 20/05/2010, as at December 31, 2014, for the Naples plant.

As already outlined in note 3, it should be noted that, in relation to the terms of the Restructuring Agreement, the credit of the ETS quotas indicated above was transferred to Intesa Sanpaolo S.p.A. (as Issuer Bank), as guarantee for the obligations deriving from the new endorsement loan agreement. These receivables transferred are actually a collateral security to the committed credit line for guarantees.

### 6. CURRENT ASSETS



| Trade receivables | 12.31.2016 | 12.31.2015 | CHANGES |
|---|---|---|---|
| Inventories | 21,293 | 23,035 | (1,743) |
| Trade receivables | 164,744 | 105,703 | 59,040 |
| Other current assets | 38,464 | 78,218 | (39,754) |
| Other current financial assets | 2,562 | 2,750 | (188) |
| Cash and cash equivalents | 53,017 | 68,638 | (15,621) |
| **Total current assets** | **280,079** | **278,344** | **1,735** |

Details of the individual items are outlined below:

**Inventories**

Inventories of fungible goods, as regards the method for determining the purchase price, show a balance sheet valuation based on the weighted average cost method.

However, as a result of events that occurred and the decisions taken in relation to the Vado Ligure site, it was considered necessary to value the inventories related to the coal units based on the lower of the presumed realisable value and the purchase cost, given that, at present, they are no longer usable in the production process.

The year 2016 saw the continued sale of coal fully written down in previous years which, therefore, concluded with the complete clearance of the coal storage facility, without having to record particular capital losses from disposal in these financial statements.

By contrast, as regards the inventories of BTZ (low sulphur content) and STZ (no sulphur content) combustible oil present in the tanks, a further write-down was effected, for a total of Euro 484 thousand, to adjust their value to the price offers actually received. As at December 31, 2016, the write-down amounted to Euro 2,282 thousand.

In addition, as regards the inventories of materials relating to the coal units, the total write-down came to Euro 22,609 thousand. In this regard, it should be noted that the value of inventories of materials booked to the financial statements as at December 31, 2016 refers to the components usable in the maintenance of combined cycle plants in operation.

Details of inventories are provided below by type:

| (in thousands of euro) | 12.31.2016 | 12.31.2015 | CHANGES |
|---|---|---|---|
| Tangible inventories | 20,982 | 21,009 | (27) |
| Fuel inventories | 142 | 1,927 | (1,784) |
| Other inventories | 168 | 100 | 68 |
| **Total inventories** | **21,293** | **23,035** | **(1,743)** |



**Trade receivables**

This item, amounting to Euro 164,744 thousand, mainly includes trade receivables for the sale of energy and other materials.

| (in thousands of Eeuro) | 12.31.2016 | 12.31.2015 | Changes |
|---|---|---|---|
| **Receivables for sale of energy:** | | | |
| -GME | 68,610 | 53,544 | 15,066 |
| -Terna S.P.A. | 15,381 | 30,206 | (14,825) |
| - Other operators | 75,746 | 20,809 | 54,937 |
| **Total receivables for sale of energy:** | **159,737** | **104,559** | **55,178** |
| **Other trade receivables** | 5,007 | 1,143 | 3,864 |
| **Total trade receivables** | **164,744** | **105,703** | **59,041** |

It should be noted that almost all of these receivables arose over the last two months of the year and to the date of this note is essentially fully collected or collectible, given that the relevant expiries are in 30/60 days.

The increase in receivables from energy sales was due to higher revenues achieved in December 2016, mainly due to bilateral contracts, compared to the corresponding period of 2015. An increase was also recorded in receivables due from the GME, despite the reduction due to the start of the weekly settlement from December 1, 2016, which was actually more than offset by higher revenues from the sale of energy on the Power Exchange in the months of November and December 2016, compared to the corresponding months of 2015.

**Other current assets**

The item, amounting to Euro 38,464 thousand, mainly includes tax credits. The latter amounted to Euro 34,120 thousand at the reporting date and essentially include the receivable due from the Tax Authorities for VAT (Euro 27,100 thousand), in relation to which it is repayment is likely to take place within twelve months, in addition to accrued interest (Euro 55 thousand) and the tax credit, amounting to Euro 2,925 thousand, obtained from the transformation of deferred tax assets (recognised in 2012 and 2013 against the goodwill impairment charge) to tax credits.

This transformation, set out in Decree Law No. 225 of December 29, 2010, allows the Company to immediately recover the credit, in financial terms, through offsetting in the F24 forms, with no limit and with any kind of tax.

As regards VAT, in particular, credits for which a refund was requested relating to the 2nd quarter of 2016 (Euro 6,100 thousand) and 2015 (Euro 21,000 thousand) were recorded.



In 2016, credits relating to the 2nd quarter of 2014 (Euro 4,900 thousand) and to the 3rd quarter of 2014 (Euro 9,500 thousand) were collected, as well as the receivables assigned to Banca Sistema - as provided for in the Restructuring Agreement - relating to the year 2013 (Euro 34,900 thousand) and VAT credits relating to the 1st quarter of 2016 (Euro 6,500 thousand).

The item also includes loans to shareholders, amounting to Euro 2,351 thousand, relating to IRES (corporate income tax) refund requests for non-IRAP deductions, presented when the Company signed up to the tax transparency regime in accordance with art. 115 of the Consolidated Law on Income Tax.

**Other current financial assets**

Other current financial assets, amounting to Euro 2,562 thousand, refer essentially to shares of commissions for sureties paid and not yet accrued for Euro 2,533 thousand.

**Cash and cash equivalents**

The item, amounting to Euro 53,017 thousand includes, essentially, the positive balances of accounts held with leading banks.

## LIABILITIES

### 7. SHAREHOLDERS' EQUITY

For information on changes in shareholders' equity, please refer to the table of changes in shareholders' equity in these financial statements.

The share capital at December 31, 2016 is represented by 60,516,142 ordinary shares with a nominal value of Euro 1.00 each, fully paid up and held by ENGIE Italia S.p.A. (50%) and ENERGIA ITALIANA S.p.A. (50%).

The item "Other reserves" includes:

- the reserve from contribution of subscription of Junior PFIs amounting to a nominal Euro 284,386,754, approved at the Extraordinary Shareholders' Meeting on December 16, 2015 and recorded at fair value, amounting to Euro 204,000,000. This reserve is also reduced for the coverage of losses resolved at the same extraordinary shareholders' meeting amounting to Euro 88,735 thousand. The amount of this reserve at December 31, 2016, is therefore of Euro 115,265 thousand;
- the available reserve for coverage of losses amounts to Euro 68,200 thousand;
- the legal reserve amounts to Euro 695 thousand;
- the reserve for gains and losses on discounting, established as required by IAS 19 revised, is a negative Euro 457 thousand, net of the associated tax effect.



Details of items of shareholders' equity and an indication of their possibility of use and distribution, as well as their use in previous years, is provided below:

| Nature/description | Amount | Possibility of use | Available portion | Summary of uses made in the three previous years | |
|---|---|---|---|---|---|
| | | | | To cover losses | For other reasons |
| Share capital: | 60,516 | | | | |
| Share capital reserves: | | | | | |
| Reserve from contribution of subscription of Junior PFI | 115,265 | B | | | |
| Available reserve for coverage of losses | 68,200 | B | | | |
| Profit reserves: | | | | | |
| Legal reserve | 695 | B | | | |
| CFH and IAS 19 reserves | -457 | B | | | |
| Retained earnings | 13,196 | A,B,C | | | |
| **TOTAL RESERVES** | **196,898** | | | | |

**Key:**
A: for share capital increase
B: to cover losses
C: for distribution to shareholders



The Participating Financial instruments (PFIs), as defined in art. 2346, paragraph 6 of the Italian Civil Code, are financial instruments with equity or administrative rights, excluding voting rights at the shareholders' meeting. The articles of association govern their methods and conditions of issue, the rights of entitlement, sanctions for non-performance of the services and, if permitted, the methods of circulation. The PFIs are therefore included in the so-called hybrid financial instruments. This definition means instruments with similar characteristics, both shares and obligations in relation to the characteristics outlined for the instrument, but with their own identity.

Each financial instrument is measured according to its own characteristics, from which is also derived the valuation method that is better able to define the value. The features of the PFIs can be identified by their own regulation.

The Junior PFIs are represented by one or more registered paper certificates issued by the Company for a total of 284,386,754 certificates with a nominal value one euro each.

These certificates are fully regulated by the Articles of Association of the Company, and more precisely, Annex 1 "Regulations of the participating financial instruments of the Senior and Junior categories of Tirreno Power S.p.A.".

The main rights that such certificates incorporate are shown below:

- they are freely transferable securities;
- right of withdrawal in cases expressly provided for in the Articles of Association;

- right of co-sale in case of disposal of the shares by the shareholders;
- information and inspection rights;
- election of the Common Representative to protect the common interests of the holders of PFIs against the Company;
- participation in the meeting of the holders of PFIs which approves the resolutions of the shareholders' meeting of the Company in certain matters, including:
  - changes to PFI Regulations;
  - changes to specific clauses of the Articles of Association (Transferability of Shares, Rights of PFI Holders, the Drag Right on PFIs and connected Right of Co-sale, the Drag Right on the Shares, Purchase Option on PFIs, PFI Special Shareholders' Meeting, the number of Directors who make up the Board of Directors, Independent Directors, termination of office of Independent Directors, matters that require the approval of seven directors, gains - losses);
  - the issuance of new financial instruments;
  - the voluntary reduction of the share capital;
  - changes in the corporate purpose clause;
  - transformation, merger or spin-off;

PFIs do not, under any circumstances, entitle holders the right to attend or to vote at the ordinary and extraordinary shareholders' meeting of the Company.



The other main features are:

- the fixed rate (4%) remuneration and reimbursement up to the maximum of the initial contribution;
- privileges in the satisfaction of requirements in the event of Exit/M&A;
- remuneration and reimbursement defined by the Regulations annexed to the Articles of Association and subject to the verification of certain conditions and provided in the presence of approved dividends;
- provision is also made for privileges with respect to other categories of equity, while they are deferred with respect to the payment of financial payables and Senior PFIs.

**NON-CURRENT LIABILITIES**

**8. PAYABLES FOR LOANS**

Payables for loans refer to the Restated Facilities Agreement signed with the financial institutions on December 15, 2015.

The credit lines that compose it are indicated below:

- “Tranche A” of Euro 300,000 thousand, to be repaid based on a repayment plan starting from a date no earlier than June 30, 2017, remunerated at the Euribor rate + 2.07%, maturity in December 2022 (+ optional extension for another 2 years);
- “revolving credit facility” of Euro 50,000 thousand remunerated at the Euribor rate + 2% with the possibility of repayment and drawdown up to the maturity date set for December 2022 (+ optional extension for another 2 years);
- Tranche B of Euro 250,000 thousand (“convertible” credit line), remunerated at a rate of 3.42% PIK, maturity in December 2024 (with the possibility of optional extension for another 2 years);
- Hedging credit line of Euro 2,309 thousand repaid with repayment plan comprised of 6 semi-annual instalments starting from June 30, 2017, remunerated at the Euribor rate + 2%.



As for the Convertible credit line, the Company will have the right to arrange for its full or partial conversion in the following cases:

- to meet capital / financial requirements for operations;
- remedy capital deficiencies;
- address violations of the leverage ratio.

As at December 31, 2016, capitalised interest totalled Euro 15,111 thousand, of which Euro 6,210 thousand relating to the “term loan A” and Euro 8,901 thousand relating to the Convertible credit line.

The Restated Facilities Agreement requires, at the end of each half, the cash and cash equivalents exceeding Euro 50,000 thousand, to be used for the early repayment of the credit lines, starting with Tranche A and on a pro-rata basis on the expiries of the repayment plan, together with interest capitalised on the principal portion repaid early.

In relation to the above, the company reclassified to current liabilities the portion of debt, equal to surplus cash, repaid in February 2017, as indicated in the section “Significant events after the close of the period”.

## 9. PROVISIONS FOR RISKS AND CHARGES

Provisions for risks and charges amounted to Euro 101,798 thousand, an increase of Euro 29,621 thousand compared to December 31, 2015.

The size of the provision and the changes are summarised below:

| (in thousands of Euro) | 12.31.2015 | Provisions | Uses | Other changes | 12.31.2016 | of which current | of which non-current |
|---|---|---|---|---|---|---|---|
| **Dispute provision** | **3,275** | **88** | **(601)** | **(290)** | **2,473** | | **2,473** |
| **Provision for expenses for redundancy incentives** | **477** | **20,229** | **(817)** | | **19,889** | **19,889** | |
| **Provision for expenses for mobility incentives** | **911** | | | **(311)** | **600** | | **600** |
| **Provision for sundry risks:** | **67,514** | **14,755** | **(3,066)** | **(367)** | **78,836** | **7,785** | **71,051** |
| - site dismantling and restoration | *60,998* | *6,172* | *(1,544)* | | **65,625** | 5,408 | 59,164 |
| - other | *6,517* | *8,583* | *(1,522)* | *(367)* | **13,211** | 2,377 | 11,887 |
| **Total provisions for risks and charges** | **72,177** | **35,072** | **(4,483)** | **(967)** | **101,798** | **27,673** | **74,124** |

The **allocations** in the period, amounting to Euro 35,072 thousand, increased the provisions, mainly owing to the following:

- Euro 20,229 thousand relating to the expenses for the staff redundancy incentive, as detailed earlier in the section “Organisational Development and Industrial Relations”;
- Euro 5,055 thousand relating to Terna’s adjustment of the recalculation of 2012-2014 imbalance charges, already accounted for under other revenues, as highlighted in the relevant section. This provision was made to cover the risk, deemed likely, of having to repay the amount to Terna as a result of a number of appeals filed by the other operators;
- Euro 3,518 thousand for the adjustment of the estimated present value of the costs of dismantling coal plants;
- Euro 2,654 thousand for the recognition of borrowing costs on the provisions for decommissioning due to the discount rate of 5%;
- Euro 1,736 thousand for company performance-related pay and personnel meritocracy. The estimate was made for executives and middle managers on the basis of the MBOs assigned for 2016, and for employees and workers, using the amounts from the previous agreement signed (2015 bonuses), in the absence of a new agreement for 2016;
- Euro 630 thousand for the risk of higher IMU due to the municipalities of the Renewable Sources Sector;
- Euro 397 thousand for the floods in the Renewable Sources Sector;

As regards **uses**, in relation to payments made during the year, amounting to Euro 4,483 thousand, the following should be noted in particular:

- Euro 936 thousand for the dismantling activities in the extra combined cycle area of Naples;
- Euro 817 thousand for the redundancy incentive for personnel that left the company during the year;
- Euro 716 thousand for activities carried out at some hydroelectric plants, such as the rectification of the damages suffered because of the floods of 2014 and the repair of the channels;
- Euro 601 thousand for payment of the fees of the appointed professionals for ongoing disputes;
- Euro 431 thousand for demolition of the Torrevaldaliga tanks.

As regards **other changes**, the following should be noted in particular:

- Euro 300 thousand relates to the write-off of part of the provision as a result of the partial repayment of the escrow deposit following the favourable outcome to Tirreno Solar's ICI (municipal property tax) dispute;
- Euro 257 thousand for the write-off of the excess provision for disputes and litigation with respect to the commitments undertaken as a result of the reconciliation statement signed on 12/212016 concerning an asbestos-related dispute;
- Euro 311 thousand for the write-off of part of the mobility provision, due to the accrual of the pension right for 11 former employees who were beneficiaries of the 2014 mobility agreement.



The provision for other risks includes Euro 65,625 for the estimated discounted costs expected to be incurred at the end of production activities of the Torrevaldaliga, Naples and Vado Ligure sites due to abandonment of the area, dismantling, removal of structures and restoration of the site in the presence of current obligations.

The most significant outlays related to the dismantling and restoration works will be incurred over a period between 2020 and 2039.

The "dispute" provision includes liabilities that are estimated could result from ongoing legal disputes (mainly related to supply relations, work and the operation of the plants), according to the recommendations of the Company's internal and external legal representatives.

As for the asbestos dispute, for which Euro 1,924 thousand was allocated, the following should be noted:

1. as regards the application for social security benefits resulting from more than ten years of alleged exposure to asbestos and the assessment of the differential damage of 16% for occupational disease already recognised by INAIL (National Institution for Insurance against Accidents in the Workplace), at the current stage, the outcome of the dispute cannot be predicted albeit, in light of the case-law on the subject and the opinion of legal advisors assisting the Company, the risk of being the losing party can be classified as probable;

2. as regards the proceedings in which the Company is the defendant, together with Enel S.p.A. and Enel Production S.p.A., for the compensation for all non-pecuniary damages under art. 2087 of the Italian Civil Code that would have been suffered by a former employee based on the contraction of lung cancer attributable to occupational exposure to asbestos. At the hearing on December 21, 2016, based on the lateness in filing the expert's report with respect to the final deadline set by the Judge, the latter declared the court-appointed expert witness report to be invalid, ordering it to be renewed. The case was put back to the hearing of March 29, 2017.

3. lastly, for the two appeals filed by the heirs of two former employees who claim compensation for all the damages suffered before the Court of Savona, both iure proprio and iure hereditatis, as a result of the disease contracted by their relatives (pleural mesothelioma), for both, at the first hearing, the judge authorised the summonsing of ENEL SpA, Generali Italia S.p.A., the co-insurance companies and Inail, giving the parties the deadline for filing memorandums. At the hearing on December 1, 2015, the judge formulated a settlement proposal and admitted the items of evidence submitted by the claimants and by the Company. For one of these two proceedings, the claimant accepted the settlement proposal formulated by the judge, therefore, at the hearing on December 21, 2016 the case was settled and the judge declared the proceedings closed (in this regard, see the comments of the item "Other changes"). The sum paid by the claimant (Euro 50 thousand) was divided equally between TP (50%) and the insurance company (50%).

   For the other proceedings, following the hearing of all witnesses, both of the counterparty and of Tirreno Power, at the hearing on January 17, 2017, the claimant entered into the minutes its intention to accept the settlement proposal of the Judge already formulated at the hearing on December 1, 2015. The Judge adjourned the case to the hearing of March 28, 2017 to verify the outcome of the negotiations.



In consideration of the likely negative outcome of the aforementioned disputes, the relevant provision was allocated.

**Other information:**

As regards the asbestos-related dispute, the Company filed an appeal against the ruling issued by the Civil Court of Civitavecchia in relation to the case brought by the heirs of a former employee for compensation for alleged damages suffered as a result of the occupational exposure to asbestos.

It should be noted that said heirs may file a cross-appeal for the reform of the first instance judgment, by requesting the payment, by way of iure hereditatis compensation, of an additional amount. The next hearing will be held on June 19, 2017, in consideration of the non-obtainment of the official first instance file.

Again as regards the asbestos issue, TP filed an appeal against the first instance judgment issued by the Civil Court of Rome, Labour Section, in relation to the case lodged by the heirs of a former employee, to obtain compensation for all damages, financial and non-financial, both iure hereditatis in accordance with art. 2087 of the Italian Civil Code and iure proprio pursuant to art. 2043 of the Italian Civil Code, allegedly suffered due to occupational exposure of the deceased to asbestos, who died because of a pleural mesothelioma. The Rome Court of Appeal, by means of a judgment filed on March 14, 2016, rejected the appeal submitted by Tirreno Power, fully compensating all first instance legal costs.

On September 14, 2016, Tirreno Power filed an appeal against this judgment to the Court of Cassation. We are currently waiting for a hearing to be set.

### 10. POST-EMPLOYMENT AND OTHER EMPLOYEE BENEFITS

They amounted to Euro 17,136 thousand and reflect the severance pay and other benefits accrued at year-end by employees that are valued according to the actuarial criteria of IAS 19 laid out for defined benefit plans. In particular, as regards the economic and financial scenario, the parameters used for the evaluation are as follows:

| TFR | 2016 | 2015 |
|---|---|---|
| Annual technical discount rate | 1,31% | 2,03% |
| Annual inflation rate | 1,50% | 1,50% |
| Annual rate of increase in post-employment benefits | 2,63% | 2,62% |

| Other employee benefits | 2016 | 2015 |
|---|---|---|
| Annual technical discount rate | 1,31% | 2,03% |
| Annual rate of salary increase | 0,50% | 0,50% |



The following table illustrates the changes:

| (in thousands of Euro) | TFR | Energy discount for retirees | Substitute indemnity - Electricity discount | Additional months' pay | Loyalty bonuses | BOOK VALUE |
|---|---|---|---|---|---|---|
| **Values at 12.31.2015 (A)** | **6,875** | **8,335** | **763** | **726** | **488** | **17,188** |
| ***Curtailment*** | ***-257*** | | ***32*** | ***-255*** | | ***-480*** |
| - Provisions | | | | 19 | 17 | 36 |
| - Financial expenses (+) | 108 | 131 | 12 | 12 | 6 | 269 |
| - Gains (losses) from discounting (-/+) | 337 | 166 | 42 | 80 | 1 | 626 |
| -Uses (-) | -67 | -395 | 0 | 0 | -39 | -501 |
| **Total changes (B)** | 121 | -98 | 86 | -144 | -15 | **-51** |
| **Values at 12.31.2016 (A+B)** | **6,996** | **8,236** | **850** | **582** | **472** | **17,136** |

The Curtailment reflects the effects of the Restructuring Plan targeted at managing redundant staff. For details, please refer to the Management Report. The overall positive effect, amounting to Euro 480 thousand, is recorded under Financial expenses.

Costs for employee benefits were also recognised in the year, amounting to Euro 305 thousand, of which Euro 269 thousand for interest recorded under financial expenses and Euro 36 thousand recorded under personnel costs.

Lastly, losses from discounting amounted to Euro 625 thousand and are recognised in the shareholders' equity reserve (Euro 474 thousand net of taxes), excluding those relating to loyalty bonuses which are booked directly to the income statement.

As a result of the issuance of the new IAS 19 revised, the additional information is summarised in the tables below:

**Sensitivity analysis of the main valuation parameters on data as at 12.31.2016**

| | TFR | Additional Months' pay | Energy discount | Indemnity Energy discount |
|---|---|---|---|---|
| Inflation rate +0.25% | 7.050.678,19 | N/A | N/A | N/A |
| Inflation rate -0.25% | 6.927.460,91 | N/A | N/A | N/A |
| Discount rate +0.25% | 6.890.581,18 | 568.569,37 | 7.977.985,72 | 839.076,07 |
| Discount rate -0.25% | 7.089.825,40 | 595.677,05 | 8.506.010,59 | 861.720,24 |

| | TFR | Additional Months' pay | Energy discount | Indemnity Energy discount |
|---|---|---|---|---|
| Pro future service cost | - | 7.348,68 | - | - |
| Duration of the plan | 9,8 | 7,5 | 13 | 6,5 |

The number of employees by category is shown in the following table:

| (units) | 12.31.2015 | Hires | Exits | Other / Reclassifications | 12.31.2016 |
|---|---|---|---|---|---|
| Executives and Middle Managers | 44 | | 2 | 2 | 44 |
| Employees | 225 | | 3 | 1 | 223 |
| Workers | 117 | | 10 | -3 | 104 |
| **Total** | **386** | **0** | **15** | **0** | **371** |

### 11. DEFERRED TAX LIABILITIES

The item includes deferred taxes relating to costs not charged to the income statement, but deducted from taxable income in the tax return, as detailed in the following table:

| (in thousands of Euro) | SITUATION AT 12.31.2015 | SITUATION AT 12.31.2016 | | | |
|---|---|---|---|---|---|
| | Balance | Provisions | Uses | Other changes | Balance |
| **Deferred tax liabilities** | | | | | |
| Amortisation | 38.519 | | (1.199) | | 37.320 |
| FV IAS 19 to shareholders' equity reserve | 69 | | | | 69 |
| **Total deferred tax liabilities** | **38.588** | | **(1.199)** | | **37.389** |

The uses of the item "Amortisation" refer to the completion of tax amortisation for IRES purposes.

### 12. OTHER NON-CURRENT LIABILITIES

The item, amounting to Euro 3,117 thousand, includes the non-current portion of the debt to the MATTM resulting from the settlement act signed in 2011 by means of which Tirreno Power was expressly and definitively freed from any obligation or liability in connection with the design and implementation of measures for the safety, environmental remediation and restoration of groundwater, surface water and marine sediments overlooking the site of Naples.



### 13. CURRENT LIABILITIES

| (in thousands of Euro) | 12.31.2016 | 12.31.2015 | Changes |
|---|---|---|---|
| Payables for loans | 8,083 | 0 | 8,083 |
| Provisions for risks and charges | 27,673 | 6,426 | 21,248 |
| Trade payables | 154,364 | 85,253 | 69,111 |
| Other current liabilities | 15,214 | 18,996 | (3,782) |
| Short-term financial liabilities | 23 | 31,089 | (31,066) |
| **Total current liabilities** | **205,358** | **141,764** | **63,594** |

Details of the individual items are outlined below:

#### Payables for loans

The item Payables for loans refer to the Restated Facilities Agreement signed with the financial institutions on December 15, 2015, as detailed in note 8.

**Provisions for risks and charges**

This item includes current liabilities for business expenses and risk, commented on in detail in note 9.

**Trade payables**

"Trade payables", amounting to Euro 154,364 thousand, relate to supplies of fuel, materials and equipment, tenders and services, as well as debts to TERNA and GME for supplies and activities carried out by December 31, 2016. The maturities of these debts are generally comprised between 30 and 120 days.

The increase of Euro 69,111 thousand is attributable mainly to:

- higher payables due to the GME for the purchase of energy on the Power Exchange (Euro 44,186 thousand). The effect of the start of the weekly settlement with the GME from December 1, 2016, was more than offset by higher revenues from the sale of energy on the Power Exchange in the months of November and December 2016, compared to the same period of 2015;
- higher payables for gas purchase (amounting to Euro 11,676 thousand);
- higher payables due to Terna for the purchase of energy (Euro 10,751 thousand), as a result of greater trading on the Dispatching Services Market.

**Other current liabilities**

Other current liabilities, amounting to Euro 15,214 thousand, mainly refer to the payable relating to the to the expense pertaining to the year for $CO_2$ emissions rights (Euro 11,008 thousand) valued at weighted average purchase price.



The item also includes payables to employees and payables to social security, welfare and insurance institutions.

The table below provides a breakdown:

| (in thousands of Euro) | 12.31.2016 | 12.31.2015 | Changes |
|---|---|---|---|
| Payables for green certificates and CO2 emission rights | 11,008 | 11,905 | (897) |
| Other taxes | 1,029 | 1,186 | (157) |
| Payables due to social security institutions | 1,633 | 2,313 | (680) |
| Payables due to personnel | 834 | 2,870 | (2,036) |
| Other | 710 | 721 | (11) |
| **Total other current liabilities** | **15,214** | **18,996** | **(3,782)** |

The decrease in the item payables to employees is mainly attributable to the recognition of performance-related pay under provisions for risks and charges (amounting to Euro 1,736 thousand), unlike what was done in 2015, given that a trade union agreement has still not been reached by the parties which defines the criteria and base value to be allocated to company bonuses for the year.

### Short-term financial liabilities

Current financial liabilities, amounting to Euro 23 thousand, refer exclusively to the portion of interest of the 2nd half of 2016 of the Hedging credit line of the Restated Facilities Agreement.

## COMMITMENTS AND GUARANTEES

Commitments to suppliers are detailed below:

| (in thousands of Euro) | 12.31.2016 | 12.31.2015 | Changes |
|---|---|---|---|
| Tenders and miscellaneous supplies | 65,799 | 63,122 | 2,677 |
| Purchase of thermal fuel | 39,645 | 54,799 | (15,154) |
| **Total commitments to suppliers** | **105,444** | **117,921** | **(12,477)** |



Commitments for the purchase of thermal fuel relate exclusively to the term fixed on natural gas purchase contracts.

The sureties requested in favour of third parties, amounting to Euro 178,801 thousand, concern policies issued by banks and insurance companies, at the request of the Company, and relate mainly to the guarantee of the VAT credit (Euro 144,366 thousand), the participation in the energy markets (Euro 29,000 thousand), as well as the guarantee for state concessions (Euro 2,227 thousand).

## Notes to the Income Statement

### 14. REVENUES

The table below provides a breakdown of sales revenues:

| (in thousands of euro) | 12.31.2016 | 12.31.2015 | CHANGES | CHANGES % |
|---|---|---|---|---|
| **Sale of energy:** | | | | |
| - Power Exchange | 397,706 | 263,120 | 134,586 | 51% |
| - Free market | 333,433 | 161,216 | 172,217 | 107% |
| - incentivised contributions - ex Green Certificates | 7,201 | 0 | 7,201 | n.a. |
| - photovoltaic contributions | 31 | 35 | (4) | -11% |
| **Total energy sales:** | **738,371** | **424,371** | **314,000** | 74% |
| **Other sales and services** | 109 | 47 | 62 | 132% |
| **Insurance reimbursements** | 0 | 999 | (999) | n.a. |
| **Total revenues from sales** | **738,480** | **425,417** | **313,063** | **74%** |

Tirreno Power's commercial portfolio consists of two types of customers, customers that operate in the free market and those, instead, that operate on the power exchange. Revenues from Power Exchange sales include the results of trading on the dispatching services market. Sales on the free market instead refer to physical bilateral contracts.

The increase relates to the higher sales volumes attributable to the trading in the Dispatching Services Market and higher sales volumes on the Day-ahead market as a result of the higher PUN level recorded in the last few months of the year, coinciding with the shutdowns of a number of French nuclear power plants for maintenance.

As set forth in Ministerial Decree dated July 6, 2012, the Company recorded contribution incentives (former Green Certificates) for the first year. In fact, the decree requires a replacement incentive to be recognised, after December 31, 2015, to production of electricity from renewable plants in operation as at December 31, 2012 already admitted to the recognition of Green Certificates. This incentive is disbursed by the GSE on a quarterly basis within the second quarter after the relevant one.

The item "Other sales and services" refers mainly to the sale of warehouse materials to third parties.



### 15. OTHER REVENUES

"Other revenues" amounting to Euro 10,262 thousand refer primarily:

- for Euro 5,229 thousand, to the adjustment by Terna of the recalculation of imbalance charges for 2012, 2013 and 2014. An amount was allocated to the provisions for risks and charges to cover the risk of having to repay said amount to Terna as a result of a number of appeals filed by the other operators;
- for Euro 1,551 thousand, to adjustments to energy items of previous years, mainly due to the definition by Terna of the adjustment of the second component of the 2011 capacity payment (Euro 1,121 thousand);

- for Euro 1,255 thousand, to the reduction in liabilities to employees for bonuses and company welfare relating to previous years;
- for Euro 967 thousand to the transfer of provisions for risks, mainly due to the partial repayment of the Escrow security deposit of Tirreno Solar for Euro 300 thousand, adjustment of the redundancy provision for Euro 311 thousand plus the adjustment, amounting to Euro 290 thousand, of the disputes and litigation provision, relating to expenses for ongoing proceedings and the related legal costs**.**

## 16. OWN WORK CAPITALISED

The item totalled Euro 286 thousand, relating to the capitalisation of materials taken from the warehouse, used for the Major Inspections capitalised during the year.

## 17. CONSUMPTION OF RAW MATERIALS

| (in thousands of euro) | 12.31.2016 | 12.31.2015 | CHANGES | CHANGES % |
|---|---|---|---|---|
| Energy purchased on the Electricity Market | 393,619 | 191,869 | 201,750 | 105% |
| Purchase of fuel for heat production | 231,093 | 161,513 | 69,580 | 43% |
| Purchase of materials and other equipment | 2,908 | 2,664 | 244 | 9% |
| Change in fuel stocks | 1 | 173 | (172) | -99% |
| Change in other stocks | (40) | (219) | 179 | -82% |
| **Total consumption of raw materials** | **627,581** | **356,000** | **271,581** | **76%** |



The purchase of fuels is related, exclusively, to the natural gas supply contracts.

The increase relates mainly to higher energy purchases to meet the sales under contract in the hours when the electricity purchase prices were lower than the marginal costs of production and also to higher purchases of methane gas in relation to greater volumes of energy produced.

For more details, please refer to the Management report.

## 18. PERSONNEL COSTS

Labour costs amounted to Euro 23,750 thousand, a decrease of Euro 3,269 thousand compared to the figure recorded in 2015.

The decrease is attributable primarily to the recognition of performance-related pay (Euro 1,736 thousand) under provisions, unlike what was done in 2015, as already outlined in note no. 13 to the item “Other current liabilities”, as well as the effects of the fall in average volumes compared to 2015.

### 19. SERVICE COSTS

Service costs amounted to Euro 23,157 thousand, down by Euro 5,943 thousand compared to December 31, 2015 and include the following types of costs:

| (in thousands of euro) | 12.31.2016 | 12.31.2015 | CHANGES | CHANGES % |
|---|---|---|---|---|
| Costs of services and tenders | 12,879 | 18,104 | (5,224) | -29% |
| Expenses for transactions on the Electricity Market | 1,700 | 1,307 | 393 | 30% |
| Insurance costs | 2,715 | 2,880 | (165) | -6% |
| Security, cleaning and other building costs | 666 | 809 | (143) | -18% |
| Waste disposal | 605 | 646 | (42) | -6% |
| IT services | 1,400 | 1,252 | 148 | 12% |
| Telephone and data transmission expenses | 740 | 785 | (45) | -6% |
| Other services | 2,452 | 3,317 | (866) | -26% |
| **Total service costs** | **23,157** | **29,100** | **(5,943)** | **-20%** |

The reduction in service and tender costs refers mainly to the decrease in costs compared to those incurred in the previous year, in relation to the Debt Restructuring Agreement.

Additional savings in service costs have also been made possible by a thorough analysis of all the contracts in place, with subsequent initiatives involving new contracts and to increase the efficiency of the activities involved in the contracts.

"Other services" mainly relate to costs for studies, consulting and professional services (Euro 1,411 thousand), expenses for travel and training (Euro 319 thousand), the fees of the Statutory Auditors (Euro 284 thousand), as well as the remuneration to the auditing firm (Euro 91 thousand).



### 20. OTHER OPERATING COSTS

Other operating costs amounted to Euro 52,743 thousand, up by Euro 15,738 thousand compared to December 31, 2015.

The following table shows a breakdown of other operating costs:

| (in thousands of euro) | 12.31.2016 | 12.31.2015 | CHANGES | CHANGES % |
|---|---|---|---|---|
| Contributions and fees | 3,262 | 3,318 | (56) | -2% |
| Provisions for risks and charges | 32,540 | 3,314 | 29,226 | 882% |
| Adjustment of value of materials and raw materials | 364 | 5,690 | (5,326) | n.a. |
| Expenses for green certificates and CO2 rights | 11,008 | 15,631 | (4,622) | -30% |
| ICI (municipal property tax) and other taxes and duties | 3,386 | 7,419 | (4,033) | -54% |
| Other expenses | 2,181 | 1,633 | 549 | 34% |
| **Total operating costs** | **52,743** | **37,005** | **15,738** | **43%** |

In particular, higher expenses were recorded for emissions rights (Euro 3,435 thousand) as a result of higher emissions in the period (approx. 1,053 Kton). This increase was offset by lower expenses for Green Certificates of Euro 8,058 thousand, due to the end of the obligation in 2015.

In addition, IMU (single municipal tax) fell by Euro 3,607 compared to 2015, due to the recalculation of the tax based on the exclusion of the so-called "imbullonati" (machinery or plants fixed to the ground or incorporated in the construction but which, at the same time, can be dismantled and transferred from one site to another) from cadastral rents.

The sizeable increase in provisions for risks and charges is mainly attributable, for Euro 20,229 thousand, to expenses for staff redundancy incentives; for Euro 5,055 thousand to the adjustment received by Terna of the Imbalance Charges relating to previous years and, for Euro 3,518 thousand, to the adjustment of the estimated present value of the costs of dismantling of coal-powered plants. For more details, please refer to note no. 9.

## 21. AMORTISATION, DEPRECIATION AND WRITE-DOWNS

The item refers to the depreciation/amortisation in the period, calculated on the basis of economic-technical rates, totalling Euro 59,976 thousand.

The increase in amortisation/depreciation compared to 2015 is mainly due to the Major Inspection of VL5 capitalised in May 2016.

The table below sets out the depreciation by type of asset compared with data for the previous year:

| (in thousands of euro) | 12.31.2016 | 12.31.2015 | CHANGES | CHANGES % |
|---|---|---|---|---|
| Depreciation of buildings | 7,674 | 7,668 | 5 | 0% |
| Depreciation of plant and equipment | 51,263 | 47,865 | 3,398 | 7% |
| Depreciation of industrial equipment | 198 | 199 | (1) | -1% |
| Depreciation of other assets | 256 | 274 | (18) | -7% |
| Amortisation of intangible fixed assets | 586 | 983 | (397) | -40% |
| Write-downs | 0 | 691 | (691) | -100% |
| **Total** | **59,976** | **57,680** | **2,296** | **3.98%** |



## 22. FINANCIAL EXPENSES

Financial expenses amounted to Euro 20,938 thousand, up by Euro 8,925 thousand compared to 2015. The variation is primarily attributable to the higher average cost of debt relating to the credit lines set out in the debt Restructuring Agreement reached with banks last year (average interest rate of 2.63%), compared to those of 2015 relating to the previous loan agreement (stipulated in 2007, with an average interest rate of 0.45%).

The following table shows a breakdown:

| (in thousands of euro) | 12.31.2016 | 12.31.2015 | CHANGES | CHANGES % |
|---|---|---|---|---|
| Interest expenses and charges on loans | 15,665 | 3,853 | 11,812 | 307% |
| Interest expenses for decommissioning, post-employment and other benefits | 2,647 | 3,107 | (460) | -15% |
| Other financial expenses | 2,626 | 5,053 | (2,427) | -48% |
| **Total financial expenses** | **20,938** | **12,013** | **8,925** | **74%** |

"Interest expense and charges on loans" relate exclusively to interest and fees accrued on the new loan.

"Interest expense for decommissioning", amounting to Euro 2,857 thousand, was mainly offset by the site dismantling and restoration provisions, while the "interest on post-employment and other benefits" recognised in application of IAS 19, were a positive Euro 210 thousand.

The item "Other financial charges" refers essentially to the commissions on sureties of Euro 2,375 thousand, financial commissions paid to Banca Sistema for the transfer of the VAT credit for 2013 and 2014 (Euro 159 thousand); as well as negative exchange differences of Euro 126 thousand.

## 23. FINANCIAL INCOME

Financial income amounted to Euro 427 thousand, a decrease of Euro 86,575 thousand compared to December 31, 2015.

The table below shows a breakdown:

| (in thousands of euro) | 12.31.2016 | 12.31.2015 | CHANGES | CHANGES % |
|---|---|---|---|---|
| Interest on receivables due from the tax authorities | 285 | 691 | (406) | -59% |
| Interest income on bank current accounts | 28 | 107 | (79) | -73% |
| Other financial income | 113 | 86,204 | (86,090) | n.a. |
| **Total financial income** | **427** | **87,001** | **(86,575)** | **-100%** |



The decrease is attributable mainly to the recognition of the following in 2015:

- Euro 80,387 thousand relating to the difference between the nominal value of the Participating Financial instruments (Junior PFIs) (Euro 284,387 thousand) and the related fair value (Euro 204,000 thousand), as stated in the appraisal of an independent expert, recognised, in compliance with the provisions of IFRIC 19, following the issue of the PFIs resolved by the Extraordinary Shareholders' Meeting of December 16, 2015, subscribed by the financial institutions as set forth in the Restructuring Agreement;
- Euro 5,430 thousand related to the write-off of 55% of the total value of financial payables for interest expense on hedging contracts of previous years, as set out in the Debt Restructuring Agreement.

"Other financial income" refers mainly to the positive differences relating to the payment of trade payables in dollars.

## 24. INCOME TAX

Income taxes were determined by a proper and prudent interpretation of current tax legislation at the date of these financial statements and according to the specific methods required by IAS 12.

The detailed breakdown of the estimated taxes for the year, compared with the previous year is shown below:

| (in thousands of euro) | 12.31.2016 | 12.31.2015 | CHANGES | CHANGES % |
|---|---|---|---|---|
| Deferred tax assets | (1,199) | (1,016) | (183) | 18% |
| Deferred tax liabilities | 1,199 | 1,016 | 183 | 18% |
| **Total** | **0** | **0** | **0** | **n.a.** |

As for the recognition of deferred tax assets and liabilities, please refer to the comments on the respective balance sheet items.

## 26. EARNINGS PER SHARE



For the calculation of earnings per share, the net profit attributed to shareholders was considered. The denominator used in the calculation is the number of shares issued, in the calculation of both basic and diluted earnings per share, as there are no dilutive effects as at December 31, 2016 or December 31, 2015.

| (in thousands of Euro) | 12.31.2016 | 12.31.2015 | Changes |
|---|---|---|---|
| Tenders and miscellaneous supplies | 65,799 | 63,122 | 2,677 |
| Purchase of thermal fuel | 39,645 | 54,799 | (15,154) |
| **Total commitments to suppliers** | **105,444** | **117,921** | **(12,477)** |

## 27. NET FINANCIAL POSITION

The net financial position at December 31, 2016 is detailed as follows:

| | Thousands of Euro | as at 12.31.2016 | as at 12.31.2015 | difference |
|---|---|---|---|---|
| A | Cash at bank and in hand | 16 | 18 | *(2)* |
| B | Bank deposits | 53,001 | 68,620 | *(15,619)* |
| C | Securities | - | - | - |
| **D** | **Cash and cash equivalents (A+B+C)** | **53,017** | **68,638** | ***(15,621)*** |
| **E** | **Current financial receivables** | **-** | **-** | **-** |
| F | Current bank payables | - | | - |
| G | Current portion of non-current debt | | | - |
| H | Other current financial liabilities | (8,106) | (31,080) | *22,974* |
| **I** | **Total short-term financial liabilities (F+G+H)** | **(8,106)** | **(31,080)** | ***22,974*** |
| **J** | **Net current financial position (D+E+I)** | **44,911** | **37,558** | ***7,353*** |
| **K** | **Non-current financial receivables** | **-** | **-** | **-** |
| L | Non-current bank payables | (559,337) | (602,660) | *43,323* |
| M | Other non-current payables | - | - | - |
| **N** | **Non-current financial debt (L+M)** | **(559,337)** | **(602,660)** | ***43,323*** |
| **O** | **Net non-current financial position (K+N)** | **(559,337)** | **(602,660)** | ***43,323*** |
| **P** | **OVERALL NET FINANCIAL POSITION (J+O)** | **(514,426)** | **(565,102)** | ***50,676*** |

## 28. OTHER INFORMATION:

### Cash flows

| Thousands of Euro | 12.31.2016 | 12.31.2015 | difference |
|---|---|---|---|
| **Opening cash and cash equivalents** | **68,638** | **46,347** | **22,291** |
| Cash Flow from operating activities | 91,509 | (36,536) | 128,046 |
| Cash Flow from investment activities | (40,833) | (4,928) | (35,906) |
| Cash Flow from financing activities | (66,297) | 63,755 | (130,052) |
| **Closing cash and cash equivalents** | **53,017** | **68,638** | **(15,621)** |

The cash flow from operations stood at Euro 91,509 thousand, marking an increase of Euro 128,046 thousand compared to the previous year. The increase is attributable to the better economic results and the collection of VAT credits totalling Euro 67,853 thousand.

The cash flow from operations allowed the coverage of investment activities (Euro 40,833 thousand) as well as a reduction in net financial debt of Euro 66,297 thousand (the "Revolving" line was repaid in March 2016 for Euro 50,000 thousand).

Cash and cash equivalents amounted to Euro 68,638 thousand at December 31, 2015, a decrease of Euro 15,621 thousand as a result of the aforementioned changes, and amounted to Euro 53,017 thousand at December 31, 2016.



Net financial debt decreased from Euro 565,102 thousand at December 31, 2015 to Euro 514,426 thousand at December 31, 2016.

### 28.1 Relationships with subsidiaries, affiliates, parent companies and companies controlled by the latter

Any transactions carried out with other related parties, as described below, were carried out under normal market conditions and in the interest of each company:

| (thousands of Euro) | Receivables 12.31.2016 | Payables 12.31.2016 | Costs 12.31.2016 | Revenues 12.31.2016 |
|---|---|---|---|---|
| **Financial:** | | | | |
| **ENGIE ITALIA S.p.A.** | | | | |
| Tax transparency | 1,210 | | | |
| **ENERGIA ITALIANA S.p.A.** | | | | |
| Tax transparency | 1,141 | | | |
| **Trade:** | | | | |
| Sorgenia S.p.A. | | | | 51 |
| Sorgenia Trading Spa | | 304 | 5,683 | |

Loans to shareholders, amounting to Euro 2,351 thousand, relate to IRES (corporate income tax) refund requests for non-IRAP deductions, presented when the Company signed up to the tax transparency regime in accordance with art. 115 of the Consolidated Law on Income Tax.

Commercial items due to Sorgenia Trading S.p.A. instead relate to the purchase of 103 GWh of energy. The payable as at December 31, 2016 is the net figure from the supply value and the effect of the Credit Support Agreement (CSA).

### 28.2 Contingent assets and liabilities

There are no additional contingent assets and liabilities to be highlighted arising from events that occurred during the year 2016, in addition to what has already been reported in the Management Report and in the notes.



With regards to the contingent liabilities arising from the criminal proceedings pending at the Prosecutor's Office of Savona, the preliminary investigations are closed as of today under art. 415 bis c.p.p. (Code of Criminal Procedure) and there are no changes with respect to the update provided in the section of the management report "Operating structure."

Moreover, also taking into account the opinion of the legal advisors assisting the Company, the lack of claims for damages accompanied by disclosure of the demonstration and quantification criteria of the damages caused by the disputed conduct and the uncertainty about the number of potential plaintiffs eventually entitled to appear and that may be accepted by the Court in the criminal proceedings, do not currently make it possible to foresee any consequence for damages deriving from the criminal proceedings in progress.

### 28.3 Atypical and unusual transactions

There were no atypical or unusual transactions, or outside normal company operations or capable of significantly impacting the Company's financial position.

### 28.4 Subsequent events

Please refer to the relevant section of the Management report.

Building a better working world

# Tirreno Power S.p.A.

**Financial statements as at December 31, 2016**

**Independent auditor's report in accordance with article 14 of Legislative Decree n. 39, dated January 27, 2010**

**(Translation from the original Italian text)**

EY S.p.A.
Via Po, 32
00198 Roma

Tel: +39 06 324751
Fax: +39 06 32475504
ey.com

# Independent auditor's report in accordance with article 14 of Legislative Decree n. 39, dated January 27, 2010
# (Translation from the original Italian text)

To the Shareholders of
Tirreno Power S.p.A.

## Report on the financial statements

We have audited the accompanying financial statements of Tirreno Power S.p.A., which comprise the balance sheet as at December 31, 2016, the income statement, the statement of comprehensive income/(loss), the cash flow statement, the statement of changes in shareholders' equity for the year then ended, a summary of significant accounting policies and other explanatory notes.

### Directors' responsibility for the financial statements

The Directors of Tirreno Power S.p.A. are responsible for the preparation of these financial statements that give a true and fair view in accordance with International Financial Reporting Standards as adopted by the European Union.

### Auditor's responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing (ISA Italia) implemented in accordance with article 11 of Legislative Decree n. 39, dated January 27, 2010. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's professional judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation of the financial statements that give a true and fair view in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by Directors, as well as evaluating the overall presentation of the financial statements.

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

### Opinion

In our opinion, the financial statements give a true and fair view of the financial position of Tirreno Power S.p.A. as at December 31, 2016, and of its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards as adopted by the European Union.

EY S.p.A.
Sede Legale: Via Po, 32 - 00198 Roma
Capitale Sociale deliberato Euro 3.250.000,00, sottoscritto e versato Euro 2.950.000,00 i.v.
Iscritta alla S.O. del Registro delle Imprese presso la C.C.I.A.A. di Roma
Codice fiscale e numero di iscrizione 00434000584 - numero R.E.A. 250904
P.IVA 00891231003
Iscritta al Registro Revisori Legali al n. 70945 Pubblicato sulla G.U. Suppl. 13 - IV Serie Speciale del 17/2/1998
Iscritta all'Albo Speciale delle società di revisione
Consob al progressivo n. 2 delibera n.10831 del 16/7/1997

A member firm of Ernst & Young Global Limited

## Emphasis of matters

Without qualifying our opinion, we draw attention to:

a. the explanatory note "Assessment of the going concern assumption" for the events and results which have affected the fiscal year 2016, the assumptions included in the Business and Financial Plan utilized for the Restructuring Agreement and the uncertainties related to it. In particular, the Directors report that they have prepared the financial statements on the going concern basis, provided that such basis have to be considered, as necessary, subject to the realization of the assumptions set out in the Plan, according to the assumed methods and timing of implementation;
b. the paragraphs "Operating Structure" of the Management Report and to the explanatory note "Contingent assets and liabilities", which describe the events and the Directors' assessments on the criminal proceedings started by the Prosecutor's Office of Savona, concerning the plant in Vado Ligure.

# Report on other legal and regulatory requirements

## Opinion on the consistency of the Management Report with the financial statements

We have performed the procedures required under audit standard SA Italia n. 720B in order to express an opinion, as required by law, on the consistency of the Management Report with the financial statements. The Directors of Tirreno Power S.p.A. are responsible for the preparation of the Management Report in accordance with the applicable laws and regulations. In our opinion the Management Report is consistent with the financial statements of Tirreno Power S.p.A. as at December 31, 2016.

Rome, April 7, 2017

EY S.p.A.

Signed by: Beatrice Amaturo, partner

*This report has been translated into the English language solely for the convenience of international readers.*