

Exhibit 12

AUDIT REPORT

IBERDROLA, S.A.

**Annual Accounts and Management Report for the year
ended 31 December 2006**

**(Translation of a report and annual accounts originally issued in Spanish.
In the event of discrepancy, the Spanish-language version prevails)**

AUDIT REPORT ON THE ANNUAL ACCOUNTS

Translation of a report and annual accounts originally issued in Spanish. In the event of discrepancy,
the Spanish-language version prevails (See Note 24)

To the Shareholders of
IBERDROLA, S.A.

We have audited the annual accounts of IBERDROLA, S.A., which consist of the balance sheet at December 31, 2006, the income statement and the notes thereto for the year then ended, the preparation of which is the responsibility of the Company's directors. Our responsibility is to express an opinion on the aforementioned annual accounts taken as a whole, based upon work performed in accordance with auditing standards generally accepted in Spain, which require the examination, through the performance of selective tests, of the evidence supporting the annual accounts, and the evaluation of their presentation, of the accounting principles applied and of the estimates made. Our work did not include the audit of the 2006 annual accounts of several subsidiaries, whose net investment value and reversal of the long-term investments provision in the accompanying annual accounts amount to 6% and 9%, respectively, of the Company's total assets and net profit. The annual accounts of these companies have been audited by other auditors (see Appendix for detail) and our opinion in this audit report on the annual accounts of IBERDROLA, S.A. with respect to its investment in these companies is based only on the audit report of the other auditors.

In accordance with Spanish mercantile law, for comparative purposes the Company's directors have included for each of the captions included in the balance sheet, the income statement and the statement of source and application of funds, in addition to the figures of 2006, those of 2005. Our opinion refers only to the annual accounts for 2006. On February 23, 2006, other auditors issued their audit report on the 2005 annual accounts, in which they expressed an unqualified opinion.

In our opinion, based on our audit and on the reports of the other auditors, the accompanying 2006 annual accounts give a true and fair view, in all material respects, of the net equity and financial position of IBERDROLA, S.A. at December 31, 2006 and the results of its operations and the source and application of funds for the year then ended, and contain the required information necessary for their adequate interpretation and comprehension, in conformity with accounting principles and criteria generally accepted in Spain, applied on a basis consistent with those of the preceding year.

The accompanying management report for the year ended December 31, 2006 contains such explanations as the directors consider appropriate concerning the situation of the Company, the evolution of its business and other matters, and is not an integral part of the annual accounts. We have checked that the accounting information included in the management report mentioned above agrees with the annual accounts for the year ended December 31, 2006. Our work as auditors is limited to verifying the management report in accordance with the scope mentioned in this paragraph, and does not include the review of information other than that obtained from the Company's accounting records.

INSTITUTO DE
CONTABLES PÚBLICOS
DE ESPAÑA

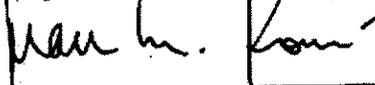
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ERNST & YOUNG, S.L.

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ERNST & YOUNG, S.L.
(Registered in ROAC under nº 90530)



Juan María Román Gonçalves

February 21, 2007

**ANNUAL ACCOUNTS AND MANAGEMENT REPORT
FOR THE YEAR ENDED
31 DECEMBER 2006**

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Translation of annual accounts originally issued in Spanish and prepared in accordance with accounting principles generally accepted in Spain (see Note 24). In the event of a discrepancy, the Spanish-language version prevails.

IBERDROLA, S.A.
Balance sheets
at 31 December

	Thousands of euros	
	2006	2005 (*)
ASSETS		
Fixed and other non-current assets		
Intangible assets (Note 5)		
Research and development expenses	-	6,271
Concessions, patents, licenses, trademarks and other	44,649	44,703
Computer software	210,265	201,841
Rights on leased assets	104,133	113,410
Accumulated amortisation	<u>(181,357)</u>	<u>(176,857)</u>
	177,690	189,368
Tangible fixed assets (Note 6)		
Land and structures	208,706	195,676
Technical installations and machinery	1,005,222	978,710
Other fixtures, tools and furniture	248,293	221,761
Technical installations in progress	27,717	22,651
Advances and other construction in progress	11,270	9,953
Allowances	(29,345)	(32,628)
Accumulated amortisation	<u>(815,476)</u>	<u>(773,291)</u>
	656,387	622,832
Long-term financial investments (Note 7)		
Holdings in Group companies	9,196,552	8,926,657
Holdings in associated companies	799,944	296,574
Long-term investment securities	142,726	187,899
Loans to Group and associated companies (Note 13)	1,575,604	3,552,169
Other loans	49,953	9,123
Long-term taxes receivable (Note 14)	226,535	300,092
Long-term deposits and guarantees given	352	19
Account receivable due to shortfall in revenues	586,647	1,259,115
Allowances	<u>(290,420)</u>	<u>(456,123)</u>
	12,287,893	14,075,525
Long-term trade accounts receivable (Note 7)	25,972	42,524
Treasury stock (Note 8)	1,045	1,151
Total fixed and other non current assets	13,148,987	14,931,400
Deferred charges	85,136	107,925
Current assets		
Inventories	84,311	48,725
Accounts receivable		
Trade receivables for sales and services	682,282	429,598
Unbilled power supplied	63,431	161,872
Receivable from Group companies (Note 13)	5,893,161	4,600,798
Receivable from associated companies (Note 13)	14,998	14,750
Sundry accounts receivable	84,591	34,244
Employee receivables	441	251
Taxes receivable (Note 14)	254,431	362,516
Allowances	<u>(38,334)</u>	<u>(15,190)</u>
	6,955,001	5,588,839
Short-term financial investments (Note 7)		
Loans to Group and associated companies (Note 13)	2,078,274	433,884
Short-term investment securities	8,214	77
Other loans	186,900	486,808
Short-term deposits and guarantees given	1,344	1,026
Allowances	<u>(42)</u>	<u>(317)</u>
	2,274,690	921,478
Accrual accounts	25,349	16,456
Total current assets	9,339,351	6,575,498
TOTAL ASSETS	22,573,474	21,614,823

(*) The balance sheet at 31 December 2005 is presented for comparative purposes only.

Notes 1 to 24 described in the attached Notes to the accounts and the appendix are an integral part of the balance sheet at 31 December 2006.

Translation of annual accounts originally issued in Spanish and prepared in accordance with accounting principles generally accepted in Spain (see Note 24). In the event of a discrepancy, the Spanish-language version prevails.

IBERDROLA, S.A.
Balance sheets
at 31 December

	Thousands of Euros	
	2006	2005 (*)
SHAREHOLDERS' EQUITY AND LIABILITIES		
Shareholders' equity (Note 9)		
Share capital	2,704,648	2,704,648
Share premium	459,577	459,577
Revaluation reserves	1,389,408	1,389,408
Other reserves of the Parent Company		
Legal reserve	540,929	540,929
Reserve for treasury stock	1,045	1,151
Other reserves	964,740	965,438
Retained earnings	1,049,384	1,046,754
Profit for the year	940,964	800,501
Interim dividend paid during the year	(405,697)	(330,828)
Total shareholders' equity	7,644,998	7,577,578
Deferred revenues		
Exchange gains	110	295
Other deferred revenues	45,828	45,859
Total deferred revenues	45,938	46,154
Provisions for contingencies and expenses (Note 10)		
Provisions for pensions and similar obligations	459,986	499,924
Provisions for taxes and other provisions	245,652	186,491
Total provisions for contingencies and expenses	705,638	686,415
Long-term debt		
Debentures and other marketable debt securities (Note 11)		
Non-convertible debentures and bonds	363,362	363,868
Other marketable debt securities	943,050	308,900
Unaccrued interest	(10,122)	(1,128)
Payable to credit institutions (Note 12)	3,692,955	4,045,399
Payable to Group and associated companies (Note 13)	6,040,779	4,978,270
Other long-term payables		
Long-term guarantees and deposits received	11,035	316
Other payables	25,624	29,755
Long-term taxes payable (Note 14)	16,942	19,366
Uncalled capital payments payable		
From Group companies	225	56,429
From associated companies	386	3,252
From other companies	4,117	403
Total long-term debt	11,088,353	9,804,830
Current liabilities		
Debentures and other marketable debt securities (Note 11)		
Non-convertible debentures and bonds	507	40,329
Unaccrued interest	3,636	5,039
Payable to credit institutions (Note 12)		
Loans and other payables	465,010	370,082
Interest payable	18,578	27,650
Payable to Group companies (Note 13)	1,109,295	1,284,063
Payable to associated companies (Note 13)	482,595	261,226
Trade accounts payable		
Accounts payable for purchases and services	475,076	1,079,084
Other non-trade payables		
Taxes payable (Note 14)	74,537	40,993
Other payables	438,845	345,155
Compensation payable	17,471	15,903
Short-term guarantees and deposits received	83	27,047
Operating allowances	226	226
Accrual accounts	2,688	3,049
Total current liabilities	3,088,547	3,499,846
TOTAL SHAREHOLDERS' EQUITY AND LIABILITIES	22,573,474	21,614,823

(*) The balance sheet at 31 December 2005 is presented for comparative purposes only.

Notes 1 to 24 described in the attached Notes to the accounts and the appendix are an integral part of the balance sheet at 31 December 2006.

Translation of annual accounts originally issued in Spanish and prepared in accordance with accounting principles generally accepted in Spain (see Note 24). In the event of a discrepancy, the Spanish-language version prevails.

IBERDROLA, S.A.
Income statements
for the years ended 31 December

	Thousands of Euros	
	2006	2005 (*)
DEBIT		
Expenses		
Procurements		
Energy purchases	1,899,964	2,422,069
Other external expenses	339,634	756,469
Personnel expenses		
Wages, salaries and similar expenses	133,573	150,004
Employee welfare expenses	68,733	81,014
Depreciation and amortisation expense	87,016	95,370
Variation in operating allowances		
Variation in allowances for and losses on uncollectible receivables	30,908	5,770
Other operating expenses		
Outside services	184,183	199,482
Taxes other than income tax	11,917	23,786
Other current operating expenses	6,251	6,795
Operating profit	<u>152,039</u>	<u>-</u>
	2,914,218	3,740,759
Financial and similar expenses		
On debts to group companies	273,973	193,666
On debts to associated companies	11,392	5,607
On debts to third parties and similar expenses	251,118	185,785
Losses on short-term investments	53,352	39,507
Exchange losses	23,132	46,765
Variation in allowances for short-term investments	(738)	117,652
Interest expenses allocable to provisions for pensions and similar obligations	17,105	13,122
Financial profit	<u>815,560</u>	<u>352,089</u>
	1,444,894	954,193
Profit from ordinary activities	<u>967,599</u>	<u>319,651</u>
Variation in allowances for intangible assets, tangible fixed assets and long-term investments (Note 15)	(88,171)	(418,847)
Losses on intangible assets, tangible fixed assets and long-term investments	39	287
Losses on transactions involving treasury stock (Note 8)	2,674	1,696
Extraordinary expenses (Note 15)	86,834	296,450
Prior years' expenses and losses	2,588	101
Extraordinary profit	<u>30,659</u>	<u>300,335</u>
	34,623	180,022
Profit before taxes	<u>998,258</u>	<u>619,986</u>
Less-Corporate income tax (Note 14)	57,294	(180,515)
Profit for the year	<u>940,964</u>	<u>800,501</u>

(*) The income statement for the year ended 31 December 2005 is presented for comparative purposes only.

Notes 1 to 24 described in the attached Notes to the accounts and the appendix are an integral part of the income statement for the year ended 31 December 2006.

Translation of annual accounts originally issued in Spanish and prepared in accordance with accounting principles generally accepted in Spain (see Note 24). In the event of a discrepancy, the Spanish-language version prevails.

IBERDROLA, S.A.
Income statements
for the years ended 31 December

	Thousands of Euros	
	2006	2005 (*)
CREDIT		
Revenues		
Net revenues (Note 15)		
Sales	2,467,835	3,206,686
Services	118,751	140,203
Capitalised expenses of in-house work on fixed assets	16,085	19,527
Other operating revenues		
Non-core and other current operating revenues	310,597	339,969
Operating subsidies	195	484
Overprovision for contingencies and expenses	755	1,452
Operating loss	<u>-</u>	<u>32,438</u>
	2,914,218	3,740,759
Revenues from equity investments		
Group companies (Note 15)	748,236	566,221
Associated companies (Note 15)	155,400	2,302
Other companies	46,984	15,567
Revenues from other marketable securities and non-current loans		
Group companies	141,976	140,922
Associated companies	1,074	1,217
Other companies	501	1,663
Other interest and similar revenues		
Group companies	154,239	93,848
Associated companies	6,656	6,565
Other interest	27,923	4,644
Gains on short-term investments	137,099	72,363
Capitalised financial expenses	314	504
Exchange gains	24,492	48,377
Financial loss	<u>-</u>	<u>-</u>
	1,444,894	954,193
Loss from ordinary activities	<u>-</u>	<u>-</u>
Gains on disposal of intangible assets, tangible fixed assets and long-term investments (Note 15)	12,275	174,190
Gains on disposal of treasury stock (Note 8)	3,317	4,177
Capital subsidies transferred to income for the year	5	756
Extraordinary revenues	18,747	899
Prior years income	279	-
Extraordinary losses	<u>-</u>	<u>-</u>
	34,623	180,022
Loss before taxes	<u>-</u>	<u>-</u>
Corporate income tax		
Loss for the year	<u>-</u>	<u>-</u>

(*) The income statement for the year ended 31 December 2005 is presented for comparative purposes only.

Notes 1 to 24 described in the attached Notes to the accounts and the appendix are an integral part of the income statement for the year ended 31 December 2006.

IBERDROLA, S.A.

Notes to the Annual Accounts

31 December 2006

1. COMPANY ACTIVITY

Pursuant to Article 2 of its bylaws, the corporate purpose of IBERDROLA, S.A. ("IBERDROLA" or the "Company") is as follows:

- To carry out all manner of activities and construction work and provide services required for, or related to, the production, transmission, switching and distribution or retailing of electric power or electricity by-products and their applications, and involving the raw materials or primary energies required for electric power generation, energy, engineering, computer and telecommunications services, services relating to the Internet, the treatment and distribution of water, the integral provision of urban and gas retailing services, and other gas storage, regasification, transmission or distribution activities, which will be provided indirectly through the ownership of shares or other equity investments in companies that do not engage in the retailing of gas.
- The distribution, representation and marketing of all manner of goods and services, products, articles, merchandise, computer programs, industrial equipment, machinery, machine and hand tools, spare parts and accessories.
- To engage in the research, study and planning of investment and corporate organisation projects, and to promote, set up and develop industrial, commercial and service companies.
- To provide assistance and support services to the Group companies and other investees, providing for them the guarantees and collateral required for this purpose.

The aforementioned activities may be performed in Spain and abroad, and may be performed totally or partially either directly by IBERDROLA or through the ownership of shares or other equity investments in other companies, subject in all cases to the legislation applicable at any given time and, in particular, to the legislation applicable to the electricity industry.

The only energy business IBERDROLA is engaged in is the retailing of electricity and gas to eligible customers.

IBERDROLA also provides various services to other Group companies, such as leasing of measuring devices, natural gas purchases for the Group's electricity generation plants, telecommunications-related services (e.g. fibre optics networks and dispatching centres), information technology services and other non-operating, backbone and support services, as well as Group financing, which is managed centrally.

IBERDROLA individually considered, it has no environmental liabilities, expenses, assets, provisions or contingencies that could have a significant effect on its equity, financial situation and results. Consequently, these notes do not include specific details regarding environmental issues.

2. BASIS OF PRESENTATION OF THE ANNUAL ACCOUNTS

The accompanying Annual Accounts are presented in accordance with Law 19/1989, of 25 July, partially reforming and adapting Spanish corporate law to EC Directives on companies, with Royal Decree 437/1998, of 20 March, approving the rules for adapting the Spanish National Chart of Accounts for electric utilities and with the Spanish National Chart of Accounts approved by Royal Decree 1643/1990, of 20 December, and, accordingly, they give a true and fair view of the net equity, financial position and results of operations of IBERDROLA.

The Annual Accounts, which have been prepared by IBERDROLA's directors, will be submitted for approval by the shareholders in general meeting and are expected to be approved without modification.

In addition, pursuant to current legislation, IBERDROLA has prepared its Consolidated Annual Accounts in accordance with International Financial Reporting Standards (IFRSs). The principal balance sheet and income statement headings in the 2006 Consolidated Annual Accounts of the IBERDROLA Group are the following:

	Thousand of euros
Total assets	33,060,843
Equity:	
- Of the Parent	10,418,214
- Of minority interests	148,789
Revenue	11,017,408
Net profit for the year:	
- Attributable to the Parent	1,660,256
- Minority interests	30,629

3. PROFIT DISTRIBUTION

The Board of Directors of IBERDROLA plans to submit for approval at the General Shareholders' Meeting the following distribution of 2006 income and retained earnings:

	Thousand of euros
Distribution basis:	
Retained earnings	1,049,384
2006 profit	<u>940,964</u>
	<u><u>1,990,348</u></u>
Distribution:	
To dividends:	
Interim (Note 9)	405,697
Final dividend	691,764
To retained earnings	<u>892,887</u>
	<u><u>1,990,348</u></u>

On 10 November 2006, the Board of Directors of IBERDROLA, based on its projected income for 2006, declared an interim dividend of EUR 405,697 thousand. This amount is recorded under "Interim dividend paid during the year" and "Other non-trade payables – Other payables" in the accompanying balance sheet at 31 December 2006 (see Note 9). This dividend was paid on 2 January 2007. The amount of this dividend is less than the maximum legal amount stipulated in Article 216 of the revised Spanish Corporations Law as regards profit obtained since the end of the previous fiscal year.

IBERDROLA had at that date the minimum unrestricted reserves required under Article 194 of the aforementioned Law for payment of the interim dividend.

The provisional accounting statement prepared as required by Article 216 of the revised Spanish Corporations Law disclosing the existence of sufficient liquidity for distribution of the interim dividend was as follows:

	Thousand of euros
Cash available at 1 November 2006	607,519
Projected collections through 2 January 2007:	
Operating collections	2,710,658
Financial collections	1,888,485
Projected payments through 2 January 2007:	
Operating payments	(2,217,682)
Financial payments	<u>(1,060,711)</u>
Projected cash available at 2 January 2007, before payment of the interim dividend	1,928,269
Payment of dividend, net of withholding	<u>(345,519)</u>
Projected cash available at 2 January 2007, after payment of the interim dividend	1,582,750
Projected collections through 10 November 2007:	
Operating and financial collections	16,849,842
Non-operating collections	365,188
Projected payments through 10 November 2007:	
Operating and financial payments	(13,875,849)
Non-operating payments	(2,737,105)
Final dividend	<u>(691,764)</u>
Projected cash available at 10 November 2007	<u>1,493,062</u>

In addition, at the date of preparation of these Annual Accounts, the Board of Directors of IBERDROLA had agreed to seek approval at the Ordinary General Shareholders' Meeting for the distribution of a maximum final dividend of EUR 691,764 thousand, consisting of a fixed gross dividend of EUR 0.593 per share for all the outstanding shares of IBERDROLA at the date on which the Board so agreed (901,549,181) and of EUR 0.593 per share for all the shares, if any, as a result of the bid to acquire the shares of Scottish Power, Plc., detailed in Note 22. This final dividend will be paid on July 2, 2007.

If this final dividend is approved at the Ordinary General Shareholders' Meeting, the total dividend in 2006 will amount to EUR 1.043 per share. The 2005 dividend amounted to EUR 0.884 per share.

4. ACCOUNTING POLICIES

The main accounting policies used in preparing the accompanying Annual Accounts were as follows:

a) Intangible assets

Research and development expenses incurred in projects for which there are sound reasons to expect their technical success and economic and commercial profitability at year end are recorded as intangible assets and amortised over a period of between three and five years from completion of the project, depending on the individual characteristics. In 2006, IBERDROLA derecognised all its research and development projects, which had been fully amortised at 31 December 2005.

External costs incurred in research and development projects which are not expected to be profitable in the future are recorded with a charge to "Outside Services" in the income statement for the year in which they are incurred.

The costs incurred in connection with the basic computer systems used by IBERDROLA's management and developed in-house, and the amounts paid for the title to or the right to use programs are also recorded under this balance sheet heading. These items are amortised on a straight-line basis over a maximum period of five years from the date on which each application is put to use.

Personnel expenses related to IBERDROLA employees who have worked on research and development and information technology projects are recognised as an increase in the cost of the projects and recorded under "Capitalised expenses of in-house work on fixed assets" in the income statement. This heading included EUR 4,551 thousand in this connection in 2006.

The amounts recorded by IBERDROLA for concessions, patents, licenses, trademarks and other relate to the cost effectively incurred in the acquisition thereof and are amortised on a straight-line basis over the shorter of the related license term or the period over which they are expected to generate revenues.

Assets under capital leases are recorded at the cash value of the asset and amortised in keeping with the criteria applied to intangible assets (see Note 4.c) based on their estimated useful life. "Long-term debt – Payable to credit institutions" on the liability side of the balance sheet includes the amount payable on the lease contract plus the purchase option. The interest expenses related to the leases are recorded under "Deferred charges" in the balance sheet assets and taken to income in accordance with financial criteria (see Note 4.e).

b) Tangible fixed assets

Tangible fixed assets are valued at updated cost in keeping with prevailing legislation, including Royal Decree-Law 7/1996 (see Notes 6 and 9).

Cost includes the following expenses, incurred during the construction period only:

- Financial expenses related to external financing.

In accordance with Royal Decree 437/1998 (see Note 2), the method used by IBERDROLA to determine the amount of financial expenses which can be capitalised is as follows:

- a) Specific-purpose financing used for the acquisition or construction of certain assets is allocated to IBERDROLA's assets and, accordingly, the related financial expenses are capitalised in full.
- b) General-purpose financing, both equity and debt, is allocated proportionally to the other assets, and the accrued interest on borrowed funds allocated to construction in progress (in the same proportions) by applying the effective average interest rate on such financing to the average aggregate capitalisable investment.

The financial expenses capitalised as an increase in tangible fixed assets by IBERDROLA in 2006 by the method described above amounted to EUR 314 thousand, included under "Capitalised financial expenses" with a charge to the related tangible fixed asset headings.

- Personnel expenses relating directly or indirectly to construction in progress.

The personnel expenses capitalised in this connection in 2006 amounted to EUR 11,534 thousand. This amount is recorded under "Capitalised expenses of in-house work on fixed assets" in the 2006 income statement.

IBERDROLA transfers construction in progress to operating tangible fixed assets at the end of the related trial period.

The costs of expansion or improvements of tangible fixed assets leading to increased productivity or capacity or to a lengthening of the useful lives of the assets are capitalised.

Replacements or renewals of complete units are recorded as fixed asset additions, and the units replaced or renewed are derecognised.

Periodic maintenance, upkeep and repair expenses are expensed currently.

c) Depreciation of operating tangible fixed assets

Operating tangible fixed assets are depreciated by the straight-line method at annual rates based on the following years of estimated useful life:

	<u>Average years of estimated useful lives</u>
Buildings	50
Data processing equipment	5 - 8
Measuring devices	15 - 27
Fibre optic installations	5 - 40
Dispatching centres and other tangible fixed assets	4 - 50

"Depreciation and amortisation expense" in the accompanying income statement for 2006 includes EUR 61,119 thousand of depreciation of operating tangible fixed assets (see Note 6).

d) Marketable securities and other similar investments

Investments in short and long-term marketable fixed-income and equity securities are recorded in the balance sheet at the lower of cost or market value. Market value is the lower of the average listed price of the latest quarter or the closing price for listed securities that do not relate to Group and associated companies, or the underlying book value, adjusted to make the accounting policies applied uniform with those used by IBERDROLA, plus the amount of the unrealised gains disclosed at the time of the acquisition and still existing at present, for the rest (see Note 7).

Reversible unrealised losses (cost higher than market value at year end) are recorded under "Long-term investments – Allowances" on the accompanying balance sheet (see Note 7). In 2006, IBERDROLA allocated EUR 158,878 thousand to allowances and reversed EUR 243,766 thousand. These amounts are recorded under "Variation in allowances for intangible assets, tangible fixed assets and long-term investments" in the accompanying income statement.

e) Deferred charges

The accounting principles applied to the items under this balance sheet heading and their recognition in the income statement are as follows:

1. Expenses incurred in the issue and placement of debentures and bonds and debt arrangement expenses are recorded under "Deferred charges" and amortised financially in accordance with the outstanding balance of the related issues and loans. In 2006, IBERDROLA amortised EUR 7,046 thousand of such deferred charges, recorded under "Financial and similar expenses - On debts to third parties and similar expenses" in the income statement.
2. Expenses incurred in relation to specific actions or activities that are expected to generate future income are recorded under "Deferred charges" and amortised over the estimated period during which they contribute to the generation of income. "Outside services" in the 2006 income statement includes EUR 15,200 thousand for this concept.
3. Deferred interest expenses arise from the difference between the redemption value of the debt generated by financial lease transactions and the value of the leased goods. In 2006, IBERDROLA amortised EUR 4,720 thousand of interest expenses, appearing under "Financial and similar expenses - On debts to third parties and similar expenses" in the accompanying income statement.

f) Inventories

Inventories, which correspond mainly to natural gas and liquid natural gas, are valued at the lower of cost using the FIFO (first in, first out) method or market.

At 31 December 2006, the gas stocks were deposited at the regasification and storage plants belonging to Enagás, S.A., Bahía de Bizkaia Gas, S.A. and Planta de Regasificación de Sagunto, S.A.

At 31 December 2006, IBERDROLA had entered into take or pay contracts with several natural and liquefied natural gas suppliers for the supply of 116.4 bcm of gas in the period from 2007 to 2026, which reasonably cover the amounts earmarked for retailing and for consumption at the electricity production facilities. The prices under these contracts are determined on the basis of formulas commonly used in the market, which index the price of gas to the performance of other energy variables.

g) Unbilled power supplied

The revenue figure for each year includes an estimate of the power supplied to customers in the liberalised market but not billed because it had not been metered at year end for reasons relating to the regular meter-reading period. The estimated unbilled power at 31 December 2006 amounted to EUR 63,431 thousand (see Note 15). This amount is included under "Accounts receivable – Unbilled power supplied" on the asset side of the accompanying balance sheet.

h) Treasury stock

Own shares held at the end of 2006 that were not acquired to reduce IBERDROLA's capital stock are recorded under "Treasury stock" in the accompanying balance sheet.

In keeping with prevailing accounting standards, treasury stock is valued at the lower of cost or market. Market value is the lower of:

- The listing on the last day of the year.
- The average listing of the last quarter.
- The underlying book value.

Unrealised losses arising from the difference between cost and listing are recorded under "Losses on transactions involving treasury stock" in the income statement. Any additional capital losses between cost and underlying book value are recognised with a charge to "Reserve for treasury stock" in the balance sheet.

The reversal of previously recorded unrealised losses arising from subsequent value adjustments or disposals of treasury stock are recorded with a credit to income for the year or reserves, depending on the account to which they were previously charged.

i) Deferred revenues

This balance sheet heading includes the following items:

- Unrealised positive value adjustments appear under "Deferred revenues – Exchange gains" as described in Note 4.m.

- “Deferred revenues – Other deferred revenues” includes mainly collections or prepaid bills relating to the lease of fibre optics to third parties, which are taken to income on a straight-line basis over the life of the related contracts. “Net revenues – Sales” in the 2006 income statement includes EUR 3,236 thousand for this concept.

j) Employee benefits supplementary to social security benefits and other employee welfare commitments

IBERDROLA’s main commitments to its employees other than social security benefits are the following:

- a) The present employees of IBERDROLA and employees who have retired since 9 October 1996 are covered by an employment-based, defined-contribution retirement pension scheme independent from the social security system.

In accordance with this system and the collective labour agreement in force for IBERDROLA, the periodic contribution to be made is calculated as a percentage of the annual pensionable salary of each employee. IBERDROLA finances these contributions for all its present employees, except for employees hired since 1 January 1996, for whom the Company contributes one-third and the employee contributes two-thirds.

The contributions made by IBERDROLA in 2006 amounted to EUR 12,309 thousand and are recorded under “Employee welfare expenses” in the accompanying income statement.

- b) The employees who retired before 9 October 1996 are covered by a defined benefit retirement pension scheme, the actuarial value of which had been externalised in full in previous years through an insurance policy.
- c) Also, in relation to present employees and employees who have retired since 1996, in connection with risk benefits (e.g. for death of spouse, permanent disability or death of present employee’s parent) which guarantee capital equivalent to one year’s recognised salary and the long-service bonus at the time the event giving rise to such benefits occurs, are instrumented through an annually renewable insurance policy. The premium paid under the aforementioned insurance policy in 2006 amounted to EUR 2,294 thousand and is recorded under “Employee welfare expenses” in the income statement.

IBERDROLA also has certain commitments to its employees other than those indicated above, which are covered by in-house pension provisions (see Note 10.a) consisting mainly of long-service bonuses for serving employees and of free electricity for retired employees. IBERDROLA records the expense for both these commitments as they are accrued over the period of employment of the beneficiary concerned. The normal costs and financial expenses incurred in 2006 related to these commitments amounted to EUR 4,091 thousand and EUR 12,187 thousand, respectively, recorded under "Employee welfare expenses" and "Interest expenses allocable to provisions for pensions and similar obligations," respectively, in the 2006 income statement. In addition, the actuarial differences arising due to changes in the assumptions used to determine the actuarial liabilities accrued at the end of that year led to an expense of EUR 11,415 thousand, recorded with a debit to "Extraordinary revenues" in the accompanying 2006 income statement.

"Provisions for pensions and similar commitments" in the accompany balance sheet includes the allocation for commitments to Board Members as per the Company's by-laws (see Note 18.a).

Note 10.a below describes how the provisions recorded for pensions and similar obligations are assigned to cover the aforementioned commitments.

k) Voluntary collective redundancy procedure and other early retirement plans for employees

In 1997, the Board of Directors of IBERDROLA resolved to adapt, by various means, its labour force and that of some of its subsidiaries to the demands of the new competitive environment with the intention of establishing in the period from 1998 through 2004 specific early retirement plans and other means of reducing headcount until the targets had been met. These restructuring plans were put before the Company's employees' representatives, and an agreement was reached. According to IBERDROLA's best estimates, restructuring expenses at 1 January 1998 amounted to EUR 512,717 thousand, recorded under "Provisions for contingencies and expenses – Other provisions." IBERDROLA's policy is to transfer the costs related to plans already carried out to "Provisions for pensions and similar obligations" on the liability side of the balance sheet until they are externalised or paid (see Note 10.a).

From 1998 to 2001, fulfilling the intention it had expressed previously, IBERDROLA proposed to employees who met certain conditions certain early retirement plans and a "Special Labour Situation" arrangement prior to adhesion to the early retirement plan.

In December 2000, the obligations to the employees who, having availed themselves of the above-mentioned retirement plans, had actually retired at 30 November 2000, were externalised, and a single premium was paid to a third party for the actuarial value relating to the aforementioned obligations.

Without prejudice to the continuity of the restructuring plans agreed on in prior years, in 2003 IBERDROLA reached an agreement with the trade union representatives to implement a voluntary collective redundancy procedure applicable to all employees reaching 58 or more years of age before 31 December 2006, which was approved by the Ministry of Employment and Social Affairs in 2003.

Between 2003 and 2006, 2,333 employees had availed themselves of this procedure, of which 633 were already covered by the restructuring plans established previously.

The total actuarial provisions to cover the future costs of employees included in the aforementioned redundancy procedure and the restructuring plans before 2003 amount to EUR 61,233 thousand and EUR 27,605 thousand, respectively, and are recorded under "Provisions for pensions and similar obligations" in the balance sheet at 31 December 2006 (see Note 10.a).

General and financial expenses incurred in 2006 in this connection amounted to EUR 631 thousand and EUR 4,918 thousand, respectively, recorded under "Extraordinary expenses" and "Interest expenses allocable to provisions for pensions and similar obligations", respectively, in the accompanying income statement. The actuarial differences arising due to changes in the assumptions used to determine the actuarial liabilities accrued at the end of that year led to income of EUR 18,229 thousand, recorded with a credit to "Extraordinary revenues" in the accompanying 2006 income statement.

Prior to 31 December 2006, IBERDROLA, after reaching the corresponding agreement with the trade union representatives, extended the 2003 collective redundancy program to employees turning 58 in 2007, as well as to those employees who had the opportunity to avail themselves of the initial plan but opted not to. The faculty to so extend the program was approved by the labour authorities in 2003. In the 2006 income statement "Extraordinary expenses" includes EUR 41,769 thousand for this concept, based on the best estimate of the number of employees that will avail themselves of the aforementioned program extension. In addition, the Company has transferred EUR 1,256 thousand included in the provision for long-service bonuses to the provision for the labour force reduction plan, as this was the amount allocated in prior years based on the estimate of the number of employees who would avail themselves of the extended labour force reduction plan.

l) Provision for taxes and other provisions for contingencies and expenses

IBERDROLA records provisions for contingencies and expenses to cover probable or certain quantifiable third-party liability arising from litigation in progress or from indemnity payments, obligations or unpaid expenses of undetermined amount, and collateral and other similar guarantees provided by the Company based on its best estimate. These provisions are recorded when the related liability or obligation arises (see Note 10.b).

m) Transactions in currencies other than the euro

Transactions carried out in currencies other than the euro are translated to euros at the exchange rates prevailing at the transaction date. During the year, the differences arising between the exchange rates at which the transactions were recorded and those in force at the date on which the related collections or payments are made are charged or credited, as appropriate, to income.

The cash balances held by IBERDROLA at 31 December each year in currencies other than the euro are translated to euros at the year-end exchange rate and any exchange differences are charged or credited, as appropriate, to "Exchange losses" or "Exchange gains," respectively, in the income statement.

Any fixed-income securities and receivables and payables denominated in currencies other than the euro at 31 December each year are translated at the year-end exchange rate or the locked-in exchange rate if the Company had arranged hedges on the transactions concerned. Exchange differences are grouped by maturity and currency and the exchange losses that arise in each of these groups are allocated to "Exchange losses" in the related income statement, whereas unrealised exchange gains that arise in each currency group identified are recorded under "Deferred revenues – Exchange gains" on the liability side of the Balance Sheet until the related securities, receivables or payables mature, once the exchange losses allocated previously to the income statement for each currency group have been offset.

n) Classification of debt

In the accompanying balance sheet, debts maturing in under 12 months from year-end are classified as current liabilities and those maturing at over 12 months as long-term debt.

o) Recognition of revenues and expenses

Revenues and expenses are recorded on an accrual basis, i.e. when the actual flow of the related goods and services occurs, regardless of when the resulting monetary or financial flow arises.

p) Settlements relating to regulated activities and shortfall in revenues

In 1998, basically as a result of the entry into force of Spanish Electricity Industry Law 54/1997 and the related implementing regulations, inter-company settlements were created. These settlements are made by the Spanish National Energy Commission and take the form of collections from or payments to other electric utilities in order to redistribute tariff revenue, net of energy purchases made to cover demand from customers supplied under the tariff system. Accordingly, each utility receives the revenue corresponding to its regulated activities, including distribution and transmission activities. Tariffs are set annually by Royal Decree.

IBERDROLA is the legal entity with which the revenue shortfall described hereafter is settled and Iberdrola Distribución Eléctrica, S.A.U. is the entity with which power distribution and transmission activities are settled.

As of the date of preparation of these Annual Accounts, IBERDROLA had not received the final settlements for these concepts corresponding to the years from 2002 to 2006.

Because in 2006 and 2005 the revenues received by utilities for regulated sales to their customers were not sufficient to remunerate the system's various activities and costs, the utilities themselves were forced to finance the resulting tariff deficit.

In 2005, Royal Decree Law 5/2005, of 11 March, ruled provisionally that IBERDROLA must finance 35.01% of the tariff deficit. Subsequently, Royal Decree 1556/2005, of 28 December, established that the amounts contributed by each utility to finance the shortfall in revenue for 2005 would be reimbursed through settlements for regulated activities in later years, including accrued financing costs.

As a consequence of this recognition by the Spanish government to reimburse the tariff deficit independent of future billings, in 2005 IBERDROLA recognised a receivable for its corresponding portion of the tariff deficit, estimated at EUR 1,259,115 thousand. This amount is included under "Long-term investments - Account receivable due to shortfall in revenues" on the accompanying balance sheet at 31 December 2005.

Later, Royal Decree 809/2006, passed to revise the electricity tariff applicable from 1 July 2006, ruled that 2005 tariff deficit could be securitised. Accordingly, prior to year-end 2006, the Iberdrola Group entered into a securitisation agreement with a group of financial entities by virtue of which it transferred the right to collect the 2005 tariff deficit receivable to said entities, along with substantially all the associated risks and rewards. “Long-term investments – Account receivable due to shortfall in revenues” in the balance sheet at 31 December 2006 includes EUR 6,977 thousand corresponding to the difference between the amount securitised and IBERDROLA’s best estimate of the percentage corresponding to it of the shortfall generated in 2005.

Finally, Royal Decree 1634/2006, which establishes the electricity tariff applicable from 1 January 2007, guarantees the recovery of the 2006 tariff deficit independent of future billings, as happened with the 2005 tariff deficit. As a result, “Long-term investments – Account receivable due to shortfall in revenues” in the balance sheet at 31 December 2006 includes EUR 579,670 thousand corresponding to the best estimate of the portion of the deficit in 2006 that corresponds to IBERDROLA, assuming the same deficit allocation percentage of 35.01% (see Note 7).

q) Rights to inspection and coupling and meter rentals

The rights to inspection and coupling and meter rentals charged by IBERDROLA to customers in the liberalised market and to Iberdrola Distribución Eléctrica, S.A.U. are recorded as revenues with a credit to “Net revenues – Services” in the income statement. In 2006, IBERDROLA obtained EUR 118,698 thousand of revenues for these concepts (see Note 15).

r) Corporate income tax

IBERDROLA files consolidated tax returns with certain Group companies.

The expense for corporate income tax for the year is calculated on the basis of book income before taxes, increased or decreased, as appropriate, by permanent differences from taxable income.

Double taxation tax credits and other tax credits and tax relief earned as a result of economic events occurring in the year are deducted from the income tax expense, unless there are doubts as to whether they can be realised.

s) Severance costs

Under current labour legislation, IBERDROLA is required to pay severance to employees terminated under certain conditions. The Company does not expect any future terminations that might give rise to material liabilities. Accordingly, the accompanying Annual Accounts do not include any provision for these concepts.

t) Financial derivatives and hedges

The financial derivatives held by IBERDROLA relate to hedges arranged to mitigate the Company's exposure to certain risks, mainly exchange rate and interest rate risk, and fluctuations in stock (gas and electricity) costs.

The resulting gains or losses on these hedges are allocated to income by the same method of recognition with respect to timing as that applied to the gains or losses on the underlying hedged transaction.

At year-end 2006, IBERDROLA had arranged currency and interest-rate swaps to hedge its financial debt (loans, debentures and other marketable securities, see Note 12) with nominal amounts of EUR 888,189 thousand and EUR 5,748,671 thousand, respectively. Of these amounts, EUR 1,224,644 thousand of interest-rate swaps were arranged with Group companies. IBERDROLA has also interest-rate options with a nominal amount of EUR 1,280,000 thousand.

In addition, at 31 December 2006, IBERDROLA had entered into hedges on gas costs for 0.3 bcm with certain financial institutions and a hedge on the cost of electricity with the Iberdrola Generación, S.A.U. subsidiary, which led to a decrease in supply costs of EUR 111,467 thousand in the year.

The Company also entered into several trading derivatives to hedge the price performance of various stocks, as well as its own shares. Losses on these contracts are recorded when known at the market value of each contract, while gains are taken to income when realised. "Financial and similar expenses – Losses on short-term investments" and "Other interest and similar revenues – Gains on short-term investments" in the 2006 income statement include EUR 53,352 thousand and EUR 134,111 thousand, respectively, from contracts expiring in the year and the valuation of open positions at 31 December 2006. The detail of outstanding trading derivatives at 31 December 2006, is as follows:

Derivatives on treasury stock			
Type of contract	No. of shares	Maturity date	Market value (thousands of euros)
Equity Swap	2,351,858	2007	760
Collar	860,277	2007	17
Put options sold	<u>1,513,857</u>	2007	<u>615</u>
	<u>4,725,992</u>		<u>1,392</u>

Derivatives on other marketable securities			
Type of contract	No. of shares	Maturity date	Market value (thousands of euros)
Equity swap	<u>5,460,550</u>	2007	<u>13,250</u>

The market value shown in the preceding tables represents the potential gain for the IBERDROLA Group on the early settlement of its positions at 31 December 2006.

In addition, the fair value of IBERDROLA's derivatives which, in conformity with Spanish GAAP, have not been measured at market value amounts to EUR 10,847 thousand.

On the other hand, at year-end, IBERDROLA had arranged with Group companies various exchange rate hedges amounting to USD 1,400,611 thousand to cover transactions. Additionally, exchange rate hedges arranged with others amounted to USD 333,822 thousand.

5. INTANGIBLE ASSETS

The changes in 2006 in intangible asset accounts and in the related accumulated amortisation were as follows:

Thousand of euros					
	Balance at 01.01.06	Additions or charges	Transfers	Disposals, derecognition, reductions and write-offs	Balance at 12.31.06
<u>Cost:</u>					
Research and development expenses	6,271	-	-	(6,271)	-
Concessions, patents, licenses, trademarks and other	44,703	-	-	(54)	44,649
Computer software	201,841	26,668	-	(18,244)	210,265
Rights on leased assets	<u>113,410</u>	<u>-</u>	<u>(9,277)</u>	<u>-</u>	<u>104,133</u>
Total cost	<u>366,225</u>	<u>26,668</u>	<u>(9,277)</u>	<u>(24,569)</u>	<u>359,047</u>
<u>Accumulated amortisation:</u>					
Research and development expenses	6,271	-	-	(6,271)	-
Concessions, patents, licenses, trademarks and other	13,415	5,152	-	-	18,567
Computer software	147,809	19,494	-	(8,338)	158,965
Rights on leased assets	<u>9,362</u>	<u>1,251</u>	<u>(6,788)</u>	<u>-</u>	<u>3,825</u>
Total accumulated amortisation	<u>176,857</u>	<u>25,897</u>	<u>(6,788)</u>	<u>(14,609)</u>	<u>181,357</u>
Total net cost	<u>189,368</u>	<u>771</u>	<u>(2,489)</u>	<u>(9,960)</u>	<u>177,690</u>

The detail of the Company's outstanding financial leases at 31 December 2006 is the following:

Thousand of euros							
Leased asset	Term of lease (months)	Months elapsed at 12.31.06	Cost at source	Initial interest charge	Instalments paid as of 12.31.06	Outstanding instalments (plus purchase option)	Value of purchase option
Corporate building	<u>240</u>	<u>40</u>	<u>104,133</u>	<u>70,747</u>	<u>25,146</u>	<u>149,734</u>	<u>31,188</u>

6. TANGIBLE FIXED ASSETS

The changes in 2006 in tangible fixed asset accounts and in the related accumulated amortisation and provisions were as follows:

	Thousand of euros				Balance at 12.31.06
	Balance at 01.01.06	Additions or charges	Transfers	Decreases, disposals or reductions	
Cost:					
Operating tangible fixed assets					
Technical installations:					
Fibre optics network	185,335	27	10,804	-	196,166
Measuring devices	674,316	29,705	-	(20,834)	683,187
Other communications installations	<u>119,059</u>	-	<u>6,810</u>	-	<u>125,869</u>
	978,710	29,732	17,614	(20,834)	1,005,222
Other operating assets	<u>417,437</u>	<u>39,572</u>	<u>9,277</u>	<u>(9,287)</u>	<u>456,999</u>
Total operating tangible fixed assets	<u>1,396,147</u>	<u>69,304</u>	<u>26,891</u>	<u>(30,121)</u>	<u>1,462,221</u>
Technical installations in progress	22,651	10,176	(5,110)	-	27,717
Advances and other construction in progress	<u>9,953</u>	<u>17,453</u>	<u>(12,504)</u>	<u>(3,632)</u>	<u>11,270</u>
Total cost	<u>1,428,751</u>	<u>96,933</u>	<u>9,277</u>	<u>(33,753)</u>	<u>1,501,208</u>
Accumulated amortisation:					
Technical installations:					
Fibre optics network	32,555	7,640	-	-	40,195
Measuring devices	432,038	29,427	-	(20,805)	440,660
Other communications installations	<u>77,750</u>	<u>6,352</u>	-	-	<u>84,102</u>
	542,343	43,419	-	(20,805)	564,957
Other operating assets	<u>230,948</u>	<u>17,700</u>	<u>6,788</u>	<u>(4,917)</u>	<u>250,519</u>
Total accumulated amortisation	<u>773,291</u>	<u>61,119</u>	<u>6,788</u>	<u>(25,722)</u>	<u>815,476</u>
Allowances for decline in value of tangible fixed assets	<u>32,628</u>	-	-	(3,283)	<u>29,345</u>
Total accumulated amortisation and allowances	<u>805,919</u>	<u>61,119</u>	<u>6,788</u>	<u>(29,005)</u>	<u>844,821</u>
Total net cost	<u>622,832</u>	<u>35,814</u>	<u>2,489</u>	<u>(4,748)</u>	<u>656,387</u>

Amortisation in 2006 corresponding to the revaluation of assets permitted under Royal Decree-Law 7/1996 amounted to EUR 498 thousand, with EUR 5,132 thousand pending amortisation at year-end.

At 31 December 2006, IBERDROLA had tangible fixed asset purchase commitments amounting to EUR 6,070 thousand.

Fully depreciated operating tangible fixed assets at 31 December 2006 amounted to EUR 449,371 thousand.

7. LONG AND SHORT-TERM FINANCIAL INVESTMENTS

The movement in “Long-term financial investments” and “Short-term financial investments” and the related allowances in 2006 were the following:

	Thousand of euros				
	Balance at 01.01.06	Additions or provisions	Transfers	Decreases, disposals or reductions	Balance at 12.31.06
<u>Long-term investments</u>					
Holdings in Group companies	8,926,657	458,457	-	(188,562)	9,196,552
Holdings in associated companies	296,574	457,935	45,435	-	799,944
Long-term investment securities	187,899	8,559	(53,618)	(114)	142,726
Loans to Group and associated companies (Note 13)	3,552,169	-	(1,923,595)	(52,970)	1,575,604
Other loans	9,123	46,151	(4,500)	(821)	49,953
Long-term taxes receivable (Note 14)	300,092	4,936	-	(78,493)	226,535
Long-term deposits and guarantees given	19	-	340	(7)	352
Amount receivable due to shortfall in revenues (Note 4.p.)	1,259,115	579,670	-	(1,252,138)	586,647
Allowances	(456,123)	(159,007)	-	324,710	(290,420)
	<u>14,075,525</u>	<u>1,396,701</u>	<u>(1,935,938)</u>	<u>(1,248,395)</u>	<u>12,287,893</u>
<u>Short-term financial investments:</u>					
Loans to Group and associated companies (Note 13)	433,884	155,395	1,922,879	(433,884)	2,078,274
Short-term investment securities	77	-	8,183	(46)	8,214
Other loans	486,808	182,400	4,500	(486,808)	186,900
Short-term deposits and guarantees given	1,026	137	376	(195)	1,344
Allowances	(317)	-	-	275	(42)
	<u>921,478</u>	<u>337,932</u>	<u>1,935,938</u>	<u>(920,658)</u>	<u>2,274,690</u>

Details of IBERDROLA Group and associated companies as of 31 December 2006 are as follows:

Company	Location	Line of business	% of ownership by IBERDROLA			Thousands of euros					Dividends received by IBERDROLA in 2006 (Note 15)
			Direct	Indirect	Total	Net value per IBERDROLA books	Capital	Reserves	Profit (Loss)		
Iberdrola Generación, S.A.U. (a)	Bilbao	Energy	100	-	100	3,718,098	1,333,407	2,502,360	922,979	539,552	
Iberdrola Energía, S.A.U. (a)	Madrid	Holding co.	100	-	100	1,900,492	1,477,831	132,910	289,262	-	
Iberdrola Ingeniería y Construcción, S.A.U. (a)	Bilbao	Services	100	-	100	3,065	660	113,244	33,169	-	
Iberdrola International, B.V.	Holland	Finance - Instrumental	100	-	100	388	388	16,316	2,388	-	
Iberdrola Portugal-Electricidade e Gás, S.A. (a)	Portugal	Energy	100	-	100	854,559	200	872,280	19,139	-	
Iberdrola Energías Renovables, S.A.U. (a)	Madrid	Energy	100	-	100	223,566	164,600	408,989	152,098	36,411	
Corporación IBV, Participaciones Empresariales, S.A. (a)	Bilbao	Holding	50	-	50	136,857	228,445	371,902	532,755	150,000	
Amara, S.A.U. (a)	Madrid	Sale of insulated wires, gear electric gear shifts, safety material	100	-	100	3,925	3,606	16,545	4,806	-	
Iberdrola Inmobiliaria, S.A.U. (a)	Madrid	Real estate development	100	-	100	289,668	221,002	361,860	108,751	-	
Investigación y Desarrollo de Equipos Avanzados, S.A.U.	Madrid	Telemarketing	100	-	100	5,381	2,725	1,567	1,089	-	
NEO-SKY 2002, S.A.	Madrid	Telecommunications	94.29	-	94.29	41,841	65,673	(12,336)	(8,962)	-	
Iberdrola Distribución Eléctrica, S.A.U.	Bilbao	Energy	100	-	100	1,770,034	645,210	1,124,824	224	170,719	
Eléctrica Conquense, S.A.	Cuenca	Energy	53.59	-	53.59	1,520	3,087	2,065	378	241	
Anselmo León, S.A. (a)	Valladolid	Energy	100	-	100	20,103	1,082	6,723	4,575	1,187	
Gamesa Corporación Tecnológica, S.A. (a)	Vitoria	Holding Co.	17	7.39	24.39	591,692	41,361	758,337	220,126(b)	2,400	
Iberdrola Inversiones 2010, S.A.	Bilbao	Finance	100	-	100	75,000	75,000	(602)	280	-	
Vector M Servicios de Marketing, S.A.U.	Bilbao	Marketing	100	-	100	3,746	4,410	(440)	(224)	-	
Iberdrola Infraestructuras Gasistas, S.L.	Madrid	Construction	100	-	100	5,138	5,000	110	28	-	
Veo Televisión, S.A.	Madrid	Digital Terrestrial Television	20	-	20	3,519	27,329	(525)	(9,208)	-	
Bahía de Bizkaia Gas, S.L.	Zierbena	Energy	25	-	25	12,847	6,000	78,605	11,654	3,000	
Euskaltel, S.A.	Zamudio	Telecommunications	11.14	-	11.14	43,513	325,200	32,859	32,541	-	
Other companies			-	-	-	14,829	-	-	-	126	
						9,719,781				903,636	

(a) Group parent company. Data for capital, reserves and profit (loss) for 2006 are consolidated. See appendix for details on subsidiaries of 100%-owned IBERDROLA subgroups

(b) Figures to 30 September 2006 reported to the markets by this company.

The detail of “Long-term investments – Long-term investment securities” in the balance sheet at 31 December 2006 is the following:

	Thousands of euros	
	Cost	% of ownership
Long-term investment securities:		
Galp, S.A.	113,238	4%
Medgaz, S.A.	4,683	15.79%
Eutilia, S.A.	3,900	8.50%
Ciudad Real Aeropuertos, S.L.	9,269	9.22%
Refinería Balboa, S.A.	5,000	10%
Other	<u>6,636</u>	-
	<u><u>142,726</u></u>	

The interest in Red Electrica de España, S.A., which amounts to EUR 8,183 thousand, was reclassified under “Short-term investment securities” in the balance sheet at 31 December 2006, since IBERDROLA is obliged to dispose of this investment in 2007.

The details of “Long-term investments – Other loans”, “Long-term trade accounts receivable” and “Short-term financial investments – Other loans” are the following:

	Thousands of euros	Interest rate	Maturity
Other long-term loans			
Home loans	3,217	0.9%	2008 – 2028
Other	<u>46,736</u>	3.82%	2008 – 2024
	<u><u>49,953</u></u>		
Long-term trade accounts receivable			
France Telecom España, S.A.	17,272	EURO LIBOR +0.3%	2008 – 2019
Madrid Municipal Council	7,667	-	2008 – 2014
Other	<u>1,033</u>		
	<u><u>25,972</u></u>		
Other short-term loans			
Short-term cash deposits	90,539	3.6%	2007
Dividends declared but not collected from:			
- Corporación IBV	50,000	-	2007
- Red Eléctrica de España, S.A.	1,319	-	2007
- Iberdrola Generación, S.A.U.	40,002	-	2007
Factoría de Canales, S.A.	4,500	3M EURIBOR + 1.5%	2007
Other	<u>540</u>	-	2007
	<u><u>186,900</u></u>		

Most significant transactions in 2006

The most significant transactions, in 2006 involving IBERDROLA's equity investments were the following:

- On 10 July 2006, IBERDROLA acquired an 11% stake in the share capital of Gamesa Corporación Tecnológica, S.A. from Corporación IBV, Participaciones Empresariales, S.A., a 50%-owned subsidiary of IBERDROLA, for EUR 445,336 thousand. Following the transaction, IBERDROLA's stake in Gamesa Corporación Tecnológica, S.A. stands at 24.39%.
- On 4 July 2006, IBERDROLA participated, in proportion to its holding, in the capital increase carried out by Bahía de Bizkaia Gas, S.L., via the compensation of the EUR 12,000 thousand participating loan it had with this company.
- In 2006, IBERDROLA increased capital of its wholly owned Iberdrola Portugal – Electricidade e Gás, S.A. in EUR 422,250 thousand.
- On 27 February 2006, IBERDROLA transferred to its wholly owned subsidiary, Iberdrola Inmobiliaria, S.A., a member of Tax Group 2/86 of which IBERDROLA is parent, the entire shareholding in Media Park, S.A. for EUR 77,393 thousand. This amount was the investment's value that appeared in IBERDROLA's books.

8. TREASURY STOCK

The movement in this heading during the year was the following:

	No. of shares	Thousands of euros
Balance at 1 January 2006	109,537	1,151
Acquisitions	8,270,501	228,171
Disposals	(8,284,425)	(227,427)
Value adjustments recorded in prior years reversed with credit to reserves (Note 9)	-	(804)
Value adjustments recorded with a charge to profit and loss	-	(46)
Balance at 31 December 2006	<u>95,613</u>	<u>1,045</u>

At 31 December 2006, the Company had a restricted reserve for treasury stock for the full amount of own shares held at that date (see Note 9).

The gain on the disposals of treasury stock in 2006 amounted to EUR 3,317 thousand and is recorded under "Gains on disposal of treasury stock" in the accompanying income statement. Losses for this concept amounted to EUR 2,674 thousand, recorded under "Losses on transactions involving treasury stock" in the 2006 income statement.

9. SHAREHOLDERS' EQUITY

The movement in this heading in 2006 was the following:

	Thousands of euros											
	Capital stock	Additional paid-in capital	Revaluation reserves	Legal reserve	Reserve for treasury stock (Note 8)	Redeemed capital reserve	Other reserves			Total		
							Restricted reserve for converting capital to euros	Voluntary reserves	Retained earnings			
Balance at 1 January 2006	2,704,648	459,577	1,389,408	540,929	1,151	81,708	4,561	879,169	1,046,754	800,501	(330,828)	7,577,578
Distribution of income:												
- Dividends	-	-	-	-	-	-	-	-	-	(797,871)	330,828	(467,043)
- Retained earnings	-	-	-	-	-	-	-	-	2,630	(2,630)	-	-
Transfer between reserves	-	-	-	-	698	-	-	(698)	-	-	-	-
Value adjustment to treasury stock (Notes 4.h and 8)	-	-	-	-	(804)	-	-	-	-	-	-	(804)
Interim dividend (Note 3)	-	-	-	-	-	-	-	-	-	-	(405,697)	(405,697)
Profit for the year												
										940,964	-	940,964
Balance at 31 December 2006	2,704,648	459,577	1,389,408	540,929	1,045	81,708	4,561	878,471	1,049,384	940,964	(405,697)	7,644,998

Share Capital

At 31 December 2006, the capital stock of IBERDROLA consisted of 901,549,181 shares of EUR 3 par value each. These shares are listed on the Spanish Continuous Market (Spanish computerised trading system), are included in the IBEX 35 index and, since September 2003, have been included in the European Eurostoxx 50 index.

Since IBERDROLA's shares are represented by the book-entry system, the exact stakes held by its shareholders are not known. Nonetheless, based on publicly available information, at 31 December 2006 the stakes held by ACS, Actividades de Construcción y Servicios, S.A., Bilbao Bizkaia Kutxa and Banco Bilbao Vizcaya Argentaria, S.A. in the share capital of IBERDROLA, S.A., directly and indirectly, stood at 10.882%, 9.97% and 6.47%, respectively.

At 31 December 2006, the direct and indirect stakes in IBERDROLA held by Board members were the following:

<u>Board member</u>	Number of shares		
	<u>Direct</u>	<u>Indirect</u>	<u>Total</u>
José Ignacio Sánchez Galán	202,472	161,973	364,445
Juan Luis Arregui Ciarsolo	200	18,410,000	18,410,200
Víctor de Urrutia Vallejo	525,000	863,500	1,388,500
José Orbeagozo Arroyo	23,666	476,334	500,000
Lucas M ^a de Oriol López-Montenegro	17,330	162,403	179,733
Ricardo Alvarez Isasi	50,000	1,075,742	1,125,742
Mariano Ybarra y Zubiria	34,001	30,000	64,001
José Ignacio Berroeta Echevarria	2,915	31,476	34,391
Julio de Miguel Aynat	44,521	-	44,521
Sebastián Battaner Arias	13,500	-	13,500
Xavier de Irala Estévez	40,328	-	40,328
Iñigo Victor de Oriol Ibarra	2,214	-	2,214
Inés Macho Stadler	10,000	-	10,000
Braulio Medel Cámara	10,000	-	10,000
José Carlos Pla Royo	1,000	-	1,000
	<u>977,147</u>	<u>21,211,428</u>	<u>22,188,575</u>

At the General Shareholders' Meeting held on 30 March 2006 the Board of Directors was authorised, in accordance with Article 153.1b) of the Spanish Corporations Law, within a 5-year period ending 30 March 2011, if deemed appropriate, to increase its capital stock by as much as one-half, in one or a series of increases, in the amount deemed appropriate, with the exclusion of preemptive subscription rights. At 31 December 2006, the Board of Directors had not availed of this authorization.

Share premium

The Spanish Corporations Law expressly permits the use of this account balance to increase capital and does not establish any specific restrictions as to its use.

Legal reserve

Under the Spanish Corporations Law, 10% of net profit for each year must be transferred to the legal reserve until the balance of this reserve reaches at least 20% of the share capital.

At 31 December 2006, this reserve had reached the threshold established by the aforementioned legislation.

The legal reserve can be used to increase capital provided that the remaining reserve balance does not fall below 10% of the increased share capital amount. Otherwise, until the legal reserve exceeds 20% of capital stock, it can only be used to offset losses, provided that sufficient other reserves are not available for this purpose.

Revaluation reserves

This reserve, included in the balance sheet of the 1996 Annual Accounts, arose as a result of the revaluation of tangible fixed assets made by IBERDROLA pursuant to Royal Decree-Law 7/1996 of 7 June (see Note 4.b).

This balance can be used, free of tax, to offset recorded losses (both prior years' accumulated losses and current year losses) or losses which might arise in the future, and to increase share capital. From 1 January 2007, the balance of this reserve can be taken to unrestricted reserves, provided that the monetary surplus has been realised. The surplus will be deemed to have been realised on the portion on which depreciation has been taken for accounting purposes or if the revalued assets have been transferred or derecognised. If the balance of this account were used in any way other than as specified in Royal Decree-Law 7/1996, it would be subject to tax.

Redeemed capital reserve

Prior to 2001, IBERDROLA decreased capital by redeeming treasury stock, lowering capital stock by EUR 81,708 thousand and voluntary reserves by EUR 238,722 thousand, pursuant to a resolution adopted at the General Shareholders' Meeting held on 25 May 1996.

In accordance with Article 167.3 of the Spanish Corporations Law, IBERDROLA has a restricted "Redeemed capital reserve" amounting to EUR 81,708 thousand, equivalent to the pay value of the decreased capital stock.

10. PROVISIONS FOR CONTINGENCIES AND EXPENSES

a) Provisions for pensions and similar obligations

The movement in 2006 in this heading on the liability side of the balance sheet was as follows:

	Thousands of euros
Balance at 1 January 2006	499,924
Provisions:	
Bylaw-stipulated emoluments (Note 18.a)	16,602
With a charge to income and loss (Notes 4.j and 4.k)	56,782
Less – payments made	<u>(113,322)</u>
Balance at 31 December 2006	<u><u>459,986</u></u>

“Provisions for pensions and similar obligations” in the accompanying balance sheet at 31 December 2006 included coverage of the following commitments (see Notes 4.j and 4.k):

	Thousands of euros
Long-service bonus and electricity for employees	314,946
Voluntary collective redundancy procedure (Note 4.k)	104,258
Other restructuring plans (Note 4.k)	27,605
Board of directors	<u>13,177</u>
	<u><u>459,986</u></u>

b) Provision for taxes and other provisions for contingencies and expenses

The detail of the movement in 2006 in this heading on the liability side of the accompanying balance sheet was as follows:

	Thousands of euros
Balance at 1 January 2006	186,491
Provisions	72,301
Overprovision	(11,641)
Provisions used and payments	(1,358)
Transfers	<u>(141)</u>
Balance at 31 December 2006	<u><u>245,652</u></u>

11. DEBENTURES AND OTHER MARKETABLE DEBT SECURITIES

The detail of outstanding debentures, bonds and commercial paper at 31 December 2006 and their estimated maturity is the following:

	Thousands of euros							Total long-term
	Short-term		Maturity					
	2007	2008	2009	2010	2011	2012 and beyond		
Balance at 12.31.06								
Simple bonds and debentures	507	240,841	121,439	404	402	276	363,362	
Other marketable debt securities (commercial paper)	507	240,841	121,439	404	402	943,050	943,050	
Total	507	240,841	121,439	404	402	943,326	1,306,412	
Unaccrued interest	(10,122)					(10,122)	(10,122)	
	1,296,797	240,841	121,439	404	402	933,204	1,296,290	

The balance of simple bonds and debentures outstanding at 31 December 2006, carried a weighted average annual interest rate of 8.88% considering the related hedges.

The balance of "Other marketable debt securities" at 31 December 2006 carried an average annual interest rate of 3.401%.

All these issues are denominated in euros.

At the General Shareholders' Meeting held 30 March 2006, the Board of Directors was authorised to issue EUR 9,000,000 thousand of five-year convertible bonds and debentures and up to EUR 4,000,000 of commercial paper. At 31 December 2006, it had not exercised this power.

12. PAYABLE TO CREDIT INSTITUTIONS

The maturity of outstanding loans and credits at 31 December 2006, including financial lease instalments pending payment (see Note 4.a), is the following:

<u>Year</u>		<u>Thousands of euros</u>
2007	Short-term	465,010
2008		113,032
2009		240,219
2010		1,443,262
2011		150,626
2012 and beyond		<u>1,745,816</u>
	Long-term	3,692,955

The outstanding loans are denominated in euros or foreign currency. However, at year-end 2006, IBERDROLA had arranged currency (euro swap) and interest-rate swaps to hedge its financial debt (loans, debentures and other marketable securities, see Note 11) for EUR 888,189 thousand and EUR 5,748,671 thousand, respectively (see Note 4.t).

The loans outstanding at 31 December 2006 bear average annual interest of 3.69% considering the related hedges.

These balances correspond to amounts drawn down and pending payment at 31 December 2006. At year-end 2006, IBERDROLA had EUR 13,821,245 thousand of unused loans and credit facilities maturing between 2007 and 2011 and bearing a weighted average interest rate of 5.2%.

Most of the loans taken out by IBERDROLA have certain mandatory terms and covenants regarding balance sheet structure and other economic variables. At 31 December 2006, IBERDROLA was in compliance with all these terms and covenants.

13. BALANCES WITH GROUP AND ASSOCIATED COMPANIES

The detail of short and long-term “Loans to Group and associated companies” in the balance sheet at 31 December 2006 is the following (see Note 7):

	Thousands of euros		
	Short-term	Long-term	Total
Iberdrola Generación, S.A.U.	1,610,565	-	1,610,565
Iberdrola Distribución Eléctrica, S.A.U.	-	540,810	540,810
Iberdrola Energía, S.A.U.(*)	-	649,279	649,279
Iberdrola Inmobiliaria, S.A.U.	230,000	-	230,000
Iberdrola Energías Renovables de Castilla la Mancha, S.A.U	44,379	377,180	421,559
Energyworks do Brasil, Ltda (*)	1,885	6,825	8,710
Planta de Regasificación de Sagunto,S.A.	21,704	-	21,704
Bahia de Bizkaia Electricidad, S.L.	28,455	-	28,455
Tarragona Power, S.L.	113,265	-	113,265
Other Group companies	58	1,510	1,568
Accrued interest pending collection	27,963	-	27,963
	<u>2,078,274</u>	<u>1,575,604</u>	<u>3,653,878</u>

(*) These loans are denominated in US dollars and are shown at the official year-end exchange rate.

The loans bear average interest of 4.25%.

The maturity of long-term receivables is as follows:

<u>Year</u>	<u>Thousands of euros</u>
2008	46,343
2009	107,935
2010	641,342
2011	44,819
2012 and beyond	<u>735,165</u>
	<u>1,575,604</u>

The detail of IBERDROLA’s short-term accounts with Group and associated companies at 31 December 2006 is as follows:

	Thousands of euros	
	Receivable	Payable
<u>Long-term</u>		
Group companies		
Iberdrola Internacional, B.V.	-	3,453,815
Iberdrola Finanzas, S.A.	-	2,528,242
Torre Iberdrola, A.I.E.	-	<u>58,722</u>
	-	<u>6,040,779</u>
	=====	=====
<u>Short-term</u>		
Group companies		
Iberdrola Distribución Eléctrica, S.A.U.	1,924,388	19,918
Iberdrola Energías Renovables de Castilla La Mancha, S.A.U.	655,483	-
Iberdrola Generación, S.A.U.	744,920	12,280
Iberdrola Energías Renovables de Galicia, S.A.U.	449,715	-
Iberdrola Energía, S.A.U.	315,376	-
Ibernova Promociones, S.A.U.	295,552	-
Iberdrola Energías Renovables de Aragón, S.A.U.	157,516	-
Iberdrola Inmobiliaria, S.A.U.	289,035	-
Fuerzas Eléctricas de Navarra, S.A.	122,121	-
Hidroeléctrica Ibérica, S.L.	114,185	-
Iberdrola Energías Renovables, S.A.U.	437,967	-
Ciener, S.A.U.	19,728	-
Energyworks Cartagena, S.L.	38,637	-
Energyworks Vit-Vall, S.L.	59,475	-
Iberdrola Energías Renovables de la Rioja, S.A.	30,997	-
Energyworks Aranda, S.L.	15,788	-
Amara, S.A.U.	27,837	294
Sistemas Energéticos Chandrexa, S.A.	13,001	-
Iberdrola Energías Renovables de Andalucía, S.A.U.	33,074	-
NEO-SKY 2002, S.A.	-	4,730
Iberdrola Inmobiliaria Catalunya, S.A.	43,063	-
S.E. Los Campillos, S.A.	32,654	-
Iberdrola Internacional, BV	-	225,820
Iberdrola Finanzas, S.A.	-	486,986
Iberdrola Cogeneración, S.L.U.	-	15,811
Iberdrola Ingeniería y Construcción, S.A.U.	-	296,548
Iberdrola Infraestructuras Gasistas, S.L.	-	7,784
Iberdrola Operación y Mantenimiento, S.A.	-	13,128
Biovent Holding, S.A.	-	7,649
Eléctrica Conquense, S.A.	-	2,777
Vector M Servicios de Marketing, S.A.	-	3,138
Idea Telemarketing, S.A.	-	3,364
Anselmo León, S.A.	-	2,343
Erne Hueneja Tres, S.L.	5,780	-
Erne Dólar Uno, S.L.	10,809	-
Erne Dólar Dos, S.L.	10,051	-
Erne Dólar Tres, S.L.	11,445	-
Other	<u>34,564</u>	<u>6,725</u>
	<u>5,893,161</u>	<u>1,109,295</u>
	=====	=====
Associated companies		
Tarragona Power, S.L.	11,754	-
Corporación IBV Participaciones Empresariales, S.A.	-	463,692
Bahía Bizkaia Electricidad, S.L.	3,004	-
Nuclenor, S.A.	-	20,409
Other	<u>240</u>	<u>(1,506)</u>
	<u>14,998</u>	<u>482,595</u>
	=====	=====

In general, except for the amount payable to Iberdrola International B.V. described in this Note, the aforementioned balances with Group companies arose from normal business transactions and/or IBERDROLA's own cash management. They do not have any set maturity and are settled quarterly and annually, bearing interest indexed to market rates.

At 31 December 2006, Iberdrola International B.V. and Iberdrola Finanzas, S.A. had granted loans to IBERDROLA for the amounts of various debt issues in foreign currency made by them and underwritten by IBERDROLA (see Note 17). The maturities of these unpaid loans at 31 December 2006 were as follows:

<u>Maturity</u>	<u>Thousands of euros</u>
2007	618,223
2008	555,503
2009	1,215,000
2010	1,390,585
Other	<u>2,820,969</u>
	<u>6,600,280</u>

At 31 December 2006, these loans bore average annual interest of 3.71%.

Accrued interest payable at year end amounted to EUR 94,583 thousand and is recorded under "Current liabilities – Payable to Group companies" in the accompanying balance sheet.

14. TAX MATTERS

In 2006, IBERDROLA, S.A., as the Parent of Tax Group 2/86, filed a consolidated income tax return in Spain. The Group will continue to be taxed under this tax regime indefinitely for as long as the related requirements are met and the Group does not expressly waive application of the regime by filing the related taxpayer registration form.

In past years, IBERDROLA was involved in a series of corporate restructuring moves under the tax regime provided for under Chapter VIII, Title VII of the revised Spanish Corporate Income Tax Law enacted by Legislative Royal Decree 4/2004 of 5 March. The disclosures required under this law are provided in the notes to the Annual Accounts of the years in which the transactions took place.

The reconciliation of the profit per books to the taxable income for corporate income tax purposes for 2006 is as follows:

	Thousands of euros		Amount
	Increase	Decrease	
Profit before taxes			998,258
Permanent differences	164,670	(22,952)	141,718
Temporary differences	31,596	(98,358)	<u>(66,762)</u>
Taxable income			<u><u>1,073,214</u></u>

The difference between the tax charge allocated to 2006 and the tax payable for that year, which is recorded under "Long-term taxes receivable/taxes payable" or "Short-term taxes receivable/taxes payable" as appropriate, in the balance sheet at 31 December 2006, arose mainly as a result of the following:

- Temporary differences derived mainly, for the purpose of determining the taxable income for corporate income tax purposes for each year, from the tax effect of expenses recorded for pension commitments and the voluntary collective redundancy procedure (see Note 4.k).
- Temporary differences arising from changes in allowances for investment securities that are not deductible in the year in which they are recorded, for a net amount of EUR 1,578 thousand (positive difference).
- Temporary differences derived from the differences in accounting and tax criteria for recognising certain allocations to provisions and the accounting and tax depreciation of certain items.

The accrued corporate income tax expense for 2006 was calculated as follows:

	Thousands of euros
Profit before taxes	998,258
Permanent differences	<u>141,718</u>
Adjusted income	<u><u>1,139,976</u></u>
Gross tax at 35%	398,992
Deductions (a)	(331,570)
Effect of consolidated taxation:	
- Intergroup dividends (b)	(202,041)
- Provision for marketable securities (c)	(65,284)
- Correction for deductions (b)	202,041
Other effects (d)	6,795
Adjustment to tax rate (e)	<u>48,361</u>
Accrued corporate income tax expense	<u><u>57,294</u></u>

- (a) The tax credits taken by IBERDROLA, which basically correspond to deductions for double taxation, include a total of EUR 1,841 thousand relating to the tax credit for reinvestment of capital gains whose base was EUR 9,204 thousand. Pursuant to Articles 42 and 75 of the revised Spanish Corporate Income Tax Law of 5 March, which regulates this tax credit, it is hereby stated that the total amount obtained in the transfer has been reinvested by the companies belonging to tax group 2/86, and that the assets in which the reinvestment was made in order to meet the commitment are still owned.
- (b) This mainly relates to eliminating from tax payable the effect of dividends received by companies in the tax group and the elimination of the tax credit for double taxation on these dividends.
- (c) Changes in 2006 in allowances for investment securities related to the allocation/application of the provision for IBERDROLA, S.A.'s stake in IBERDROLA ENERGÍA, S.A.U. and other companies eliminated on tax consolidation as they belong to Tax Group 2/86.
- (d) Income tax incurred abroad.
- (e) Expense derived from the recalculation, pursuant to the change in tax regulations approved in November 2006, of pre-paid and deferred taxes and taxes pending reversal at 31 December 2006 according to the estimated tax rate at the time of the reversal.

The commitments and obligations arising from the tax benefits of which IBERDROLA availed itself in 2006 and prior years were met (and are currently being met) by the companies belonging to Tax Group 2/86, in the terms provided for in the revised Spanish Corporate Income Tax Law, enacted by Legislative Royal Decree 4/2004 of 5 March.

Specifically, IBERDROLA took tax credits in previous years on the capital gains obtained from the disposal of tangible fixed assets and hereby states that the full amount of the disposals has been reinvested in assets that it still owns in order to meet the commitment.

The detail of "Taxes receivable" and "Taxes payable" on the asset and liability sides, respectively, of the balance sheet of IBERDROLA, S.A. at 31 December 2006 is as follows:

	Thousands of euros	
	Short-term	Long-term
Taxes receivable		
Prepaid income tax due to:		
Accrued expenses for		
pensions and other similar obligations	-	226,410
Other	68,820	125
VAT refundable	1,853	-
Corporate tax refundable	159,629	-
Sundry taxes receivable	771	-
Social security taxes receivable	<u>23,358</u>	-
	<u>254,431</u>	<u>226,535</u>
Taxes payable		
Deferred income tax due to:		
Value adjustments to fixed assets	-	4,978
Other	-	11,964
VAT payable	41,593	-
Taxes payable for withholdings	5,536	-
Other	20,606	-
Social security taxes payable	1,866	-
Corporate income tax payable	<u>4,936</u>	-
	<u>74,537</u>	<u>16,942</u>

In general, IBERDROLA has open for review by the tax inspection authorities the year 2002 and subsequent years for the main taxes applicable to it, except for corporate income tax, for which 2001 and subsequent years are open.

In 2006, an injunction was imposed on part of Bizkaia corporate tax legislation applicable to some subsidiaries and associated companies (Provincial Regulatory Decree 1/2005 of 30 December). The ruling is not final as official appeals have been filed and as it has not been published in the Official Gazette of Bizkaia.

These subsidiaries have calculated the amounts corresponding to this tax for 2006 and for those years open to inspection in accordance with provincial regulations in effect at the end of each year given that they consider that the final resolution of the appeals filed will not have a significant effect on the Annual Accounts taken as a whole.

As a result of inspections by the tax authorities, tax assessments have been raised against several Group subsidiaries. The Group has signed in protest and appealed some of these.

The directors of IBERDROLA, S.A. and, where appropriate, its tax advisors consider that no significant liabilities would arise for IBERDROLA in the event of a review of the years open to inspection or as a result of the matters mentioned in the paragraphs above.

15. REVENUES AND EXPENSES

Net revenues

The detail of this heading in the accompanying income statement is the following:

	Thousands of euros
Sales	
Billed power supplied to end customers	760,644
Electricity billed in 2006 for energy supplied in 2005	(119,754)
Unbilled power supplied to end customers in the year (Note 4.g)	30,854
Gas billed to end customers in the year	1,539,949
Gas billed in 2006 related to gas supplied in 2005	(67,776)
Unbilled gas supplied (Note 4.g)	32,577
Sales of telecommunications services	41,362
Sales of goods and services	<u>249,979</u>
	<u>2,467,835</u>
Services	
Rights to inspection, and coupling and meter rentals (Note 4.q)	118,698
Other	<u>53</u>
	<u>118,751</u>
	<u><u>2,586,586</u></u>

The breakdown of billed electricity and gas sales by autonomous community in Spain and sales to companies abroad is the following:

	Thousands of euros
Net billed power sales	
Basque Country	177,404
Madrid	166,149
Castilla-León	147,941
Navarre	131,001
La Rioja	11,056
Extremadura	12,238
Castilla-La Mancha	143,335
Comunidad Valenciana	406,654
Murcia	71,275
Catalonia	216,305
Aragon	11,367
Asturias	4,364
Cantabria	9,410
Galicia	26,372
Andalusia	396,142
Balearic and Canary Islands	4,833
 Power sales to companies abroad	 <u>364,747</u> <u>2,300,593</u>

Procurements

The detail of this heading the accompanying income statement for 2006 is as follows:

	Thousands of euros
Purchases	
Power purchases from the wholesale electricity production market	161,570
Gas purchases	1,362,140
Changes in inventories	(35,586)
Other power purchases	305,024
Other supplies	<u>106,816</u> <u>1,899,964</u>
 Other external expenses	
Services received for the use of networks for the supply of:	
- Electricity	227,929
- Gas	111,638
Other external expenses	<u>67</u> <u>339,634</u>

Employee welfare expenses

The detail of this heading in the accompanying income statement for 2006 is the following:

	Thousands of euros
Employer social security costs	20,031
Additional provisions for pensions and similar obligations and defined contributions to the external pension plan (Note 4.j)	18,694
Bylaw-stipulated directors' emoluments (Note 18.a)	16,602
Other employee welfare expenses	<u>13,406</u>
	<u><u>68,733</u></u>

Transactions with Group and associated companies

The principal transactions carried out by IBERDROLA with Group and associated companies in 2006 affecting revenues and expenses in the year were the following:

		Thousands of euros									
		Sales	Procurements	Other operating expenses for services rendered	Personnel expenses	Operating revenues from services rendered	Interest expenses	Interest income	Dividends received	Purchases of fixed assets	Extraordinary expenses
Group companies:											
Dedicated to power-related activities:											
-	Generation	668,637	257,334	-	-	112,859	845	183,573	575,963	-	-
-	Transmission and distribution	126,704	201,206	2,766	14,443	174,882	227	82,088	172,273	144	-
-	Other	87	2,994	2,738	-	453	88	9,323	-	-	650
	Dedicated to other activities	2,898	19,385	19,742	-	16,240	272,813	21,231	-	13,001	-
Associated companies:											
Dedicated to power-related activities		186,825	72,818	-	-	-	1,220	7,730	3,000	-	-
Dedicated to other activities		135	-	-	-	(92)	10,172	-	152,400	-	-
		<u>985,286</u>	<u>553,737</u>	<u>25,246</u>	<u>14,443</u>	<u>304,342</u>	<u>285,365</u>	<u>303,945</u>	<u>903,636</u>	<u>13,145</u>	<u>650</u>

Variation in allowances for intangible assets, tangible fixed assets and long-term investments

The detail of this heading in the accompanying income statement for 2006 is as follows:

	<u>Thousands of euros</u>
Long-term investments:	
Iberdrola Energía, S.A.U.	(91,672)
Euskaltel	(2,646)
Investigación y Desarrollo de Equipos Avanzados, S.A.	(1,088)
NEO-SKY 2002, S.A.	8,452
Veo TV	1,828
Other	<u>238</u>
	(84,888)
Tangible fixed assets:	
Allowances for decline in value of tangible fixed assets (Note 6)	<u>(3,283)</u>
	<u>(88,171)</u>

Extraordinary expenses

The detail of this heading in 2006 is as follows:

	<u>Thousands of euros</u>
Provision for pensions and similar obligations for restructuring plans (Notes and 4.k)	41,769
Allocation to provision for contingencies and expenses	38,953
Other	<u>6,112</u>
	<u>86,834</u>

Extraordinary income

The detail of this heading in the income statement for the year ended 31 December 2006 is the following:

	<u>Thousands of euros</u>
Long-service bonuses and electricity for employees (Note 4.j)	(11,415)
Voluntary collective redundancy procedure (Note 4.k)	18,229
Reversal of provision for taxes and other provisions for contingencies and expenses	10,563
Other	<u>1,370</u>
	<u>18,747</u>

Gains on disposal of intangible assets, tangible fixed assets and long-term investments

The detail of this heading in 2006 is the following:

	<u>Thousands of euros</u>
Sale of buildings	9,890
Sale of land	2,291
Other	<u>94</u>
	<u><u>12,275</u></u>

Employees

The average number of employees at IBERDROLA in 2006, by professional category, was the following:

	<u>Thousands of euros</u>
University graduates	770
Associate degree graduates	458
Other	<u>782</u>
	<u><u>2,010</u></u>

The preceding table does not include the 46 employees included under the "special labour situation" (see Note 4.k).

16. SEGMENT REPORTING BY BUSINESS

IBERDROLA has decided not to disclose business segment information, as it would not be representative because the company is basically a holding company.

17. GUARANTEES WITH THIRD PARTIES AND OTHER CONTINGENT LIABILITIES

At 31 December 2006, IBERDROLA had provided guarantees to other companies, as detailed below:

	Thousands of euros
Veo Televisión	2,404
Elcogás, S.A.	32,625
Tirme, S.A.	20,547
Iberdrola Energía Monterrey, S.A. de C.V.	262,352
Iberdrola Energía Altamira, S.A.	228,962
Energyworks Fonz, S.L.	6,885
Energyworks Monzón, S.L.	15,925
Iberdrola Ingeniería y Construcción, S.A.	1,255,498
Neo Sky 2002, S.A.	6,382
	<u>1,831,580</u>

IBERDROLA has provided guarantees amounting to EUR 34,132 thousand to the Mexican Federal Electricity Commission to secure electricity supplies and the completion of combined cycle plants and EUR 1,099,231 thousand to MEF Service, S.A. for operating in the electricity pool. The Company has also provided a total of EUR 439,737 thousand of counter-guarantees for various bank loans to Group companies.

The Company has also underwritten various bond issues placed by Group companies Iberdrola Finanzas, S.A. and Iberdrola International, B.V. (see Note 13).

IBERDROLA considers that any liabilities that could arise from the guarantees provided at 31 December 2006 would not be material.

18. DIRECTORS' REMUNERATION

a) 2006 bylaw-stipulated remuneration

Article 50 of IBERDROLA's bylaws provides that "the Company shall assign, as an expense, an amount equal to up to 2% of the profit obtained in the year by the consolidated Group" for directors' remuneration.

The Board of Directors has agreed to propose at the General Shareholders' Meeting bylaw-stipulated remuneration of 1% of 2006 consolidated net profit (1.25% in 2005). In 2006 and 2005 bylaw-stipulated remuneration would accordingly amount to EUR 16,602 thousand and 17,276 thousand, respectively, which was lower than the limit provided for in Article 50 of the bylaws of IBERDROLA. These amounts were recognised with a charge to "Personnel expenses" on the accompanying income statements (see Note 15).

The breakdown of the remuneration of EUR 16,602 thousand and EUR 17,276 thousand is as follows:

Bylaw-stipulated directors' emoluments

The bylaw-stipulated directors' emoluments paid to the current directors with a charge to the aforementioned bylaw-stipulated directors' remuneration amounted to EUR 4,141 (*) thousand and EUR 3,741 thousand in 2006 and 2005, respectively. The amounts received by the directors depend on the duties assigned to them, the detail being as follows:

	Thousands of euros	
	2006	2005
Chairmen	595	447
Deputy chairmen	926	769
Committee members	1,737	1,628
Directors	<u>883</u>	<u>897</u>
	<u>4,141</u>	<u>3,741</u>

(*) These amounts include bylaw-stipulated remuneration for members of the Board of Directors that stepped down from their positions during the year.

Attendance fees

The attendance fees paid to the directors with a charge to the bylaw-stipulated directors' remuneration amounted to EUR 707 thousand and EUR 839 thousand in 2006 and 2005, respectively.

Insurance premiums

The premium incurred in order to cover benefits in the event of the death or disability of the current directors amounted to EUR 262 thousand and EUR 284 thousand in 2006 and 2005, respectively.

The premium paid to cover directors' civil liability insurance in the same years was EUR 704 thousand and EUR 732 thousand, respectively.

Other

Finally, payments for external services and compensation in kind in 2006 and 2005 amounted to EUR 1,170 thousand and EUR 1,468 thousand, respectively. The undistributed bylaw-stipulated remuneration in 2006 and 2005 amounted to EUR 9,618 thousand and EUR 9,725 thousand, respectively.

b) Previous years' bylaw-stipulated remuneration

Credits were made in 2006 to unpaid previous years' bylaw-stipulated remuneration for the following concepts:

Fixed remuneration

The outgoing Chairman's services contract gave rise to compensation of EUR 9,300 thousand and EUR 1,200 thousand in 2006 and 2005, respectively.

Variable remuneration

Variable remuneration received by the members of the Board of Directors of IBERDROLA who discharged executive duties amounted to EUR 1,000 thousand.

Life insurance premiums

The premium for regularising the insurance policy covering the vested pensions of the retired directors in 2006 and 2005 amounted to EUR 483 thousand and EUR 365 thousand, respectively.

Provisions and guarantees provided by the Company for the directors.

This heading includes EUR 5,280 of insurance premiums and EUR 1,470 thousand of severance paid to directors terminated, both concepts charged to prior years' bylaw-stipulated directors' remuneration, compared to EUR 122 thousand of termination benefits paid with a charge to the 2005 bylaw-stipulated directors' remuneration.

Other

An additional EUR 165 thousand were paid for external services.

c) Other remuneration

The remuneration received in 2006 and 2005 by the members of the Board of Directors of IBERDROLA who discharged executive duties and included under "Personnel expenses" in the accompanying income statement, amounted to EUR 1,750 thousand and EUR 1,147 thousand, respectively, of fixed remuneration; EUR 1,111 thousand and EUR 1,058 thousand, respectively, of variable remuneration; and EUR 567 thousand and EUR 733 thousand, respectively, relating to the amount of the life insurance premiums.

The sum of the remuneration relating to the bylaw-stipulated directors' remuneration and those reflected under other headings in the accompanying 2006 and 2005 income statements is lower than the limit established in Article 50 of the bylaws of IBERDROLA for the bylaw-stipulated directors' remuneration.

At 31 December 2006 and 2005, the IBERDROLA Group had not granted any loans or advances to the members of the Board of Directors of IBERDROLA.

In compliance with the terms of article 127 ter section 4 of the Spanish Corporations Law, the members of the Company's Board of Directors confirm that they hold equity investments and hold positions/perform duties (if any) in the following companies whose activities are identical, similar or complementary to that which comprises the Company's corporate purpose:

<u>Director</u>	<u>Company</u>	<u>% of ownership</u>	<u>Position or functions</u>
Juan Luis Arregui Ciarsolo	Gamesa Corporación Tecnológica, S.A.	0.465	Director
José Orbegozo Arroyo	Fanox Electronic, S.L.	5.220	None
Lucas María de Oriol López-Montenegro	Endesa, S.A.	0.000	None
Lucas María de Oriol López-Montenegro	Empresa de Alumbrado Eléctrico de Ceuta, S.A.	1.450	None
Julio de Miguel Aynat	Metrovacesa, S.A.	0.001	Director
Sebastián Battaner Arias	Gamesa Corporación Tecnológica, S.A.	0.001	None
Iñigo Victor de Oriol Ibarra	Empresa de Alumbrado Eléctrico de Ceuta, S.A.	0.000	Director
Braulio Medel Cámara	Abertis Infraestructuras, S.A.	0.001	Director

Following is the information required under the aforementioned legislation concerning the performance by the directors, as independent professionals or as employees, of activities that are identical, similar or complementary to the activity that constitutes the corporate purpose of IBERDROLA:

<u>Director</u>	<u>Company</u>	<u>Position or functions</u>
Xabier de Irala Estévez	Euskaltel, S.A.	Director
Braulio Medel Cámara	Aguagest Sur, S.A.	Chairman

19. REMUNERATION OF SENIOR EXECUTIVES

The staff costs (salary, compensation in kind, social security costs, pension schemes, etc.) relating to senior executives amounted to EUR 10,049 thousand and EUR 10,365 thousand in 2006 and 2005, respectively, and these amounts are recorded under "Personnel expenses" in the accompanying 2006 and 2005 income statements.

The foregoing figures do not include the wages and salaries, share option plans or contributions made by the Company to the "IBERDROLA Pension Plan" received by the members of the Board of Directors of IBERDROLA with executive duties, since they are disclosed in Note 18.

The employment contracts of the senior executives, including executive directors of IBERDROLA or of the Group contain golden parachute clauses for cases of termination or changes of control. These contracts have to be approved by the Company's Board of Directors.

IBERDROLA has been including this type of clause in the contracts of its executives since the nineties; however, most contracts containing golden parachute clauses were entered into in October 2000. A total of 84 executives, including the Company's senior executives, have contracts of this nature.

The objective is to achieve a level of loyalty among top-ranking executives that is effective and sufficient for the management of IBERDROLA and thereby avoid the loss of experience and skills that could jeopardise the achievement of strategic objectives. In essence, these clauses recognise termination benefits based on the length of service at the Company of the members of the executive team, with annual salary payments ranging from a minimum of one to a maximum of five years.

In 2006 and 2005 there were no transactions with executives other than those carried out in the ordinary course of the Group's business.

20. FINANCIAL POSITION AND EVENTS AFTER 31 DECEMBER 2006

In order to finance its investments planned for 2007 and to fund the cash needs arising from its financial position at 31 December 2006, IBERDROLA will need to obtain new funding of approximately EUR 13,090,612 thousand. Of this amount, EUR 11,846,612 thousand correspond to financing needs in connection with the acquisition of Scottish Power Plc. (see Note 22).

As indicated in Note 12 and taking into consideration the amounts described in Note 22, at 31 December 2006, IBERDROLA had approximately EUR 13,821,425 thousand of unused loans and credit facilities, of which EUR 11,846,612 thousand related to a bridge loan to fund the acquisition of Scottish Power Plc. and leaving EUR 1,974,813 thousand available to meet the rest of the IBERDROLA Group's financing requirements.

This figure, together with EUR 250,000 thousand of loans and debt issuances contracted after year-end and prior to the preparation of these Annual Accounts, guarantee that the Group's cash needs for 2007 will be fully covered.

21. FEES FOR SERVICES PROVIDED BY AUDITORS

Audit fees of the 2006 Annual Accounts of the various companies which comprise the IBERDROLA Group and subsidiaries by the main auditor and related companies amounted to EUR 3,218 thousand, of which EUR 947 thousand correspond to IBERDROLA. Audit fees paid to other auditors for the audit of the Annual Accounts of other Group companies amounted to EUR 742 thousand.

In addition, fees paid during the year for other services rendered by the principal auditor and related companies to Group companies in 2006 amounted to EUR 654 thousand, of which EUR 182 thousand corresponded to services provided to IBERDROLA. Fees paid for other services rendered by other auditors for this concept amounted to EUR 1,768 thousand.

22. TAKEOVER BID FOR SCOTTISH POWER, PLC.

On 27 November 2006, the Boards of IBERDROLA and Scottish Power, Plc. (hereinafter, SCOTTISH POWER), a UK energy generator and distributor, reached agreement on the terms of a takeover agreement by which IBERDROLA, directly or via a wholly owned subsidiary, will acquire the shares of SCOTTISH POWER. The Board of Directors of SCOTTISH POWER voted unanimously in favour of the transaction.

By virtue of the aforementioned agreement, IBERDROLA will acquire all the outstanding shares of SCOTTISH POWER, including those issued as a result of the potential exercise of the conversion rights on SCOTTISH POWER Class B shares, in exchange for a combination of cash and new IBERDROLA shares to be received by shareholders of SCOTTISH POWER and SCOTTISH POWER ADS holders pursuant to the following exchange ratio:

- For every SCOTTISH POWER share, 400 pence sterling and 0.1646 new IBERDROLA shares.
- For every SCOTTISH POWER ADS, 1,600 pence sterling and 0.6584 new IBERDROLA shares.

In addition, SCOTTISH POWER will declare an extraordinary dividend of 12 pence sterling for every SCOTTISH POWER share and 48 pence sterling for every SCOTTISH POWER ADS tendered in the bid.

The transaction values each SCOTTISH POWER share at 777 pence sterling and its ordinary share capital at approximately 11,600 million pounds sterling (based on calculations made on 27 November 2006).

The portion of the deal funded with cash will be financed through credit facilities taken out with a series of banks. IBERDROLA has obtained firm financing commitments totalling 7,955 million pounds sterling (EUR 11,738 million based on calculations made on 27 November 2006) from ABN Amro Bank NV, Barclays Capital and The Royal Bank of Scotland to finance the cash component of the bid and to refinance certain elements of SCOTTISH POWER's existing borrowings.

IBERDROLA believes the transaction will give rise to:

- The third largest energy group in Europe.
- Installed generation capacity at the resulting newco of 36,603 MW with 21.4 million points of supply based on figures at 30 September 2006.
- 5,700 MW of installed wind generation capacity and 333 MW of mini hydro generation capacity, making the resulting newco the largest global player in renewable energies.
- Annual savings before tax and capital expenditure of at least 88 million pounds sterling and average capex savings of an estimated 30 million pounds sterling.

The transaction schedule contemplates that the acquisition will be approved at the General Shareholders' Meetings of IBERDROLA and SCOTTISH POWER by the end of March 2007 and for the deal to close before the end of April 2007.

23. STATEMENT OF SOURCE AND APPLICATION OF FUNDS

The funds obtained in 2006, their sources and applications in fixed assets or working capital for the years ended 31 December 2006 and 2005, are the following:

	Thousands of euros	
	2006	2005
Sources of funds:		
Funds obtained from operations	1,075,853	727,008
Other deferred revenues	3,205	1,798
Long-term loans	2,912,875	8,658,806
Unpaid portion of equity investments	-	59,816
Disposal of tangible fixed assets	30,266	367,353
Disposal of treasury stock	228,070	-
Long-term trade accounts receivables	16,552	12,865
Early repayment or transfer to short-term of long-term investments	<u>3,415,487</u>	<u>1,096,565</u>
Total funds obtained	7,682,308	10,924,211
Application of funds:		
Debt arrangement expenses and other deferred expenses	4,177	14,169
Fixed asset additions		
- Intangible fixed assets	26,668	30,162
- Tangible fixed assets	96,933	84,665
- Long-term investments	1,535,709	2,532,860
Treasury stock	228,171	319,495
Dividends	872,740	729,384
Repayment or transfer to short-term of long-term debt	1,572,272	5,521,141
Provisions for contingencies and expenses	115,130	106,856
Unpaid portion of equity investments	55,356	4,474
Long-term trade accounts receivables	-	3,452
Total funds applied	<u>4,507,156</u>	<u>9,346,658</u>
Increase in working capital	<u><u>3,175,152</u></u>	<u><u>1,577,553</u></u>
Variation in working capital		
Inventories	35,586	20,275
Accounts receivable	1,366,162	1,594,533
Accounts payable	411,299	670,329
Short-term investments	1,353,212	(717,187)
Accrual accounts	<u>8,893</u>	<u>9,603</u>
Increase in working capital	<u><u>3,175,152</u></u>	<u><u>1,577,553</u></u>

The reconciliation of income in 2006 and 2005 to the funds obtained from operations is as follows:

	Thousands of euros	
	2006	2005
Profit for the year	940,964	800,501
Add:		
Provisions for pensions and for contingencies and expenses	146,694	326,371
Amortisation of deferred charges	26,966	24,294
Losses on intangible assets, tangible fixed assets and long-term investments	-	522
Losses on transactions involving treasury stock	2,674	1,696
Prepaid corporate income tax	73,557	37,611
Value adjustments of treasury stock	46	-
Exchange losses	-	180
	<u>249,937</u>	<u>390,674</u>
Less:		
Variation in allowances for fixed assets	81,970	206,139
Overprovision for contingencies and expenses	11,641	1,932
Deferred corporation income tax	2,424	72,289
Value adjustment to treasury stock	-	223
Capital subsidies transferred to income for the year	-	756
Gains on disposal of intangible assets, tangible fixed assets and long-term investments	12,275	174,190
Gains on disposal of treasury stock	3,317	4,177
Other deferred revenues	3,236	4,461
Exchange gains	185	-
	<u>115,048</u>	<u>464,167</u>
Funds obtained from operations	<u><u>1,075,853</u></u>	<u><u>727,008</u></u>

24. EXPLANATION ADDED FOR TRANSLATION TO ENGLISH

These Annual Accounts are presented on the basis of accounting principles generally accepted in Spain. Consequently, certain accounting practices applied by the Company may not conform with generally accepted accounting principles in other countries.

**ADDITIONAL INFORMATION RELATED TO SUBSIDIARIES AND ASSOCIATED COMPANIES OF THE IBERDROLA
GENERACION SUBGROUP IN 2006**

Company	Location	Line of business	% of ownership of		Thousands of euros		Auditor
			Iberdrola	Capital and reserves at	Profit (loss)	Auditor	
SUBSIDIARIES							
Iberdrola Generación, S.A.U.	Bilbao	Energy	100.00	3,718,098	863,960	Ernst & Young	
Fuerzas Eléctricas de Navarra, S.A.	Navarre	Energy	100.00	50,285	8,464	Ernst & Young	
Hidroeléctrica Ibérica, S.L.	Bilbao	Energy	100.00	54,219	5,804	Ernst & Young	
Iberduero, S.L.U.	Bilbao	Energy	100.00	4,206	(9)	-	
Navidul Cogeneración, S.A.	Madrid	Energy	55.00	1,811	(253)	Ernst & Young	
Iberdrola Cogeneración, S.L.	Madrid	Holding	100.00	37,337	(437)	Ernst & Young	
Energyworks Cartagena, S.L.	Murcia	Energy	99.00	9,720	14,803	Ernst & Young	
Energyworks Villarrobledo, S.L.	Albacete	Energy	99.00	30	1,034	Ernst & Young	
Energyworks Aranda, S.L.	Burgos	Energy	99.00	142	831	Ernst & Young	
Energyworks Carballo, S.L.	La Coruña	Energy	99.00	1,095	61	Ernst & Young	
Energyworks San Millán, S.L.	León	Energy	90.00	1,961	423	Ernst & Young	
Energyworks Milagos, S.L.	Burgos	Energy	72.81	2,150	596	Ernst & Young	
Energyworks Fonz, S.L.	Huesca	Energy	77.18	1,354	(38)	Ernst & Young	
Energyworks Monzón, S.L.	Huesca	Energy	80.68	3,177	(104)	Ernst & Young	
Energyworks Vit-Vall, S.L.	Vitoria	Energy	99.00	(560)	(6,703)	Ernst & Young	
Iberdrola Operación y Mantenimiento, S.A.U.	Madrid	Services	100.00	6,267	3,058	Ernst & Young	
Energyworks Venezuela, S.A.	Venezuela	Energy	100.00	2,533	612	-	
Centrales Nucleares Almaraz - Trillo, A.I.E.	Madrid	Energy	51.41	-	-	Deloitte	

Company	Location	Line of business	Thousands of euros			Auditor
			% of ownership of Iberdrola	Capital and reserves at 12.31.06	Profit (loss) for the year	
ASSOCIATED COMPANIES						
Nucleon, S.A.	Cantabria	Energy	50.00	79,601	64,751	Deloitte
Bahía de Bizkaia Electricidad, S.L.	Vizcaya	Energy	25.00	76,482	79,109	Deloitte
Asociación Nuclear Ascó - Vandellós II, A.I.E.	Barcelona	Energy	14.59	19,232	-	Deloitte
Tarragona Power Subgroup	Tarragona	Energy	50.00	47,536	(13,163)	Ernst & Young
Azuvi Cogeneración, S.A.	Castellón	Energy	50.00	1,117	(758)	Deloitte
Cofrusa Cogeneración, S.A.	Murcia	Energy	50.00	622	(446)	Other
Cogeneración Gequisa, S.A.	Álava	Energy	50.00	1,204	(240)	PWC
Cogeneración Tierra Atomizada, S.A.	Castellón	Energy	50.00	4,294	(574)	Other
Enercrisa, S.A.	Madrid	Energy	50.00	1,728	1,416	KPMG
Energía Portátil de Cogeneración, S.A.	Guipúzcoa	Energy	50.00	2,688	1,374	Other
Genfibre, S.A.	Burgos	Energy	50.00	1,716	60	Other
Hispagen, S.A.	Burgos	Energy	50.00	296	4,450	Other
Intermalta Energía, S.A.	Navarre	Energy	50.00	1,274	(114)	Ernst & Young
Italcogeneración, S.A.	Castellón	Energy	50.00	2,021	181	Other
Peninsular de Cogeneración, S.A.	Madrid	Energy	50.00	14,092	726	KPMG
S.E.D.A. Cogeneración, S.A.	Palencia	Energy	50.00	908	78	Ernst & Young
Zirconio Cogeneración, S.A.	Castellón	Energy	50.00	378	124	Other
Tirme, S.A.	Mallorca	Energy	20.00	21,118	4,430	Deloitte
Fudepor, S.L.	Murcia	Energy	50.00	4,376	(960)	Other
Elcogás, S.A.	Madrid	Energy	11.96	37,498	(14,259)	-
Tecnatom, S.A.	Madrid	Energy	30.00	20,324	1,692	Ernst & Young
Desarrollo Tecnológico Nuclear, S.L.	Madrid	Services	43.45	162	(142)	Other

**ADDITIONAL INFORMATION RELATED TO SUBSIDIARIES AND ASSOCIATED COMPANIES OF THE IBERDROLA
ENERGÍA SUBGROUP IN 2006**

Company	Location	Line of business	% of ownership of Iberdrola Energía, S.A. at 12.31.06	Thousands of euros		Auditor
				Capital, reserves and translation differences at 12.31.06 (a)	Profit (loss) for the year (a)	
SUBSIDIARIES						
Iberdrola Energía, S.A.U.	Madrid	Holding	100.00	1,673,980	228,384	Ernst & Young
Iberdrola Inversiones, S.U.L.	Portugal	Holding	100.00	39,013	(449)	-
Empresa de Luz y Fuerza Eléctrica de Oruro, S.A.	Bolivia	Energy	58.85	3,473	1,062	Ernst & Young
Electricidad de La Paz, S.A.	Bolivia	Energy	56.77	37,115	2,904	Ernst & Young
Compañía Administradora de Empresas - Bolivia, S.A.	Bolivia	Services	59.26	1,516	1,200	Ernst & Young
Iberdrola de Inversiones, S.R.L. de C.V.	Bolivia	Holding	99.99	36,849	2,092	Ernst & Young
Empresa de Servicios, S.A.	Bolivia	Energy	55.73	1,076	321	Ernst & Young
Iberbolivia de Inversiones, S.A.	Bolivia	Holding	63.39	59,328	3,336	Ernst & Young
Iberdrola Energía do Brasil, Ltda.	Brazil	Holding	99.99	2,932	(1,116)	Ernst & Young
Iberdrola México, S.A. de C.V.	Mexico	Holding	99.99	518,871	(4,764)	Ernst & Young
Enertek, S.A. de C.V.	Mexico	Energy	99.99	69,283	10,043	Ernst & Young
Iberdrola Energía Altamira, S.A. de C.V.	Mexico	Energy	99.99	161,620	17,119	Ernst & Young
Iberdrola Energía Altamira de Servicios, S.A. de C.V.	Mexico	Services	99.99	1,299	167	Ernst & Young
Cinergy, S.R.L. de C.V.	Mexico	Services	99.99	185	(33)	Ernst & Young
Servicios Industriales y Administrativos del Noreste, S.R.L. de C.V.	Mexico	Services	51.12	2,538	58	Ernst & Young
Iberdrola Energía Monterrey, S.A. de C.V.	Mexico	Energy	99.99	109,737	17,044	Ernst & Young
Iberdrola Servicios Monterrey, S.A. de C.V.	Mexico	Services	99.99	22	(22)	Ernst & Young
Iberoamericana de Energía Ibener, S.A.	Chile	Energy	94.74	103,677	15,333	Ernst & Young

ANEXO I

Company	Location	Line of business	% of ownership of Iberdrola Energía, S.A. at 12.31.06	Thousands of euros			Auditor
				Capital, reserves and translation differences at 12.31.06 (a)	Profit (loss) for the year (a)		
Iberdrola Energía Chile, Ltda.	Chile	Holding co.	99.90	62,611	(424)	Ernst & Young	
Iberaguas, Ltda.	Chile	Holding co.	99.80	77,281	2,120	-	
Empresa de Servicios Sanitarios de Los Lagos, S.A.	Chile	Water	50.90	69,268	10,366	PWC	
Energypworks do Brasil, Ltda.	Brazil	Energy	99.99	45,508	5,726	Ernst & Young	
Capuava Energy, Ltda.	Brazil	Energy	99.99	2,240	2,120	Ernst & Young	
Electricidad de Veracruz, S.A. de C.V.	Mexico	Energy	99.99	3,837	58	Ernst & Young	
Electricidad de Veracruz II, S.A. de C.V.	Mexico	Energy	99.99	1	-	Ernst & Young	
Iberdrola Energía La Laguna, S.A. de C.V.	Mexico	Energy	99.99	92,772	23,527	Ernst & Young	
Servicios de Operación Altamira, S.A. de C.V.	Mexico	Services	99.99	(47)	260	Ernst & Young	
Iberdrola Energía del Golfo, S.A. de C.V.	Mexico	Energy	99.99	110,097	5,549	Ernst & Young	
Gestión Empresas Eléctricas, S.A.	Guatemala	Services	99.99	171	4,604	Deloitte	
Iberdrola Energía Tamazunchale, S.A. de C.V.	Mexico	Energy	99.99	96,357	(163)	Ernst & Young	
Servicios de Operación La Laguna, S.A. de C.V.	Mexico	Services	99.99	(47)	260	Ernst & Young	
Parques Ecológicos de México, S.A. de C.V.	Mexico	Energy	99.95	174	-	Ernst & Young	
Iberdrola Servicios de Capacitación, S.A.	Mexico	Energy	99.99	(70)	104	Ernst & Young	

Company	Location	Line of business	% of ownership of Iberdrola Energía, S.A. at 12.31.06	Thousands of euros			Auditor
				Capital, reserves and translation differences at 12.31.06 (a)	Profit (loss) for the year (a)		
ASSOCIATED COMPANIES							
Neoenergia, S.A. (a)	Brazil	Holding co. - Energy	39.00	1,844,970	364,030	Deloitte	
Companhia de Electricidade do Estado do Bahia, S.A. (a)	Brazil	Energy	42.76	257,641	197,754	Deloitte	
Companhia Energetica do Rio Grande do Norte, S.A. (a)	Brazil	Energy	39.95	115,487	51,710	Deloitte	
Companhia de Electricidade do Pernambuco, S.A. (a)	Brazil	Energy	34.96	310,600	79,678	Deloitte	
Termopernambuco, S.A. (a)	Brazil	Energy	39.00	107,189	36,702	Deloitte	
Termoaçú, S.A. (a)	Brazil	Energy	14.65	183,649	-	PWC	
NC Energia Subgroup (a)	Brazil	Services	39.00	362	5,436	-	
Itapetí Geração de Energia, S.A. (a)	Brazil	Energy	38.98	54,586	24,529	Deloitte	
Distribuidora Eléctrica Centroamericana II, S.A.	Guatemala	Energy	49.00	209,350	40,706	Ernst & Young	
Empresa Eléctrica de Guatemala, S.A.	Guatemala	Energy	39.63	102,141	38,899	Ernst & Young	
Comercializadora Eléctrica de Guatemala, S.A.	Guatemala	Energy	39.63	13,017	2,702	Ernst & Young	
Crediegsa, S.A.	Guatemala	Energy	39.63	1,224	211	Ernst & Young	
Enérgica, S.A.	Guatemala	Energy	39.63	3,702	972	Ernst & Young	
Grupo Navega.com	Guatemala	Telecommunications	26.95	10,131	3,021	PWC	
Transportista Eléctrica Centroamericana, S.A.	Guatemala	Energy	39.63	24,721	9,443	Ernst & Young	
Garter Properties, Inc.	Brazil	Finance	42.76	188	(151)	Deloitte	
Gas Natural México, S.A. de C.V.	Mexico	Energy	13.25	274,346	13,113	PWC	
Sistemas de Administración y Servicios, S.A. de C.V.	Mexico	Energy	13.00	267	7	PWC	
Almacenaje y Manejo de Materiales Eléctricos, S.A.	Guatemala	Services	48.97	828	294	Ernst & Young	
Inversiones Eléctricas Centroamericanas, S.A.	Guatemala	Holding co.	39.63	42,824	14,012	Ernst & Young	
Afluente Geração e Transmissão de Energia Eléctrica, S.A. (a)	Brazil	Energy	42.76	21,804	12,184	Deloitte	
Geracao CIII, S.A.	Brazil	Energy	39.04	-	-	-	
Baghari, U.H.E.	Brazil	Energy	39.00	3,529	-	Deloitte	
Goias, S.U.L.	Brazil	Energy	39.00	1,785	-	Deloitte	
Inmobiliaria y Desarrolladora Empresarial de América, S.A.	Guatemala	Real Estate	39.63	1,557	217	Ernst & Young	

(a) For companies whose financial statements are denominated in foreign currency, capital and reserves are shown at the historical exchange rate and income and loss at the average exchange rate for the year. Translation difference, therefore, show the difference between the amount calculated by applying these exchange rates and that by applying the exchange rate prevailing at 31 December 2006.

**ADDITIONAL INFORMATION RELATED TO SUBSIDIARIES AND ASSOCIATED COMPANIES OF THE IBERDROLA
ENERGÍAS RENOVABLES SUBGROUP IN 2006**

Company	Location	Line of business	Thousands of euros			Auditor
			% of ownership of Iberdrola Energías Renovables at 12.31.06	Capital and reserves at 12.31.06	Profit (loss) for the year	
Iberdrola Energía Renovables, S.A.U.	Madrid	Energy	100.00	356,266	110,953	Ernst & Young
Ibernova Promociones, S.A.U.	Madrid	Energy	100.00	34,212	25,826	Ernst & Young
Ciener, S.A.U.	Vizcaya	Energy	100.00	16,850	5,198	Ernst & Young
Iberdrola Energías Renovables de Castilla - La Mancha, S.A.U.	Toledo	Energy	100.00	79,976	68,215	Ernst & Young
Iberdrola Energías Renovables de Galicia, S.A.U.	Orense	Energy	100.00	53,335	54,854	Ernst & Young
Energía I Vent, S.A.	Barcelona	Energy	90.00	1,834	(8)	-
Biovent Energía, S.A.	Valladolid	Energy	85.00	24,595	20,279	Ernst & Young
Minicentrales del Tajo, S.A.	Madrid	Energy	66.58	887	543	-
Eólicas de la Rioja, S.A.	La Rioja	Energy	63.55	4,306	7,062	Ernst & Young
Iberdrola Energías Renovables de Andalucía, S.A.U.	Sevilla	Energy	100.00	130	(703)	Ernst & Young
Iberdrola Energías Renovables de Aragón, S.A.U.	Zaragoza	Energy	100.00	30,496	24,099	Ernst & Young
Iberdrola Energías Renovables de La Rioja, S.A.U.	La Rioja	Energy	63.55	81,366	23,331	Ernst & Young
Sociedad Gestora de Parques Eólicos Campo de Gibraltar, S.A.	Málaga	Energy	55.00	71	(10)	Ernst & Young

SUBSIDIARIES

ANEXO I

		Thousands of euros			
Company	Location	Line of business	% of ownership of Iberdrola		Auditor
			Renovables at 12.31.06	Capital and reserves at 12.31.06	
				Profit (loss) for the year	
Biovent Holding, S.A.	Valladolid	Energy	85.00	31,970	Ernst & Young
Sistemas Energéticos Chandrexa, S.A.U.	Orense	Energy	96.07	1,955	Ernst & Young
Sistemas Energéticos Mas Garullo, S.A.	Zaragoza	Energy	51.00	2,250	Ernst & Young
Sistemas Energéticos La Muela, S.A.	Zaragoza	Energy	50.00	4,804	Ernst & Young
Sistemas Energéticos del Moncayo, S.A.	Soria	Energy	75.00	3,987	Ernst & Young
Sociedad Gestora de Parques Eólicos de Andalucía, S.A.	Málaga	Energy	55.00	2,087	Ernst & Young
Iberdrola Energ. Rinnovabili, S.P.A.	Italy	Energy	100.00	186	Ernst & Young
	United Kingdom				
Iberdrola Renewable Energies of UK Limited	Kingdom	Energy	100.00	(498)	Ernst & Young
Aeolia Producao de Energia, S.A.	Portugal	Energy	78.00	518	Ernst & Young
Iberdrola Energ. Renouveables, S.A.S.	France	Energy	100.00	(1,530)	Ernst & Young
Iberdrola Regenerat Energien, GMBH	Germany	Energy	100.00	30,539	Ernst & Young
Energias Renováveis do Brasil, Ltda.	Brazil	Energy	100.00	31,788	Ernst & Young
Iberdrola Energ. Renovaveis, S.A.	Portugal	Energy	100.00	729	Ernst & Young
Iberdrola Energia Odnawialna Spo3ka z ograniczon Odpowiedzialnocecil	Poland	Energy	100.00	(1,212)	Ernst & Young
C. Rokas, S.A. (*)	Greece	Energy	49.90	81,153	Ernst & Young
Aerocastilla, S.A.	Valladolid	Energy	51.00	1,358	Ernst & Young
Generación de Energia Eólica, S.A.	Valladolid	Energy	51.00	94	Ernst & Young
Vientos de Castilla y León, S.A.	Valladolid	Energy	51.00	55	Ernst & Young
Eólicas Fuente Isabel, S.A.	Valladolid	Energy	51.00	55	Ernst & Young

(*) Listed on the Athens (Greece) stock exchange.

Company	Location	Line of business	Thousands of euros				Auditor
			% of ownership of Iberdrola		Capital and reserves at 12.31.06	Profit (loss) for the year	
			Renovables at 12.31.06	Energy			
Productora de Energía Eólica, S.A.	Valladolid	Energy	50.92	1,867	(9)	Ernst & Young	
Energías de Castilla y León, S.A.	Valladolid	Energy	76.50	1,894	225	Ernst & Young	
Energía Global Castellana, S.A.	Valladolid	Energy	51.00	55	(273)	-	
Villadefrades Eólica, S.L.	Valladolid	Energy	68.00	1,783	(10)	-	
Eme Dólar Uno, S.L.	Seville	Energy	100.00	(2)	(25)	Ernst & Young	
Eme Dólar Tres, S.L.	Seville	Energy	100.00	(1)	(42)	Ernst & Young	
Eme Hueneja Tres, S.L.	Seville	Energy	100.00	(2)	(34)	Ernst & Young	
Eme Ferreira Dos, S.L.	Seville	Energy	100.00	(2)	(27)	Ernst & Young	
Peache Energías Renovables, S.A.	Burgos	Energy	51.00	61	(10)	-	
Sistemas Energéticos Torralba, S.A.	Zaragoza	Energy	60.00	3,728	4,543	Ernst & Young	
Global Solar Energy, S.A.	Murcia	Energy	90.00	1,500	(9)	-	
Producciones Energéticas de Castilla y León, S.A.	Valladolid	Energy	76.50	13,400	(11)	-	
Ecobarcial, S.A.	Zamora	Energy	39.02	25,610	(274)	Ernst & Young	
Ferne Eolien de Buchfeldm, SARL	France	Energy	100.00	38	(29)	Ernst & Young	
Windfarm Wirfus, GMBH	Germany	Energy	100.00	(16)	199	-	
EBV Windpark 23, GMBH	Germany	Energy	100.00	(291)	515	-	
Rastenber, GMBH	Germany	Energy	100.00	236	111	-	
Energía Wiatrowa Karscino S.P. ZOO EWK	Poland	Energy	100.00	(10)	27	-	
Iberdrola Renewable Energies Usa Limited	US	Energy	100.00	81,011	(4,304)	Ernst & Young	
Community Energy INC	US	Energy	100.00	40,832	(4,901)	Ernst & Young	
Electra Sierra de San Pedro, S.A.	Cáceres	Energy	80.00	500	(11)	-	
Sistema Energéticos Los Campillos, S.A.U.	Valladolid	Energy	100.00	60	535	Ernst & Young	
Ousauhning Raisner, A.S.	Estonia	Energy	80.00	1,279	(231)	-	
Iberdrola Energía Marinas de Cantabria, S.A.	Cantabria	Energy	60.00	2,600	(29)	-	
Parque Eólico Cruz del Carretero, S.L.	Valladolid	Energy	54.40	703	(3)	-	
Parque Eólico Los Collados, S.L.	Valladolid	Energy	68.00	244	(8)	-	
Parque Eólico Fuente Salada, S.L.	Valladolid	Energy	68.00	518	(3)	-	
Motton Wind Farm, L.L.C.	EE.UU	Energy	100.00	-	-	-	

Company	Location	Line of business	Thousands of euros			Auditor
			% of ownership of Iberdrola Energías Renovables at 12.31.06	Capital and reserves at 12.31.06	Profit (loss) for the year	
Energiaki Alogorachis, S.A.	Greece	Energy	100.00	3,984	(225)	Others
Higher Darracott Moor Wind Faem Limited	UK	Energy	100.00	(23)	(34)	-
Perfect Wind, SAS Group	France	Energy	100.00	2,927	(1,225)	Others
Iberd. Regen. Energien Verwaltung, GmbH	Germany	Energy	100.00	25	(2)	-
Windpark Julicher Land	Germany	Energy	100.00	25	3	-
EC Energoconsult Mernökszoigalati, I.E.K.	Hungary	Energy	100.00	32	(83)	-
Somozas Energías y Recursos Medioambientales (SOERMASA), S.A.	La Coruña	Energy	100.00	-	1	-
<u>ASSOCIATED COMPANIES</u>						
Eólicas de Euskadi, S.A.	Vizcaya	Energy	50.00	27,695	11,199	Attest
Desarrollo de Energías Renovables de La Rioja, S.A.	La Rioja	Energy	40.51	16,387	4,153	Ernst & Young
Energías Renovables de la Región de Murcia, S.A.	Murcia	Energy	50.00	51,766	2,983	Ernst & Young
Molinos del Cidacos, S.A.	La Rioja	Energy	31.75	17,065	8,445	Ernst & Young
Sotavento Galicia, S.A.	Orense	Energy	8.00	1,346	445	Ernst & Young
Molinos de La Rioja, S.A.	La Rioja	Energy	42.37	5,174	1,220	Ernst & Young
Eólicas de Campollano, S.A.	Madrid	Energy	25.00	10,598	8,920	KPMG
Salto de Belmontejo, S.A.	Cuenca	Energy	24.84	487	(12)	Ernst & Young
Energías Eólicas de Cuenca, S.A.	Cuenca	Energy	62.50	7,545	(42)	Ernst & Young
Electra de Malvana, S.A.	Cáceres	Energy	48.00	500	(11)	-
Electra de Montachez, S.A.	Cáceres	Energy	40.00	500	(30)	-
Sistema Eléctrico de Conexión Huenéja, S.L.	Granada	Energy	41.80	573	(170)	-
Eléctra de Layna, S.A.	Valladolid	Energy	42.50	4,241	43	-

**ADDITIONAL INFORMATION RELATED TO SUBSIDIARIES AND ASSOCIATED COMPANIES OF THE IBERDROLA
INGENIERÍA Y CONSULTORÍA SUBGROUP IN 2006**

Company	Location	Line of business	Thousands of euros			Auditor
			% of ownership of Iberinco at 12.31.06	Capital and reserves at 12.31.06	Profit (loss) for the year	
<u>SUBSIDIARIES</u>						
Iberdrola Ingeniería y Construcción, S.A.U.	Vizcaya	Services	100.00	106,805	29,281	Ernst & Young
Iberdrola Ingeniería y Consultoría Servicios, S.A.U.	Madrid	Services	100.00	148	97	Ernst & Young
Iberdrola Consultoría e Serviços do Brasil, Ltda.	Brazil	Services	100.00	868	(52)	Ernst & Young
Iberdrola Ingeniería y Consultoría México, S.A. de C.V. Group	Mexico	Services	99.99	5,829	3,104	Ernst & Young
Enermón S.A. de CV	Mexico	Engineering	99.99	5	157	Ernst & Young
Sublin 2 S.A.	Mexico	Engineering	100.00	48	(11)	Ernst & Young
Iberdrola Engineering and Construction Poland, sp	Polonia	Engineering	100.00	18	171	-
Iberdrola Ingeniería y Construcción Venezuela, S.A.	Venezuela	Engineering	98.81	1	2	-
Iberinco Hellas Techniki kai Kataskevastiki EPE	Grecia	Engineering	100.00	18	3	-
Iberdrola Engineering and Construction Germany GMBH	Alemania	Engineering	100.00	24	-	-
Iberdrola Engineering and Const UK,	UK	Engineering	100.00	50	-	-
Iberdrola Inzhimiring I Stroiteistvo LLC	Russia	Engineering	100.00	-	5	-
<u>ASSOCIATED COMPANIES</u>						
Ghesa Ingeniería y Tecnología, S.A. (*)	Madrid	Services	41.18	19,907	2,451	Ernst & Young
Keytech Sistemas Integrales, S.A.	Madrid	Services	37.00	583	-	Ernst & Young
Empresarios Agrupados Internacional, S.A.	Madrid	Services	25.46	3,393	211	Ernst & Young
Empresarios Agrupados, A.I.E.	Madrid	Services	25.46	750	-	Ernst & Young

(*) Group parent company. Data for capital, reserves and income (loss) for 2006 are consolidated.

**ADDITIONAL INFORMATION RELATED TO SUBSIDIARIES AND ASSOCIATED COMPANIES OF THE IBERDROLA -
ANSELMO LEON SUBGROUP IN 2006**

Company	Location	Line of business	Thousands of euros			Auditor
			% of ownership of Anselmo León at 12.31.06	Capital and reserves at 12.31.06	Profit (loss) for the year	
<u>SUBSIDIARIES</u>						
Anselmo León, S.A.	Valladolid	Holding	100.00	1,885	1,819	-
Anselmo León Distribución Eléctrica, S.L.	Valladolid	Energy	100.00	5,453	2,257	Ernst & Young
Anselmo León Hidráulica, S.L.	Valladolid	Energy	100.00	1,503	499	-
<u>ASSOCIATED COMPANIES</u>						
Electrodistribuidora Castellano Leonesa, S.A.	Valladolid	Energy	20.00	273	11	-

**ONAL INFORMATION RELATED TO SUBSIDIARIES AND ASSOCIATED COMPANIES OF THE IBERDROLA -
IBERDROLA INMOBILIARIA SUBGROUP IN 2006**

Company	Location	Line of business	Thousands of euros		Auditor	
			% of ownership of Iberdrola Inmobiliaria at 12.31.06	Capital and reserves at 12.31.06 Profit (loss) for the year		
<u>SUBSIDIARIES</u>						
Iberdrola Inmobiliaria, S.A.U.	Madrid	Real Estate	100.00	574,790	111,581	PWC
Fiuna, S.A.	Madrid	Real Estate	70.00	10,958	(34)	PWC
Promotora La Castellana de Burgos, S.A.	Madrid	Real Estate	100.00	13,471	(263)	PWC
Promociones Inmobiliarias Renfapex 2000, S.A.	Madrid	Real Estate	51.00	3,021	319	KPMG
Klimt XXI 22.000, S.L.	Madrid	Real Estate	60.00	1,414	(10)	Deloitte
New Klimt Tercario 2001, S.L.	Madrid	Real Estate	100.00	1,420	807	PWC
Villaverde Promotora Cántabro Leonesa, S.L.	Madrid	Real Estate	50.00	3,685	680	PWC
Gedapex, S.A.	Madrid	Real Estate	50.00	9,820	(273)	Deloitte
Oceanic Center, S.L.	Valencia	Real Estate	50.00	40,661	673	PWC
Norapex, S.A.	Madrid	Real Estate	50.00	2,172	(404)	PWC
Las Pedrazas Golf, S.L.	Madrid	Real Estate	50.00	31,941	(47)	Deloitte
Urbanizadora Marina de COPE, S.L.	Madrid	Real Estate	60.00	94,601	(166)	PWC
Iberdrola Inmobiliaria Catalunya, S.A.U. Subgroup	Barcelona	Real Estate	100.00	77,393	(4,673)	PWC
Iberd.-Ros, S.L.	Valencia	Real Estate	50.00	200	-	-
<u>ASSOCIATED COMPANIES</u>						
Nova Caia Villajoyosa, S.A	Madrid	Real Estate	25.00	1,218	(12)	-
Camarote Golf, S.A.	Madrid	Real Estate	26.00	17,953	(30)	Deloitte

**ONAL INFORMATION RELATED TO SUBSIDIARIES AND ASSOCIATED COMPANIES OF THE IBERDROLA -
IBERDROLA PORTUGAL-ELECTRICIDAD E GAS SUBGROUP IN 2006**

Company	Location	Line of business	% of ownership of Portugal at 12.31.06	Thousands of euros		Auditor
				Capital and reserves at 12.31.06	Profit (loss) for the year	
<u>SUBSIDIARIES</u>						
Iberdrola Portugal Electricidad e Gas, S.A.	Lisbon	Energy	100.00	872,481	18,859	Ernst & Young
Iberdrola Participações SGPS, S.A.	Lisbon	Holding	100.00	1,344,276	20,670	Ernst & Young

**ADDITIONAL INFORMATION RELATED TO SUBSIDIARIES AND ASSOCIATED COMPANIES OF THE IBERDROLA –
AMARA SUBGROUP IN 2006**

Company	Location	Line of business	% of ownership of Amara at 12.31.06	Thousands of euros		Auditor
				Capital and reserves at 12.31.06	Profit (loss) for the year	
<u>SUBSIDIARIES</u>						
Amara, S.A.U.	Madrid	Supply	100.00	19,900	4,583	PWC
Amara Brasil Ltda.	Salvador de Bahia	Supply	99.99	1,175	290	PWC
Amergy S.A. de CV	Monterrey	Supply	100.00	546	136	PWC
Amergy Servicios SA de CV	Monterrey	Services	100.00	9	4	PWC
Ergytech Inc	Houston	Purchasing agent	100.00	130	36	PWC
Amara Portugal S.A.	Lisbon	Supply	80.00	480	(52)	PWC

ASSOCIATED COMPANIES

Lanmara Ltda.	Salvador de Bahia	Supply	30.00	(3,115)	-	PWC
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MANAGEMENT REPORT FOR 2006

1 BUSINESS EVOLUTION

IBERDROLA, S.A., individually considered, is a holding company only engaged in the retailing of electricity and gas to eligible customers which results come from this activity and from the individuals received from its subsidiaries. Therefore, the following information is basically referred to IBERDROLA Group.

2 SIGNIFICANT FACTS FROM FISCAL YEAR 2006

2.1 Key performance indicators

In 2006, IBERDROLA reached a new record in the Group's production, which grew 10.8% to 91,991 GWh, driven by more environmentally-efficient technologies. Furthermore, this increased growth in production was achieved while reducing CO₂ emissions by 7.5%. In Spain, emissions decreased by 12.4%, with emission-free production of 65.8% out of a total of 68,348 GWh produced.

- A 49.2% increase in hydroelectric production, with 80% availability in Spain, while wind production grew 13.2%, to 7,329 GWh (705 GWh international).
- Nuclear power stations have provided high availability, even taking into account the recharging periods, corresponding to an 8.7% increase in production over 2005.
- Combined-cycle production increased by 15.8%, while production through more contaminating sources of energy was reduced, -26.7% for coal and -42.4% for fuel-oil.

2.2 Financial resources

As result of the active refinancing policy pursued by IBERDROLA, the average age of its debt continues to be around 5 years. Especially significant is the reduction in financial costs that the Company has achieved throughout the fiscal year, 4.41% as of December 2006, which is 14 basis points lower than December 2005, despite rising interest rates.

In this sense, it should be noted that on 15 December 2006, Iberdrola, together with Unión Fenosa and Hidrocarbónico, assigned the right recognized in RD 809/2006, of June 30, corresponding to the revenue deficit from payments for regulated activities from the year 2005. The amount of the right, which was assigned to a group of international banks, was EUR 2,055 million, EUR 1,334 million of which corresponded to Iberdrola.

2.3 Regulation in Spain

As to Regulation, the most noteworthy aspects of the regulatory framework in which the company operated during 2006 were:

- 2006 Rate: increased 4.48% on average over 2005. In July, a Royal Decree was published which revised the 2006 rates, producing an increase of 1.38% beginning on July 1.
- Rate shortfall: there was a new rate shortfall in 2006, with a recovery against the rate for future years being recognized by the Government.
- Bilateralization: Royal Decree-Law 3/2006, of February 24, provided that energy acquired and sold on the wholesale market by companies within the same business group must be included in physical bilateral contracts. For purposes of recognizing the costs for purchasing energy from distribution companies, the energy subject to inclusion would be provisionally recognized at a price set at 42.35 euros/MWh, much below existing market prices during such times.
- Mibel: Orden ITC/2129/2006, of June 30, provided that distributors must acquire 5% of their energy requirements on the futures market, managed on the Portuguese side by MIBEL, during the second half of 2006. With Order ITC/3990/2006, of December 28, this percentage has increased to 10% for requirements as from the first half of 2007.

Looking to 2007, various regulatory developments have occurred that entail an advance towards the complete liberalization of the industry:

- The principle of rate sufficiency is recognized through the “ex-ante” acknowledgment of the shortfall, with additive rate methodology.
- Quarterly revisions are expected beginning on July 1.
- All references to the CTCs and the results thereof on rates disappear.
- An increase in compensation for distribution, with a special injection of funds into the activity equal to EUR 500 million, of which 31.75% corresponds to IBERDROLA.
- The generation price reference that is used is consistent with market values.
- The use of the real price of energy, together with a reduction in the access rates that caused shortfall (recognized ex-ante), will strengthen retailing.

2.4 Main activities to carry out the Strategic Plan in 2006

In 2006, IBERDROLA placed into operation 2,593 MW of additional capacity over the capacity existing in December 2005, reaching 30,384 MW of total installed capacity. The additions mainly correspond to:

- Combined cycles, with the start-up of Altamira V in México (1,121 MW) and Escombreras (800 MW) in Spain.
- Renewable Energy, with the addition of 624 MW during the fiscal year.

Thus, as of December 2006, IBERDROLA reached the installed capacity targets set at the commencement of the 2001-2006 Strategic Plan, after increasing installed capacity by 83% over the capacity it had at the beginning thereof (approximately 16,600 MW). Equilibrium has also been achieved in the mix that was sought: The new combined cycles already have a production similar to hydroelectric facilities, and renewable energy has increased its weight by 12% to reach 15% of the total. Furthermore, the weight of more contaminating technologies has been reduced.

2.4.1 Combined Cycle Power Stations (Spain)

At the end of 2006, Iberdrola's total capacity at combined cycle power stations in Spain was 4,800 MW (5,600 MW under management), corresponding to 9 power stations. Thus, Iberdrola surpassed by 800 MW the initial target of the 2001-2006 Strategic Plan, having 4,000 MW of combined cycles installed in our country at the end thereof.

In 2006, the Company placed into service the Escombreras combined cycle plant (800 MW), in Cartagena (Murcia), the ninth plant that it has built in Spain since the entry into effect of the 2001-2006 Strategic Plan. This past August 11, the plant achieved base charge, commencing commercial operation thereof on November 20, and contributing to results as from the fourth quarter of the fiscal year.

2.4.2 Hydroelectric and Mini-Hydroelectric Energy

An additional 624 MW (607 hydroelectric and 17 mini-hydroelectric) were installed in 2006. Of this total, 420 MW correspond to Spain and 204 MW to other countries. With this contribution, as of the close of 2006, IBERDROLA had an installed capacity of 4,434 MW (4,102 MW hydroelectric and 332 MW mini-hydroelectric), 16.4% above the capacity existing at the close of 2005, and 434 MW (11%) above the target set in the 2001-2006 Strategic Plan, which confirms the Company's position as a world leader in this business.

The renewable energy facilities of IBERDROLA are present in thirteen Spanish autonomous communities and seven foreign countries (the United States, Poland, Brazil, France, Portugal, Germany and Greece).

2.4.3 Latin America

Total production in Latin America reached 23,643 GWh, 4,216 GWh more than in 2005 (+21.7%), of which 20,327 GWh correspond to Mexico and 3,316 to South America.

In Mexico, IBERDROLA has confirmed its position as the leading private producer of electricity. The Company already has more than 3,815 MW of installed capacity in this country. The 1,121 MW Altamira V combined cycle plant entered into operation during the fourth quarter of 2006, and the testing period commenced for the Tamazunchale power station in the Mexican state of San Luis Potosí, the largest combined cycle power station to be placed in operation in Mexico, with an installed capacity of 1,135 MW.

In Brazil, during 2006, Neoenergía (39%-owned by Iberdrola) was awarded the concessions to build, maintain and operate the Baguari hydroelectric power station and the Nova Aurora and Goiandira mini-hydroelectric power stations, which total 188 MW of installed capacity.

As regards wind energy, in 2006, IBERDROLA finished the installation and start-up of the 49.30 MW Rio do Fogo wind farm in Brazil, and has begun developments in the State of Oaxaca in Mexico, which total up to 150 MW of capacity.

2.4.4 Europe

In Greece, IBERDROLA is a strategic partner of Rokas, the main promoter and operator of wind farms, in which it has a 49.9% interest, and has 210 MW of wind energy in operation. During the third quarter of the year, IBERDROLA acquired from Motor Oil Hellas 70% of Korinthos Power, a Greek company with a license to participate in the auctions for new combined cycle capacity begun by the Government of such country.

In Portugal, Iberdrola has 18 MW of wind energy in operation, corresponding to the Catefica wind farm. In addition, it has already installed the first 14 MW of the Alto Monção wind farm. IBERDROLA also has 140 MW of advanced projects. Furthermore, IBERDROLA has received the approval of the Direcção Geral de Energia lusa to build the first gas combined cycle plant in Portugal, in the municipality of Figueira da Foz, located between Lisbon and Oporto (850 MW).

In Latvia, IBERDROLA was awarded the construction, as well as the supervision of the operation and maintenance for 12 years, of a combined cycle plant with 420 MW of installed capacity in Riga (Latvia).

IBERDROLA has several projects in other countries within the E.U., such as Germany, Poland, France, Italy and the United Kingdom, mainly in the area of wind energy.

2.4.5 United States

IBERDROLA, which has wagered on internationalization as one of its pillars of growth, considers the U.S. wind farm market to be key. In fact, it has become one of the most important markets for the development of IBERDROLA's objectives in the area of renewable energy.

In 2006, IBERDROLA acquired 100% of Community Energy (CEI) for 30 million dollars, and 100% of the companies MREC Partners and its subsidiary Midwest Renewable Energy Projects, for more than 30 million euros.

In all, IBERDROLA has 26 MW in operation and a portfolio of projects of more than 5,000 MW, which it plans to continue to grow, and already has a permanent office in the State of Pennsylvania.

2.4.6 Distribution

At the close of 2006, IBERDROLA had 9.9 million users in Spain, and the average total energy distributed on the network reached 99,520 GWh, an increase of 3.3% over the prior fiscal year. 82.2% of the energy was distributed to the Regulated market.

Regarding supply quality, the ICEIT due to incidents in IBERDROLA's Distribution network was 1.96 hours during 2006. This value signifies an availability of 99.98%. Iberdrola is thus in a leadership position in service quality, meeting the commitment made in its 2001-2006 Strategic Plan.

In Latin America, as of the end of 2006, IBERDROLA surpassed 8.5 million managed users in the region, and distributed energy reached 27,662 GWh, an increase of 4.0% over the prior fiscal year.

2.4.7 Gas Supply

IBERDROLA became the second-largest supplier of gas in Spain during 2006, supplying 15% of all gas consumed in the deregulated market. Furthermore, IBERDROLA ended this period with a global supply portfolio of more than 16 bcm annually, of which 7 bcma cover its supply needs in Spain and almost 9 bcma do so in Mexico and Brazil.

In 2006, the Company received a total of 101 shipments of liquefied natural gas (LNG) in LNG tankers, which unload at all regasification plants currently operating in Spain: Bilbao, Huelva and Sagunto.

2.5 Compliance with the 2001-2006 Strategic Plan and launch of the 2007-2009 Strategic Plan

IBERDROLA has achieved several of the targets set forth in the Plan ahead of schedule, with growth based on the basic business:

- It has doubled its size, increasing its installed capacity by 83%, to 30,384 MW, and its production by 80%, to 91,991 GWh, as compared to December 2000.
- It has also doubled its income, reaching Net Income of EUR 1,660.3 million, as compared to its target of EUR 1,600 million.
- After successfully completing the 2001-2006 Strategic Plan, IBERDROLA is looking to a future of organic growth through the 2007-2009 Strategic Plan, and non-organic growth through the merger agreement reached with ScottishPower on 27 November 2006, when the Board of Directors of IBERDROLA and ScottishPower reached an agreement regarding the terms of an offer by IBERDROLA for all of the capital stock of Scottish Power.

3 PRINCIPAL RISKS ASSOCIATED WITH THE BUSINESS ACTIVITIES OF THE IBERDROLA GROUP

3.1 Financial risk management policy

Under the General Risk Policy, which was approved in November 2004 by the Board of Directors of IBERDROLA, the Group undertakes to use its capabilities to the full in order to ensure that all the significant risks of all kinds are adequately identified, measured, managed and controlled, applying the following “basic action guidelines”:

- Incorporation of the risk-opportunity approach into the Group’s management.
- Separation, at operating level, of functions between the risk-taking areas and the areas responsible for analysing, controlling and supervising the risks.
- Assurance of short- and long-term business and financial stability, maintaining an appropriate balance between risk, value and benefit.
- Correct use of financial risk hedging instruments and their recognition in accordance with the applicable accounting and financial standards.
- Transparency in reporting on the Group’s risks and the functioning of the systems developed to control them.

- Development of a risk-opportunity control and management culture within the IBERDROLA Group.
- Bring into line with general policy all the specific risk-related policies that have to be implemented.
- Compliance with current regulations and legislation in relation to risk control, management and oversight.
- Continuous improvement on the basis of international best practices in Transparency and Good Corporate Governance in relation to risk control, management and oversight.

In order to implement this policy and respect these principles, IBERDROLA has developed an Integral Risk Control and Management System based on a suitable definition, separation and assignment of functions and responsibilities, and of the required procedures, methodologies and support tools.

The System, which in November 2005 received quality certification from AENOR under the ISO 9001:2000 standard, is based on three fundamental cornerstones:

- A risk policy and limit structure, developed in 2005, that guarantees that risks are managed by the businesses in a controlled fashion.
- Monitoring and control of the risks in the income statement.
- Analysis and control of risks associated with new investments.

In this context, IBERDROLA has certain risk policies and limits approved by the Operating Committee that cover, among others, the following risks:

3.2 Financial Risks

3.2.1 Interest rate risk

Several items in the balance sheet and the associated financial derivatives bear interest at fixed rates and, therefore, are exposed to fair value interest rate risk as a result of changes in market interest rates. Also, the IBERDROLA Group is exposed to cash flow interest rate risk in respect of items in the balance sheet and derivatives that bear interest at floating rates.

IBERDROLA mitigates this risk by managing the proportion of its debt that bears fixed interest to that which bears floating interest on the basis of the situation of the markets, through new sources of financing and the use of interest rate derivatives, all within the approved risk limits.

3.2.2 Foreign currency risk

Fluctuations in the value of the currencies in which borrowings are instrumented and purchases and sales are made with respect to the presentation currency may have an adverse effect on the finance costs and profit for the year.

The following items could be affected by foreign currency risk:

- Debt denominated in currencies other than the local or functional currency arranged by the IBERDROLA Group companies.
- Collections and payments for supplies, services or investments in currencies other than the functional currency.
- Income and expenses of certain foreign subsidiaries indexed to currencies other than the functional currency.
- Taxes derived from the accounting for tax purposes in local currencies other than the functional currency.
- Profit or loss on consolidation of the foreign subsidiaries.
- Consolidated carrying amount of investments in foreign subsidiaries.

IBERDROLA reduces this risk by ensuring that all its economic flows are denominated in the presentation currency of each Group company, provided that this is possible and economically practicable. The resulting open positions are integrated and managed through the use of derivatives, within the approved limits.

3.2.3 Liquidity risk

Exposure to adverse situations in the debt or capital markets can hinder or prevent the IBERDROLA Group from obtaining the financing required to properly carry on its business activities and implement its Strategic Plan.

IBERDROLA's liquidity policy ensures that it can meet its payment obligations without having to obtain financing under unfavourable terms. For this purpose, it uses various management measures such as the arrangement of committed credit facilities of sufficient amount and flexibility, diversification of the coverage of financing needs through access to different markets and geographical areas, and diversification of the maturities of the debt issued.

3.2.4 Credit risk

IBERDROLA Group is exposed to the credit risk arising from the default of a counterparty (customer, supplier, shareholder or financial institution) which could have an impact in results. This risk is not very significant, as a consequence of the short customers' average collection period and the effect of risks policies in relation to the time limit on open positions and the creditworthiness of the counter parties.

In particular, in the case of financial creditor positions, IBERDROLA follows a prudent policy of arranging derivatives and placing cash surpluses with highly solvent counterparties based on the credit ratings of Moody's and S&P.

3.3 Other Risks

3.3.1 Business and market risks

The business activities of the IBERDROLA Group are subject to various business risks, such as changes in demand, water availability, wind availability, and other climatological conditions, as well as various market risks, such as the price of fuel used for the generation of electric power, the price of CO2 emission rights, and the wholesale price of electricity.

In the case of the Spanish market, where IBERDROLA carries out its main business activities, the current mix of generation facilities provides significant natural coverage among various production technologies that allows for the mitigation of these risks.

The remaining risk from fluctuations in the products to which fuel is indexed and from exchange rates is mitigated through an appropriate diversification and management of supply contracts that contemplate:

- The indexation of prices, to the extent possible, to indexes that replicate changes in income occurring on the demand side (supply and generation markets).
- The inclusion of clauses to revise and re-open contracts that allow for the adjustment of prices to changes in the market.

Finally, hedging transactions are performed whenever deemed necessary to maintain the risk within established limits.

In the case of the Mexican market, the Group does not have a significant risk of regarding the price of commodities, as the main contracts are prepared in the form of "pass-through" agreements.

Likewise, in the case of electricity trading transactions performed by IBERDROLA in the international markets, there is little risk due to the limited volume of such transactions and to the limits established for open positions, as regards both financial amount and time horizon.

3.3.2 Regulatory risks

The companies of the IBERDROLA Group are subject to a complex framework of laws and regulations regarding rates and other aspects of its activities in Spain and in each of the countries in which they operate. The introduction of new laws / regulations or modifications to existing ones might negatively affect activities, financial position and results of operations.

Due to its importance at the level of the IBERDROLA Group, the rate imbalance or shortfall that occurs when the cost of electricity production estimated in the Rate Decree does not coincide with the actual cost existing during the fiscal year should be highlighted.

Royal Decree 1634/2006, by which the electricity rate is established beginning on 1 January, 2007, has guaranteed the recovery of the income shortfall arising during fiscal year 2006, regardless of future sales, just as occurred with the shortfall for fiscal year 2005. Therefore, the heading "Commercial debtors and other non-current accounts receivable" of the Consolidated Balance Sheet as of 31 December 2006 includes an amount of EUR 579,670 thousand corresponding to the best estimate of the income shortfall corresponding to IBERDROLA, once a deduction has been made for emission rights as described in the notes to the financial statements, and assuming the maintenance of the 35.01%.

The risk policies promote continuous analysis and monitoring of regulatory changes, as well as the making of decisions based on reasonable regulatory hypothesis, at both the domestic and international levels.

3.3.3 Operational risks

During the operation of all of the IBERDROLA Group's activities, there may be direct or indirect losses caused by inadequate internal processes, technological failures, human errors or a result of certain external events.

In particular, in the distribution business, these risks might cause supply cuts and, generally, a deterioration in the levels of required quality of supply, which can lead to claims and administrative penalties, with a corresponding financial and reputational impact.

IBERDROLA mitigates these risks by making the required investments, applying operating and maintenance procedures and programs, supported by quality systems, and planning appropriate personnel training and qualification programs and an appropriate insurance policy.

3.3.4 Environmental risks

The activities of the IBERDROLA Group are subject to risks relating to the extent of broad rules and regulations that require the performance of environmental studies and the procurement of licenses and permits with environmental conditions, as well as risk associated with fees and other market instruments of an environmental nature - such as greenhouse gas emission rights.

In addition, there are other environmental risks inherent in the activities of the Group arising from the management of waste, effluents, emissions and soil at its facilities and that affect biodiversity, and that may give rise to claims for damages, sanction proceedings and damages to its image and reputation.

Due to its future relevancy, the approval at the end of 2006 of Royal Decree 1370/2006, of November 24, should be highlighted, which approved the assignment to the electricity sector of an annual average of 54,053 million free greenhouse gas emission rights, approximately 39% less than the amount assigned for the 2005/2007 period. The allocation detailed for facilities will be known in the coming months. Actual emissions will depend upon electricity demand, climate conditions and the CO₂ and fuel market situation, and the Group's results will be affected by the difference between the amount of free rights that are allocated and actual emissions, taking into account the price of the rights on the market and the provisions of electricity regulation in this regard.

The risk policies contemplate environmental risks in order to mitigate them, fostering the implementation of environmental management systems within the area of the Company's production and distribution facilities, and permanent cooperation with the affected regulatory entities and agents.

3.3.5 Risks relating to new investments

All new investments are subject to various market, credit, business, regulatory, business, operational and other risks, that may compromise the profitability objectives of the project.

Noteworthy risks during the investment execution stage, due to the importance and complexity thereof, are those relating to the construction of new generation facilities, mainly combined cycles and wind farms, which might require the procurement of governmental permits and authorizations, the acquisition of land or signing of lease agreements, the signing of equipment supply, construction services, operation and maintenance, fuel supply and transportation agreements, consumption agreements and financing agreements, all of which may cause delays and lead to increased costs.

The risk policies relating to the new investments contemplate all of these risks and establish specific limits regarding forecasted profitability and the expected profitability at risk, which must be complied with in order for a project to be authorized. Furthermore, there are specific procedures for the approval of significant investments, that require the prior preparation of an investment dossier with a corresponding risk analysis.

3.3.6 Risks associated with international activities

All international activities of the IBERDROLA Group are exposed, to a greater or lesser extent and based on the nature thereof, to the above-mentioned risks (climatological, demand, regulation, fuel and energy prices, environment, etc.) and also to other kinds of risks inherent to the country in which its activities are being carried out.

4 Environment

IBERDROLA maintains a high score in the environmental dimension, according to SAM, the analyst for the Dow Jones Sustainability Index (DJSI). The analysis of environmental dimension for this index includes the following headings: environmental policy and management, environmental results (eco-efficiency), environmental information, advanced environmental management system, advanced environmental results, climate strategy, infrastructure projects, electricity generation, transportation and distribution, and biodiversity.

The Company is in a leading position among companies within its industry in Climate Strategy, according to the rating of the analyst for the Dow Jones Sustainability Index, with a grade of 92 out of 100. Furthermore, it has been selected, for the second year in a row, as “Best in Class” in the industry at the global level for its strategy with respect to Climate Change, forming part of the “Climate Leadership Index.” The strategy, based on significant development of renewable energy and natural gas combined cycle power plants, has given rise to a balanced production structure, which allows the Company to maintain itself among the large European companies with lower CO2 emissions per kWh output.

IBERDROLA has become the leading Spanish electricity multinational that implements a Global Environmental Management System throughout its organizational structure, which system has been certified by the Asociación Española de Normalización y Certificación [Spanish Standardization and Certification Association] (AENOR).

This system, the application of which has been made possible after more than two years of work in all corporate and business areas of the Company, will allow for a reduction of environmental risks, improving the management of resources and optimizing investments and costs.

5 Research and development activities

IBERDROLA’s Innovation Policy is focused on increasingly efficient management of available resources, while at the same time ensuring that the most suitable technologies are introduced at a fast pace. Furthermore, the Company believes that innovation is a key element for sustainable development. Under these premises, and as a part of its commitment to innovation, the 2007-2009 Strategic Plan has identified activities entailing an investment in this concept in the amount of EUR 200 million.

In order to reinforce this strategy, a strong push was given in 2006 to innovation management, by doubling resources and commencing a series of initiatives, the following of which are most noteworthy:

- The introduction of Ibermática's Capital Innovation Model [Modelo Capital Innovación] as a key tool that will allow for the measurement and development of IBERDROLA's capacity for change and adjustment in the face of new circumstances in the market and the environment.
- The development of the R&D&i committees of the various businesses, the principal mission of which is to manage the innovation process from a perspective that is closer thereto.
- The start-up of IBERDROLA's Innovation Network [Red de Innovación], as a forum for the development of intense activity in technological monitoring, the promotion of projects, and the exchange of knowledge.
- The commencement of the certification process for the R&D&i management system according to the UNE 166.000 set of norms.
- The application of the Innovation Reference Framework within a pilot project in which companies such as Siemens, IBM and 3M have participated.
- The identification of 15 areas of knowledge, directed by IBERDROLA's specialized technicians, that form the base of the Company's knowledge management system.

In 2006, IBERDROLA developed 131 R&D&i projects, of which 35 were new initiatives. The total investment in the Company's innovation activities reached 56 million euros, an increase of 4% over 2005.

6 Treasury Shares and capital reduction

The shareholders acting at the General Shareholders Meeting held on 30 March 2006 authorized the Board of Directors, pursuant to Section 75 of the Spanish Corporations Law, to acquire shares of the Company under certain conditions and for a period of 18 months. Pursuant to such authorization, during 2006, IBERDROLA, S.A. has acquired 8,270,501 shares of its own stock for EUR 228 million, with a par value of EUR 25 million. Furthermore, 8,284,425 treasury shares have been disposed of for an amount of EUR 227 million.

The amount resulting from the transfers of the Company's treasury stock during fiscal year 2006 is greater than the cost of acquisition at which the Group had recorded for such treasury stock, at EUR 689 thousand.

Finally, it should be pointed out that as of the close of fiscal year 2006, there were 95,613 shares of treasury stock, and there were derivatives outstanding on 4,725,992 treasury shares.

PROFIT DISTRIBUTION PROPOSAL

YEAR 2006

	<u>Thousands of euros</u>
Distribution basis:	
Retained earnings	1,049,384
2006 Profit	940,964
	<u>1,990,348</u>
 Distribution:	
To dividends	1,097,461
To retained earnings (minimum amount)	892,887
	<u>1,990,348</u>