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annual report
december, 31st 2005

GRUPPO HERA

Annual Report
as at 31 December 2005

Contents

1 - THE HERA GROUP

Preamble

Hera Group Consolidated financial statements are compliant to International Accounting Standards (IFRS) as foreseen for floated Italian companies starting from year 2005.

Full appliance of International Accounting Standards (IFRS), in particular referring to IFRS n. 3, have required to exclude the economic contribution of Meta Group despite the integration have accounting effect starting from January 1st 2005 under Italian Accounting principles.

In order to give faithful and comprehensive representation of 2005 performance, Hera Group has issued a pro-forma Consolidated Financial Report that accounts Meta Group's economic and financial results since January 1st, 2005.

This Document sets out in the following:

1. Pro-forma Consolidated Financial Report of Hera Group (including Meta Group 2005 results).
2. Financial Report of Hera S.p.A.
3. Consolidated Financial Report of Hera S.p.A.

1.01 Letter to the shareholder's

Dear Shareholders,

Not only was 2005 your company's third year of activity, but it was also a year in which your company was involved in a number of important development projects and committed to further strengthening its business model in a changing market characterised by a complex regulatory environment as well as enhanced competition.

The financial statements that we are presenting to you show further impressive growth in all the Group's activities developed in accordance with the objectives outlined in the Industrial Plan.

The main event in 2005, that significantly impacted the year's results, was, as you are probably already aware, the integration with Meta Modena that was completed at the end of the year. The integration of the two organisational structures also got off to a good start in 2006.

Along with this important transaction, other growth oriented activities were completed involving the acquisition of small or medium sized companies active, above all, in the gas sector, in order to strengthen the position of Hera's core business in the reference territory.

The year was particularly intense in terms of investments made, that reached €331 million, designed to strengthen production, particularly for the power grids and environment business.

These activities, along with the expenses connected to the Public Tender Offer on Meta's share capital, did not effect the soundness of Group's financial structure which was reflected in the rating assigned following the Group's first bond issue, successfully completed at the beginning of the current year.

In order to constantly monitor the relationship with clients, the second local customer satisfaction survey was conducted. The survey basically confirmed the levels reached the preceding year with medium-high rankings in terms of the services offered, even though problems involving the Group's new expanded invoicing system occurred in 2005 that inevitably caused a series of initial inconveniences.

Thanks to a close collaboration with the local Environmental Authorities (ATO), with whom agreements for the supply of environmental and integrated water services were signed in six provinces at tariff levels in line with the business plan, it was possible to limit overall tariff increases, as dictated by law, to the average rate of inflation, even in light of the heavy reductions planned by the Energy Authority for gas distribution and electricity.

Two more years of intense activity lie ahead of us and the current Board of Directors (whose term expires at the end of this period) during which we expect to maintain, as has been done in the past, the balance between the Group's development and sustainable social-environmental criteria that guide the company's operations.

I would like to conclude by expressing my gratitude to the Board of Directors, the Board of Statutory Auditors and the employees for the work done in 2005

1.02 Hera's Mission

To gain a market position that maximises the value of the plant, networks and experience in the core business sectors of the companies that have taken part in the integration; increase the value of the Group and its competitive capacity, to take advantage of the opportunities presented with the progressive liberalisation of the markets

To fulfil the "Hera system", creating synergies, optimising the available resources to achieve a better price/quality ratio and ensuring further margins of growth and development

To combine the capacity to respond positively to market expectations with the objective of always providing adequate responses to the needs of the consumers/customers, guaranteeing quality, continuity and safety of the services, respecting the environment and maintaining constant relations with the territory

To develop the core business activities in adjacent territories to those currently served, which present the possibilities for the attainment of economies of scale and synergies in the short-medium term.

1.03 Summary Results

Economic figures					
€/m	2002	2003	2004*	2005*§	Cagr %
Revenues	1,067.0	1,221.5	1,492.6	2,100.5	25.3%
EBITDA	191.9	242.5	292.5	386.4	26.6%
Operating profit	77.6	112.8	177.3	215.7	40.6%
Pre-tax profit	75.3	88.6	147.5	189.3	36.0%
Taxes	38.7	35.6	61.1	80.5	27.7%
Net profit	36.6	53.0	86.5	108.8	43.8%
Minority interest	3.4	3.5	5.5	7.4	29.6%
Hera net profit	33.2	49.5	81.0	101.4	45.1%

Indices					
	2002	2003	2004*	2005*§	Cagr %
Earnings per share	0.042	0.062	0.096	0.100	33.5%
Dividend per share	0.035	0.053	0.060	0.070	26.0%
D/E	29.3%	49.7%	52.8%	65.4%	
ROI	6.9%	8.4%	10.9%	8.8%	
ROE	4.2%	5.9%	7.6%	6.8%	

* IAS adjusted
§ Pro-forma

Operating figures	
Volumes	2005§
Gas sold (m^3/m)	2,786.0
Water invoiced (m^3/m)	228.4
Electricity sold (GWh)	3,754.8
Waste collected (thous. of tonnes)	1,559.8
Waste treated (thous. tonnes)	3,549.0
Customers	
Gas (units)	939.6
Electricity (units)	177.5
Water (units)	914.0

1.04 Company Officers

Board of Directors

Office	Name
Chairman	Tomaso Tommasi di Vignano
Vice Chairman	Giorgio Razzoli
Managing Director	Maurizio Chiarini
Director	Mara Bernardini
Director	Filippo Brandolini
Director	Luigi Castagna
Director	Pier Luigi Celli
Director	Piero Collina
Director	Piergiuseppe Dolcini
Director	Giuseppe Fiorani
Director	Vander Maranini
Director	Nicodemo Montanari
Director	Fabio Alberto Roversi Monaco
Director	Roberto Sacchetti
Director	Luciano Sita
Director	Ermanno Vichi
Director	Stefano Zolea

Board of Statutory Auditors

Office	Name
Chairman	Antonio Venturini
Standing Auditor	Fernando Lolli
Standing Auditor	Sergio Santi
Alternate Auditor	Roberto Picone
Alternate Auditor	Stefano Ceccacci

Internal Control Committee

Office	Name and Surname
Chairman	Giorgio Razzoli
Member	Ermanno Vichi
Member	Stefano Zolea
Member	Vander Maranini

Remuneration Committee

Office	Name and Surname
Chairman	Giorgio Razzoli
Member	Pier Luigi Celli
Member	Piero Collina
Member	Nicodemo Montanari

Independent Audit Firm

Deloitte & Touche SpA

1.05 Strategy

The results delivered over the last three years bear witness to the important progress made by the Group, which today has become the leading player in terms of turnover and the second in terms of capitalisation in the Italian utility sector. In the 2002-2005 period the EBITDA doubled with an average growth rate of +25% per year.

This expansion is the result of an efficient strategy which has pursued internal and external growth lines considered ground-breaking for the reference industry.

The Group's internal growth, which has made a significant contribution to the increase in EBITDA, has focused, on one hand, on expanding the business turnover by extending the range of services offered to a growing number of customers – hence favouring both customer loyalty and business profitability – and on the other, on raising efficiency levels through cost curbing policies and the reorganisation of operating activities.

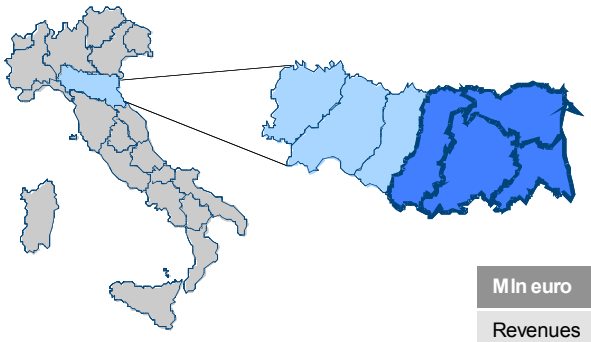
The reorganisation of activities and the centralisation of some activities within the "Industrial Holding" has added value both in terms of the operational management of services, guaranteeing strong presence on the territory while maintaining direct contract with the customer, and also in terms of the pursuit of economies of scale produced by the ever increasing dimensions.

The external growth, through mergers and acquisitions, began with the incorporation of Hera, established from the aggregation of 11 utilities of the Emilia Romagna region, and continued at a constant pace throughout the first three years of activity, contributing to the increase in EBITDA by almost +50% compared to the figure posted in 2002.

In 2004, the merger with Agea, a multi-utility company of the neighbouring province of Ferrara, extended the northern boundaries of the market served and, a year later, the merger with Meta, expanded the territory served to 70% of the Emilia Romagna region, steering the Group to market leadership in its core businesses and creating new opportunities for increased efficiency.

The consolidation strategy implemented over these years has abided by the principles established at the time of the Group's incorporation by bringing companies with business portfolios, cultural and geographical positions which are complementary to those of Hera.

In light of the results achieved it is possible to observe that thanks to these essential guidelines it has been possible to develop group synergies right from the beginning and to continue along a rapid process of integration that has led to the formation of a coherent, homogenous Group.



2002	2003	2004	2005
Seabo, Area, Unica, Ami, Amia, Amir, Taularia, Asc, Amf, Sis e Team	**Geat**	**Agea**	**Meta**

Mln euro	2002	2003	2004*	2005 * §
Revenues	1.067	1.222	1.493	2101
Ebitda	192	242	292	386

* IAS adjusted
§ Pro-forma

The external growth strategy has also been pursued through M&A transactions on mono-business companies which have allowed the Group to considerably strengthen its market positions in waste management and energy activities.

With regard to the **waste** business, mention must be given to the acquisition of the Centro Ecologia Ambiente di Ravenna from the Eni Group, through which a WTE plant dedicated to special waste with Cip 6 authorisation was acquired, and the merger of a business unit of Geat (active in the collection and treatment of urban waste in the municipality of Riccione).

External growth in the **gas** sector has chiefly focused on downstream integration in the value chain through acquisition of small-medium sized companies with a view to gradually completing coverage of the entire reference area.

Acquisitions in the gas sector in 2005	Activity	Ownership
Argile Gas (Ferrara)	Sales	100%
Gasgas (Ferrara)	Sales	100%
Tecnometano (Ferrara)	Distribution	100%
TS Distribuzione (Bologna)	Distribution	100%
TS Energia (Bologna)	Sales	100%
SGR Servizi (Rimini)	Sales	20%

In keeping with the strategic policies of the industry's major European players, Hera has implemented a dual fuel commercial strategy by which **electricity** is offered to customers who are already served by gas activities. The strategy has delivered positive results both in terms of increased customer numbers and volumes of electricity sold and in containing at marginal levels the decline in gas customers due to the fierce competition in the energy market.

The success achieved in the electricity sales market has lead to the need for further expansion in electricity generation (with the acquisition of minority interests in the companies Calenia Energia

and SET realized in 2004) in order to guarantee increasing coverage of market demand in compliance with the principles of economy and efficiency.

Acquisitions in the electricity sector	Activity (Capacity installed)	Ownership
Tirreno Power	Generation (2,600 MW)	5.5%
Calenia Energia	Generation (800 MW)	15.0%
SET	Generation (400 MW)	39.0%

The strategies which in the years since 2002 have lead to the increasing creation of value have been assimilated by all the enterprises which have converged on the Hera Group, through ongoing dialogue with the employees, shareholders and representatives of institutions and the reference territory.

All of the aforesaid strategies have been reconfirmed for the future with the aim of considerably strengthening the results achieved in Hera's short history, as illustrated at the end of 2005 at the time of approval and presentation of the new industrial plan 2006-2008 to the stakeholders.

It is worth remembering that the EBITDA posted in 2005 is already double the figure recorded in 2002, and moreover, that this has occurred two years ahead of the forecasts contained in the Industrial Plan presented at the time of the IPO.

The greatest contribution to growth is expected to come from the continued pursuit of higher levels of efficiency and from increased revenues. The expected synergies will benefit from the possibilities of increased efficiency offered by the recent integrations of Agea and Meta and by the Enel electricity distribution grid of the province of Modena which will become Hera property mid-2006.

In line with the strategic priorities defined, the Group aims to continue to enhance the exclusive know-how gained in the management and construction of new plants for the production of electricity from renewable sources (the last WTE plant became operative in the year 2004 in Bologna) with four new WTE plants, of which three are already under construction.

Lastly, in the light of implementation of the dual fuel policy, 2007 is expected to see the CCGT plants of the investee companies SET and Calenia Energia become operative and likewise the fully Group owned plant in Imola.

The Group's expansion is sustained by an investment plan of over Euro 1.4 billion chiefly financed by cash flows generated by activity in the 2006 – 2008 period. The self-financing capacity of the investments allows the Group to maintain a solid financial structure in 2008 (D/E equal to approximately 0.6).

1.06 Business Sectors

The Group is active in over 170 municipalities in the six provinces of Bologna, Rimini, Ravenna, Forlì – Cesena, Ferrara and Modena, serving a territory which covers approximately 70% of Emilia Romagna, a region with GDP and pro-capita consumption rates among the highest in Europe and where the quality and reach of the local public services have always represented an essential characteristic of economic and social development.

The multi-business nature of the Group's portfolio allows it to achieve a fair balance between services managed under "monopoly regimes" such as the integrated water cycle, the collection and disposal of urban waste, the distribution of methane gas and electricity and the management of public lighting and district heating and services managed under "free competition" conditions such as the supply of methane gas and electricity, the disposal of special and industrial waste.

The complementary nature of these activities (given the market opportunities pursued with "multi-service" commercial proposals) favours the expansion of turnover and the creation of cost synergies and achievement of higher levels of efficiency.

Solid Urban Waste Business

In an Italian context characterised by a considerable dearth of infrastructures, the Hera Group constitutes an outstanding example with one of the nation's most impressive plant structures comprising more than 70 plants capable of covering the full range of possible treatments and exploitation of waste.

The Service is managed in 6 ATOs (corresponding to the Provinces of the Emilia Romagna region in which the Group operates), on the basis of long-term concessions (2012), covering a territory of approximately 2.4 million inhabitants and handles the collection and disposal of approximately 1.5 million tonnes of solid urban waste per year.

Type	Urb. Waste	Urb/Spec W.	Spec Waste	Total plants
Landfills		12	5	**17**
WTE		6	1	**7**
Composting		6		**6**
Chemical-physical treatment			12	**12**
Selection	7	4		**11**
Sludge treatment			5	**5**
Inert treatment			2	**2**
Other plants	6		6	**12**
Total	**13**	**28**	**31**	**72**

Hera is also a leading Italian operator in the recovery of electricity and thermal energy from waste with 7 waste-to-energy plants with a total treatment capacity equal to approximately 610,000 tonnes p.a. and an installed electricity generation capacity equal to 57MW.

Plants	Treatment capacity (ton.)	Installed capacity (MW)
Bologna (Fea)	180,000	20
Rimini	120,000	10
Forlì	60,000	6
Modena	115,000	7
Ferrara	40,000	3
Ravenna	55,000	6
Centro Ecologico di Ravenna	40,000	4,5
Total	**610,000**	**56,5**

In the 2006-2006 period the Group intends to extend the recovery of energy from waste further reducing the environmental impact, that is, the use of landfills, of the service managed. The three-year plan foresees the expansion of 4 existing plants, thus raising total treatment capacity to 1 million tonnes by 2008.

Special Waste Business

In this sector too, the country's supply of waste treatment services is unable to meet domestic demand owing to a shortage of infrastructures which forces may Italian manufacturers to dispose of their waste abroad, hence incurring huge transportation costs.

The Hera Group is one of Italy's top 4 operators in the treatment and disposal of special waste with a treatment capacity equal to 2.2 million tonnes/year thanks to one of the nation's most important network of plants, which includes 31 specifically dedicated plants and 28 mix-usage plants (both special and urban waste).

The 2006-2008 Plan sees further saturation of plant capacity, which has undergone recent expansion with the acquisition of Centro Ecologia Ambiente from ENI, thanks to the positive markets trends already witnessed during 2005.

Integrated Water Cycle

The Hera Group is one of the three leading Italian operators that provide services pertaining to water collection, treatment, adduction, distribution, waste water collection and purification ("integrated water cycle").

The service is performed on the basis of concessions with average expiry in 2022 in 6 ATOs (corresponding to the 6 Provinces of the Emilia-Romagna region in which the Group operates), which include over 170 municipalities; each year approximately 230 million cubic metres of drinking water for domestic and industrial use are supplied.

The Group avails of an extensive, efficient water system extending over approximately 24,000 km and serving over 2.3 million inhabitants, a number which rises considerably in the tourist areas of the Adriatic Riviera during the summer period. Completing the plant structure utilised for the water service is the sewerage network that covers 6,600 km and includes over 350 purification plants.

Energy

The Hera Group is Italy's third operator in the sale and distribution of Gas (with approximately 2.8 million cubic metres sold per year to approximately 940,000 customers, 2,4 billion cubic metres distributed through 11,510 km of network), while in the sale and distribution of electricity, mainly thanks to integration of the Modena area, the Hera Group now ranks among the top Italian operators with over 3.8 Twh sold in 2005 and almost 177,000 customers.

The sale of gas and electricity is an activity in which liberalisation is well established, while distribution is still managed under a monopoly regime based on long-term concessions (approximately expiry 2010 for those relating to methane gas and 2030 for those relating to electricity).

The Hera Group has dealt successfully with the greater competitive pressure in the sale of energy products, by implementing a Dual Fuel commercial strategy and by strengthening Customer Care for domestic customers, thus allowing the Group to withstand competition in gas sales and to increase electricity sales.

In the light of the positive results in the electricity sales market, Hera has implemented a plan for expansion of the electricity generating capacity (primarily achieved through industrial partnerships in which Hera has acquired minority interests) and has stipulated multi-year contracts with both national and foreign suppliers.

All of the energy resources procurement activities are directly managed by Hera Trading, a company specialised in optimising the purchases of electricity through the Italian Electricity Exchange.

The new Industrial Plan expects to see substantial continuation of the results achieved in gas sales (which primarily draw advantage from merger with Meta) while the electricity market is expected to undergo significant expansion, sustained to a large extent by the new plants scheduled to start operations in 2007.

Other Businesses

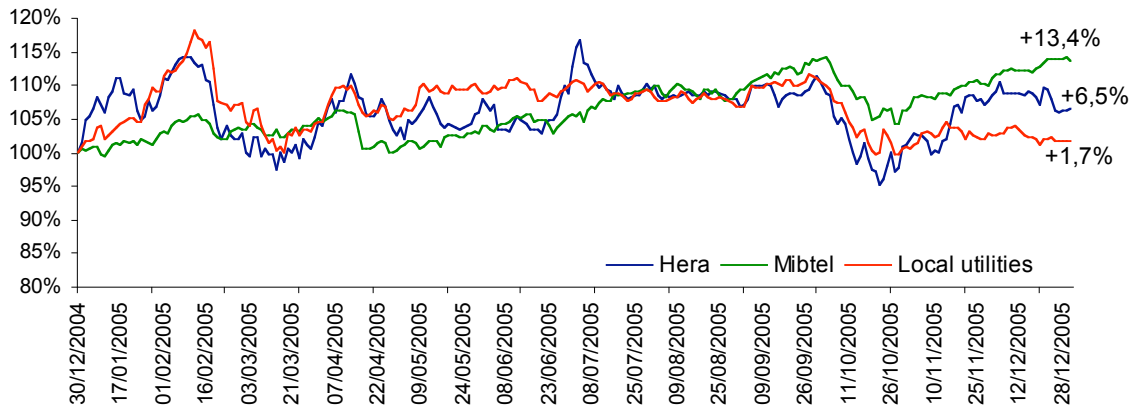
Further to the radical rationalisation of the activities of the companies within the Hera Group, the "other complementary businesses" have been reorganised and provided with integrated management. Within this context, the District Heating activities, in which Hera takes a leading role in Italy, and those relating to Public Lighting, in which Hera ranks second on the domestic market, are of particular importance.

The Group provided approximately 470 GWt/h in 2005 and managed over 293,000 light points within the area in which it operates. The development plans expect to see significant expansion of both these activities through investments and processes to heighten efficiency.

1.07 Hera's Performance on the Stock Exchange

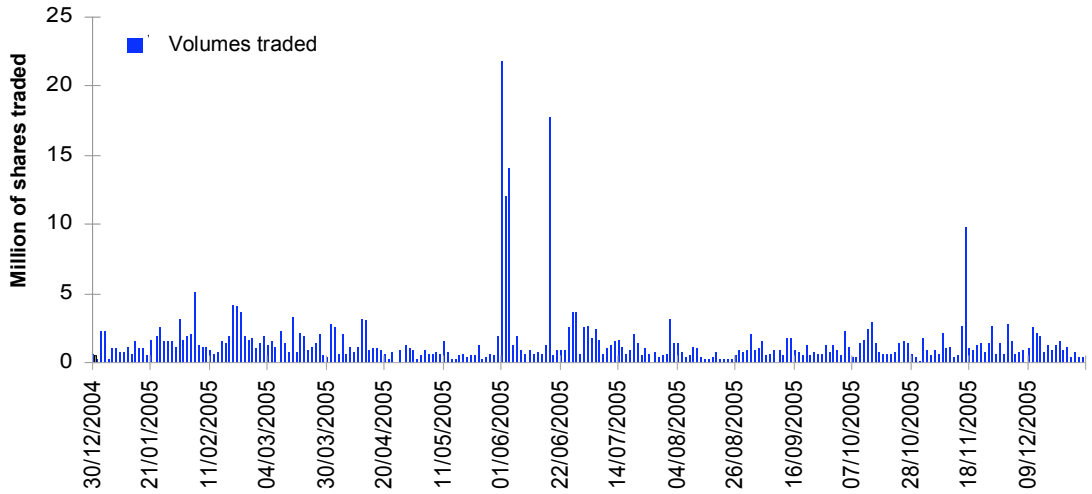
During 2005 the Hera share recorded one of the best performances in the sector of listed former municipal enterprises, closing the year at €2.26 per share with an upturn of +6.5%, compared to the national average of +1.7%. By contrast the Italian public utility services sector as a whole delivered a negative performance of -11.6%, against the +22.0% posted by the index of the European segment.

Hera Share Performance



The modest performance of the Italian multi-utility shares compared to that of the European shares is chiefly due to the uncertainty surrounding the regulatory framework in 2005 and partly due to redress of the previous year's outperformance (+31.5% in 2004).

Hera Share Volumes Traded



The average level of liquidity recorded in trading of Hera shares rose in 2005 for the second consecutive year, thanks to improvement of the medium term profit prospects, the exceptional performance achieved in the previous year, the rise in future targets reported in the industrial plan in November and the intense activity in relations with international investors (European and American). The daily average counter-value rose from Euro 2.3 million in 2004 to almost Euro 3.3 million (+43.5%) last year (in 2003 it was equal to Euro 0.7 million).

In light of increased liquidity and capitalisation (resulting from the merger with Agea), Borsa Italiana included the Hera share in the Midex index, with effect from 21 March 2005, and increased the minimum trading value admitted to the block market (Euro 500 thousand).

Particularly intense trading activity was recorded at the time of dividend distribution (€0.06 per share) and to coincide with the presentation with the new industrial plan (in November).

The Hera share is listed on the "Dow Jones Stoxx TMI" and "TMI Utility" indices, as well as on the "Axia Ethical Index" and "Kempen SNS Smaller Europe SRI Index" ethical indices.

Share Coverage

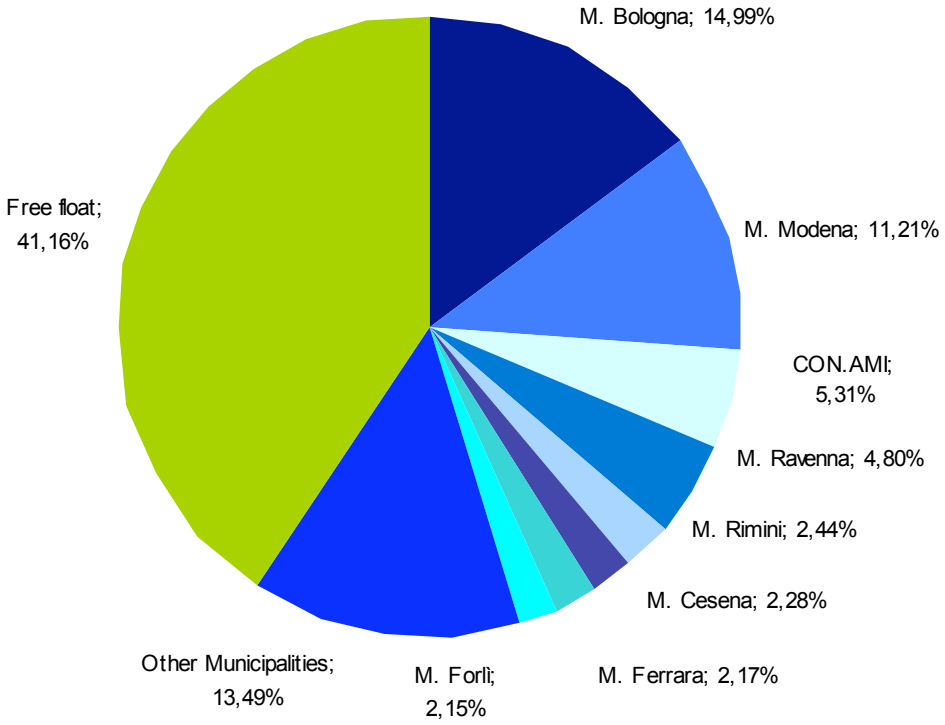
The Hera Group share is one of the most extensively covered in the Italian multi-utility sector, a factor which confirms the financial market's interest. Since the beginning of 2005, 12 independent analysts (half of which are international) have regularly covered the Hera share: Actinvest, Axia (ethical analyst) Caboto, Credit Agricole Indosuez, Euromobiliare, ING, Intermonte Securities, Jefferies, Banca IMI, Kepler and Rasbank. Since the beginning of the year Cazenove has also begun coverage.

Further to the international bond issue worth Euro 500 million listed on the Luxembourg market and placed by Banca IMI, JP Morgan and Citigroup which was implemented in the early months of 2006, some "credit analysts" have also started coverage (Banca IMI and UBS).

Shareholding Structure

Hera SpA has a widespread shareholding structure with over 180 different public shareholders (municipalities in the Emilia Romagna Region), approximately 180 Italian and international institutional investors and approximately 30,000 private shareholders. The absence of a controlling shareholder in its structure (the largest shareholder is the municipality of Bologna with approximately 15%) is a feature which distinguishes Hera from the other Local Utilities.

Shareholding Structure



Further to merger through incorporation of the company Meta S.p.A. 176.8 million new Hera shares were issued. Hence the total number of ordinary Hera shares has risen from 839.9 to 1,016.7 million shares. As at 31 December 2005 the Hera Group capitalised approximately Euro 2.3 billion.

Relations with the Financial Market

Relations with market operators were particularly intense (over 300 encounters held during 2 road shows, one Investor Day, visits at the Group premises and international conferences organised by the Brokers) and bore considerable fruits amongst which the "Leone d'Oro" prize for Investor Relations in the Mid-cap category (Milano Finanza) in addition to the prize for "creation of value" and the nomination for Financial Statements Oscar (Ferpi).

The Hera Investor Relations division maintained close contact with the institutional investors through the use of various means of communication at the time of publication of the annual accounts, presentation of the new industrial plan and merger with Meta S.p.A..

The Investor Relations section available on the Hera website (www.gruppohera.it) has been further developed with the provision of information on Group strategies and has been restructured to improve user-friendliness with specific sections dedicated to each of the major investor categories.

Following the bond issue, a further section for bondholders has also been created, from which it is possible to consult the analysts' studies, the prospectus, the daily trends in bond quotations and the rating achieved (A+ di S&P's and A1 di Moody's).

In 2005, the changes to the website contributed to Hera's promotion to 26th place in the Hallvarson & Halvarson classifications, hence allowing it to achieve equal ranking with Enel and delivering a considerable improvement on the previous year (in 2004 Hera ranked 54th in the web-ranking tables).

1.08 Notice of Call of Shareholders' Meeting

HERA S.p.A.

Registered Office in Bologna Viale C. Berti Pichat, 2/4
Share Capital € 1,016,752,029 fully paid-in
Enrolment number in the Bologna Register of Companies, Tax Code and VAT No. 04245520376

Shareholders are called to Ordinary and Extraordinary Shareholders' Meeting to be held in the Sala Auditorium of the CENTRO CONGRESSI – CNR - Via Gobetti, 101, Bologna on 26 April 2006 at 10 a.m. in first call and if necessary on 27 April 2006, at the same venue and time in second call in order to discuss and deliberate on the following:

Agenda

Ordinary Part:

1. Financial statements at 31 December 2005, Director's Report on Operations, proposal for allocation of profit and Report of the Board of Statutory Auditors: consequent resolutions;
2. Authorisation to purchase own shares and procedures for arrangement of the same: consequent provisions;
3. Acknowledgement of appointment of the members of the Board of Directors pursuant to Article 2449 of the Italian Civil Code;
4. Appointment of a new member of the Board of Directors not designated pursuant to Article 2449 of the Italian Civil Code;
5. Assignment of the audit mandate for the years 2006-2011.

Extraordinary Part:

1. Approval of the "Project for Merger by Incorporation of Geat Distribuzione Gas S.p.A. into Hera S.p.A.";
2. Amendment of Articles 7 and 17 of the Articles of Association;
3. Amendment of Articles 18, 25, 26 and 27 of the Articles of Association, introduction of a new Article 29 to the Articles of Association and renumbering of Articles 29, 30, 31 and 32 of the Articles of Association further to insertion of the new Article 29.

The reports on the matters and proposals on the Agenda, including the parent company and consolidated financial statements at 31 December 2005 and the Director's Report on Operations, have been filed at the registered offices of the Company and at Borsa Italiana S.p.A., in accordance with law and available to persons who may request a copy.

Pursuant to Article 17 of the Articles of Association:

1) Shareholders, with the exception of Shareholders holding rights pursuant to Article 2449 of the Italian Civil Code, representing at least 1% of the shares with voting rights in an Ordinary Shareholders' Meeting, are entitled to submit lists for the nomination of one member of the Board of Directors;
2) the aforesaid lists, in which the candidates must be listed in progressive order equal to the maximum number of members to be elected, will be made public through filing at the registered office and publication in three national newspapers of which two financial, at least 20 and 10

days prior to the meeting respectively;

3) each Shareholder may present and vote for only one list;
4) proposals and votes which breach this rule shall not be attributed to any list;
5) the parties presenting the lists must ensure that they file, together with the lists, a description of the candidates' professional curriculum, the irrevocable acceptance of the office on the part of the candidates (on condition of their appointment) and certification that there are no grounds for ineligibility/forfeiture;
6) no candidate may appear on more than one list and the acceptance of the candidate to more than one list renders the candidate ineligible.

Pursuant to Article 11 of the Articles of Association, the Shareholders holding the requirements set forth in legislative provisions in force are entitled to attend the Meeting.

Shareholders or their representatives who attend the Meeting may forward, by post of by fax, (to number +39- 051-287.244), to HERA S.p.A. corporate secretary's office, copy of the documentation certifying their legitimate right to attend the Meeting, at least three days prior to the date of the Meeting in first call.

Subjects other than shareholders who wish to attend the Meeting must forward, in accordance with the same procedures and terms set forth above, special request.

There is reason to believe that the necessary constituent quorum may not be reached for the meeting in first call and, hence, Shareholders are informed that the meeting shall be held in second call on 27 April 2006 at 10 a.m., in the Sala Auditorium of the CENTRO CONGRESSI – CNR - Via Gobetti,101, Bologna.

Bologna, 14 March 2006

The Chairman of the Board of Directors
(Tomaso Tommasi di Vignano)

2 – CONSOLIDATED FINANCIAL STATEMENTS PRO-FORMA OF THE HERA GROUP

2.01 Directors' report

2.01.1 Corporate Events and Group Structure

The year 2005 saw continuation of the intense activity of rationalisation of the Group's corporate equity investments, which led to the disposal or liquidation of 23 investee companies and to the merger or split-off of two further companies, as scheduled in the disposal programme.
In the course of 2004 the Group had already effected the disposal or liquidation of 12 investee companies, and the merger of four companies operating in the environmental sector.
Further corporate rationalisation transactions have already been scheduled for 2006, chiefly relating to equity investments acquired with the integration of Meta into Hera SpA, and it is with this acquisition, the most important of last year, that the report of the M&A transactions implemented in 2005 opens.

Merger of Meta SpA into Hera SpA
On 29 November 2005, with the execution of the deed of merger of Meta SpA into Hera SpA, the process of integration of the two major multi-utilities of the Emilia Romagna Region, both listed on the Milan Stock Exchange, was completed.
The transaction was implemented through the launch of a partial Public Purchase Offer on the ordinary shares representing 29% of the share capital of Meta, which began on 31 October and was completed on 22 November with a 22% subscription and a capital increase of Euro 176,848,148, with exchange ratio of 1.286 Hera shares to each Meta share.
Hence, as from 31 December 2005, the date of statutory effect of the aforesaid merger deed, the share capital of Hera SpA rose by Euro 839,903,881 to Euro 1,016,752,029, while the accounting and tax effects of the transaction are retro-effective from 1 January 2005.

Acquisition of Tecnometano Srl and Gas Gas Srl
The month of July saw formal completion of the acquisition on the part of Hera of 100% of Tecnometano Srl, a company operating in the natural gas distribution sector within the municipality of Ro Ferrarese (FE), and of 100% of Gasgas Srl, active in natural gas sales in the same territory.
The transaction allows Hera to continue the process of consolidation which it has been pursuing for some time within its own territory and, in particular, in the province of Ferrara, in which there are numerous small operators in the gas business.

Acquisition of Argile Gas Srl
The month of June saw execution of the agreement with the company Gastecnica Galliera Srl for acquisition on the part of Hera Comm of 100% of the company Argilegas Srl, which operates in the natural gas sales sector in the area of Castello d'Argile, in the province of Bologna, where Hera already provides water and environmental services.
The transaction forms part of the process of consolidation launched by Hera in its own territory.

Acquisition of TS Distribuzione Srl and TS Energia Srl

In the month of December Hera SpA acquired 100% of the company TS Distribuzione gas Srl, which operates in the distribution of natural gas in the area of Monghidoro, in the province Bologna, while Hera Comm acquired 100% of the company TS Energia Srl, which operates in the sales of natural gas in the same area.

Incorporation of Hera Energie Bologna Srl

On 30 June Hera Comm Srl, sales company of the Hera Group, set up Hera Energie Bologna Srl, a company which supplies electricity and heat management services to third parties, in which it holds 67% of the share capital.

Further Transactions

Towards the end of 2005 a number of other transactions involving companies which were already members of the Hera Group were implemented.

- On 9 November 2005 Hera SpA acquired from Capital Service Srl 48% of the share capital of Uniflotte Srl, a company which operates in the management and maintenance of equipment, thus increasing its interest from 51% to 99%.
- On 27 December 2005 Hera SpA increased its interest in ASA SpA, from 20% to 51% of the share capital, acquiring 23% from the municipality of Castemaggiore and 8% from UNIECO Soc. coop. ASA SpA operates in the territory of Bologna in the environmental sector and is owner of a landfill for dangerous waste.

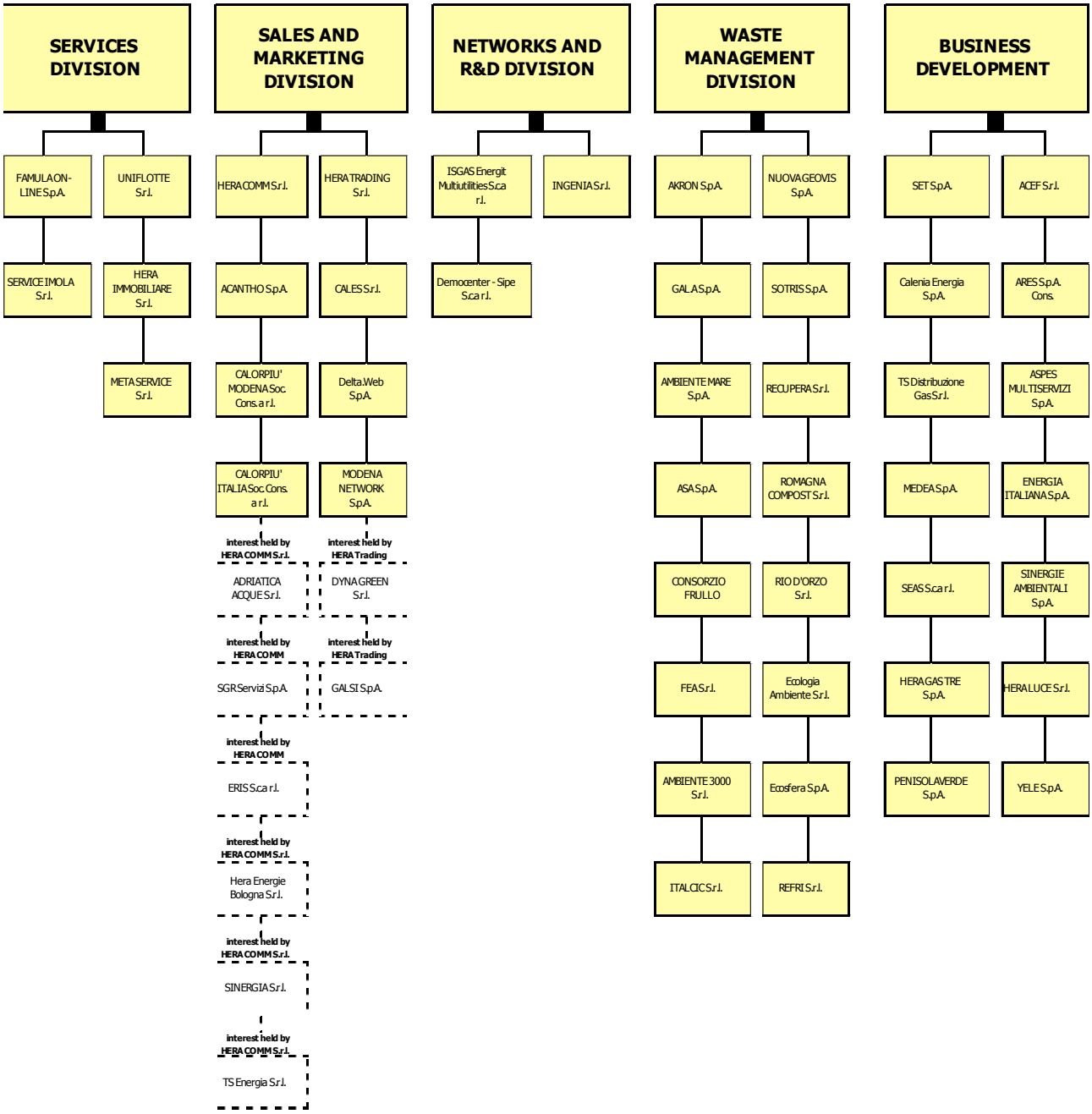
Memorandum of Understanding between Aspes Multiservizi SpA, Aset, Megas and Megas Trade.

On 15 February 2005 a memorandum was signed by the local utilities operating in the province of Pesaro-Urbino (Aspes Multiservizi, Aset, Megas and Megas Trade), the objective of which is to set up a single public service company. The memorandum provides that Hera will be the new company's industrial partner, fulfilling the role that it currently holds in Aspes Multiservizi. Development of the project is currently being examined by the various stakeholders.

Hera-Vng Agreement

On 21 February 2005 VNG – Verbundnetz Gas AG – of Leipzig and Hera SpA, at the signing of the new natural gas supply contract, also signed an agreement to establish a joint company for the trading of methane gas capable of developing its trading capacities on the European energy market. The procedures for incorporation of the company are under completion and the company shall commence operations by June 2006.

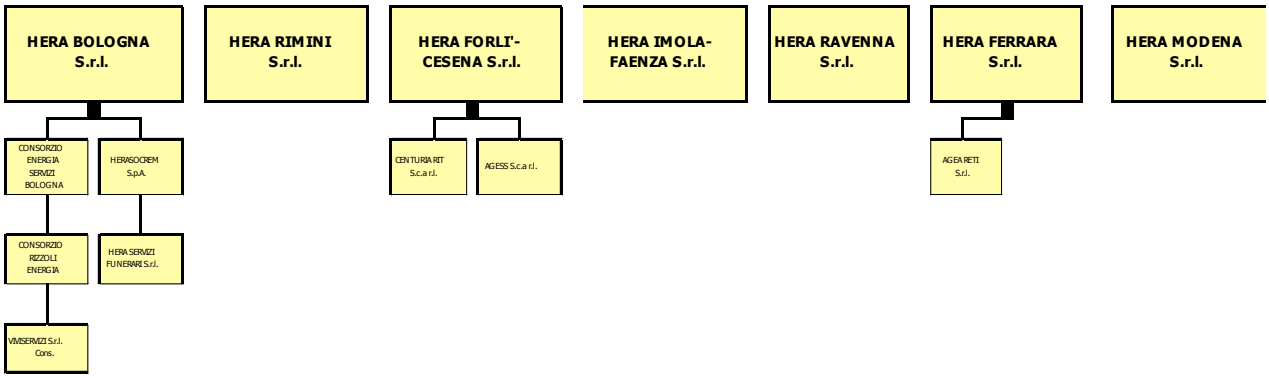
HERA SPA



Disposal of the following equity investments is scheduled: 4 Italy S.r.l. Energy & Environment, Ferrara T.U.A. - Traffico Urbano Autoparking S.p.A., Estense Global Service S.c.a r.l., acquired through the merger/split of AGEA and ACOSEA into HERA S.p.A.

Disposal of the following equity investments is also scheduled: Agenzia per l'Energia e lo Sviluppo Sostenibile, Modena Formazione S.r.l., AV2 Ecosistema S.p.A., Bio Energy S.r.l., Metaenergy S.r.l. and SO.SEL S.p.A., acquired through the merger of META S.p.A. into HERA S.p.A.

HERA SPA


HERA BOLOGNA S.r.l.
HERA RIMINI S.r.l.
HERA FORLI'-CESENA S.r.l.
HERA IMOLA-FAENZA S.r.l.
HERA RAVENNA S.r.l.
HERA FERRARA S.r.l.
HERA MODENA S.r.l.
CONSORZIO ENERGIA SERVIZI BOLOGNA
HERASOCREM S.p.A.
CENTURIA RIT S.c.a r.l.
AGESS S.c.a r.l.
AGEA RETI S.r.l.
CONSORZIO RIZZOLI ENERGIA
HERA SERVIZI FUNERARI S.r.l.
VMSERVIZI S.r.l. Cons.

2.01.02 Performance of the Hera Group in 2005:

2.01.02.01 Financial and Economic Results

As already mentioned previously, 2005 was a particularly intense year for the Group which saw an important expansion of the area in which it operates.

Following the positive conclusion of the transactions for the integration of the Ferrara companies - Agea Spa and Acosea Spa – which took place at the end of 2004, the related organisational integration was also completed by means of the creation of the territorial operating company Hera Ferrara srl at the beginning of 2005.

During the last few months of 2005, the process for the integration of Meta Spa of Modena was therefore launched, concluding with the merger within Hera spa on 31 December 2005; the transaction was however effective retroactively for tax and accounting purposes as of 1 January 2005.

When interpreting the Group's results, the effect of this merger should be taken into account and will be explained more clearly in the various detailed analysis.

During 2005, the process continued for the recovery of efficiency having contributed to the Group's growth over the last few years; besides the afore-mentioned Modena company integration operation, this process made it possible to close the accounting period with sharp improvement in all the main economic-financial figures achieving the results anticipated by the business plan, put together at the time Hera was established, two years in advance.

The figures shown, as required by the legislation for listed companies, reflect the full application of the international IAS/IFRS accounting standards.

2005 featured several events which had both positive and negative effects on the performance of operations:

- the particularly rigid climate trend helped gas sales, and the fully operative status of the new disposal plants started up or acquired in 2004, such as the new waste-to-energy plant at Bologna and the Ravenna Ecologic Centre, supported the satisfactory result of the Environment sector;
- by contrast, the 2004 tariff adjustments of the Authority for Electricity and Gas had a negative impact, especially in the distribution sector, together with the rise in competitive pressure in the gas and electricity sectors, particularly in the metropolitan areas. It should also be pointed out that the Summer was extremely wet and, penalizing the tourist season, had a significant effect on sales of the water cycle in coastal areas.

When interpreting the results, it should also be borne in mind that the Group, between the end of 2004 and 2005, entered into agreements with all the areas agencies in its territory, both for the waste management sector and the water cycle and that, just like all the other companies in the sector, it felt the effect of the important increase in prices of raw energy materials.

The above matters will be looked at in more depth further on, when analyzing the individual business areas.

A summary of the principal results in the period, followed by a more detailed analysis of the results by business area, is shown below:

Income statement (mln/€)	31-dec-2004	Incr.%	31-dec-2005	Incr.%	Change	Change %
Net sales	1.492,6		2.100,5		+607,9	+40,7%
Change in inventories of finished products and products in work in progress	9,2	0,6%	2,2	0,1%	-7,0	-76,2%
Other operating revenues	27,1	1,8%	44,9	2,1%	+17,8	+65,7%
Raw materials and consumable materials	(622,0)	-41,7%	(1.014,8)	-48,3%	-392,8	+63,2%
Service costs	(416,9)	-27,9%	(496,2)	-23,6%	-79,3	+19,0%
Other operating expenses	(92,2)	-6,2%	(124,4)	-5,9%	-32,3	+35,0%
Oersonnel costs	(215,9)	-14,5%	(270,1)	-12,9%	-54,2	+25,1%
Capitalized costs	110,6	7,4%	144,3	6,9%	+33,7	+30,5%
EBITDA	**292,5**	**19,6%**	**386,4**	**18,4%**	**+93,9**	**+32,1%**
Amm. & Depr.	(115,3)	-7,7%	(170,7)	-8,1%	-55,4	+48,1%
EBIT	**177,3**	**11,9%**	**215,7**	**10,3%**	**+38,5**	**+21,7%**
Adjustments to technical fixed assets	-	0,0%	15,5	0,7%	+15,5	+0,0%
Quota of profits/(losses) of associated companies	(3,0)	-0,2%	(0,6)	0,0%	+2,4	-79,5%
Net financial charges	(26,7)	-1,8%	(41,3)	-2,0%	-14,6	+54,9%
Pre-tax profit	**147,5**	**9,9%**	**189,3**	**9,0%**	**+41,7**	**+28,3%**
Tax	(61,1)	-4,1%	(80,5)	-3,8%	-19,4	+31,8%
Net profit	**86,5**	**5,8%**	**108,8**	**5,2%**	**+22,3**	**+25,8%**
of which:						
Minorities	5,5		7,4		+1,9	+34,6%
Gruop net profit	81,0		101,4		+20,4	+25,2%

The increase in **Revenues**, from Euro 1,492.6 million to Euro 2,100.5 million, should be placed in relation to the integration of the Modena area for nearly 65%, and, for the remaining part, essentially the rise in prices/volumes of energy commodities.

There was a significant increase in the Waste Management sector which, net of the integration of the Modena area, produced a rise in revenues of approximately Euro 55 million.

In conclusion, with regards to the tariff trend, as described in more detail in the specific section, against scheduled increases in the Integrated Water Cycle and Waste Management areas there were the awaited tariff reductions, as well as in the Gas Distribution areas and, to a lesser extent, in the area of Electricity Distribution.

The rise in the **Costs of raw materials**, equating to Euro 392.8 million (+ 63.2%), derives from the Modena merger for 55% and from the increase in the costs associated with energy materials for the rest.

Service costs rose from Euro 416.9 million to Euro 496.2 million, disclosing an increase of 19.0%, and entirely concerned the Meta Spa merger.

The increase in the item **Other operating charges**, from Euro 92.2 million to Euro 124.4 million (+ 35.0%), is due, to an equal extent, to the Modena merger and the additional costs associated with the application of the conventions stipulated with the area agencies, in particular for the Integrated Water Service.

Mention should be made of the fact that Meta Spa's contribution to the items "Service costs" and "Other operating charges" amounted in total to Euro 71.7 million, and together with the increase in the item "Capitalized costs", almost entirely justified the cumulative increase of said items: this means that in the previous Hera area of consolidation the increase between 2004 and 2005 saw a rise in these items which was completely negligible. If one takes into account the increase in the services provided, especially in the Integrated Water Cycle area and the new plants of the Waste Management area, the endeavour made by the Group to seek maximum efficiency and containment of the operating costs emerges as evident.

The **Personnel costs** rose from Euro 215.9 million to Euro 270.1 million in 2005 (+ 25.1%); as a percentage of Revenues, the figure improved by 1.6 percentage points, passing from 14.5% in 2004 to 12.9% in 2005. Nearly 80% of the increase in absolute terms concerns the Meta merger. The remaining portion essentially concerns both the personnel in service at the new Waste Management plants and the extraordinary commitment required by the start-up of the new customer computerised information system which led to the use of temporary staff (on average 70 units over the year) as well as a heavier commitment of the customer contact structures.

The item **Capitalized costs** rose from Euro 110.6 million to Euro 144.3 million (+ Euro 33.7 million, or 30.5%) due to the combined effect of the inclusion of Meta and the reduction of the capitalisations on the previous consolidation area of the Group.

The Group's consolidated **EBITDA** at the end of 2005 rose by 32.1%, passing from Euro 292.5 million to Euro 386.4 million. Net of the merger of the Meta Group, the increase in this margin came to around 10.0%. This result was essentially obtained thanks to the positive performance of the Waste Management, Water Cycle and, to a lesser extent, Electricity sectors, while the marginal nature of the Gas business was down despite the favourable climate trend during the last few months of the year.

The percentage-based incidence of the Ebitda dropped from 19.6% to 18.4%, in relation to the afore-mentioned increase in energy commodities' prices.

Amortisation, depreciation and provisions rose from Euro 115.3 million in 2004 to Euro 170.7 million in 2005 (+ 55.4%), with an increase in the percentage-based incidence on revenues from 7.7% to 8.1%. The Meta merger originated around 50% of this increase; the remaining portion is associated with the consistent investment plan sustained and some changes in the consolidation area.

The year 2005 closed with **EBIT** of Euro 215.7 million, up by 21.7% when compared with last year thanks, amongst other things, to the positive performance of the activities for improving efficiency and reducing costs pursued during the year and the satisfactory results of the new plants in the Waste Management area, as well as, obviously, the merger of the Modena area.

The item **Writeback of values of tangible fixed assets** refers to the revaluation of assets written down at the time of the changeover to the new IAS/IFRS accounting standards, passing from reserves which, in relation to the Modena acquisition and a number of contractual changes, saw the reinstatement of the original value in the impairment test at the end of 2005.

The increase in **Financial charges**, rising from Euro 26.7 million to Euro 41.3 million, mainly reflects the rise in figurative charges linked to the application of the financial method to the provisions (IAS Nos. 17, 19 and 37) for approximately Euro 6.2 million, and the increase in indebtedness associated with (i) the transaction for the purchase of Meta shareholdings, (ii) the investment plan carried out and (iii) the increase in working capital, associated with both the rise in total turnover and the implementation of the new SAP billing system.

In light of the above, the year closed with a **Pre-tax profit** of Euro 189.3 million, an improvement of 28.3% on the previous year.

Taxation for 2005 amounted to Euro 80.5 million, with a ratio to Revenues of 3.8% and to pre-tax profits of 42.5%, compared with 4.1% and 41.4% respectively last year.

The **Net profit** for 2005 came to Euro 108.8 million, compared with Euro 86.5 in the previous year, involving a percentage based increase of 25.8%.

The **Net profit pertaining to the Group** rose from Euro 81.0 to Euro 101.4 million in 2005, involving an increase of 25.2%: the minority interest share increased (from Euro 5.5 to Euro 7.4 million) in 2005 thanks to the improved results of a number of consolidated investee companies, in particular Fea Srl.

The table below presents a reclassification of the Group balance sheet at 31 December 2005 presented on a comparative with the results for 2004, showing the evolution of the net capital employed and the sources of financing:

Analysis of the capital employed and the sources of financing of the Group

(milioni di euro)	**31 Dec. 04**	**%**	**31 Dec. 05**	**%**	**Change**	**Change %**
Intangible assets	*362,6*	*22,3%*	*493,0*	20,0%	*130,4*	*36,0%*
Tangible assets	*1.298,9*	*79,9%*	*1.914,9*	77,7%	*616,0*	*47,4%*
Financial assets	*13,0*	*0,8%*	(44,9)	(1,8%)	(57,9)	*-445,4%*
Total fixed assets	1.674,5	103,0%	2.363,0	95,9%	688,5	*41,1%*
Net working capital	113,1	7,0%	322,0	13,1%	208,9	*184,7%*
(Provisions)	(161,8)	(10,0%)	(220,8)	(9,0%)	(59,0)	*36,5%*
Net capital employed	**1.625,8**	**100,0%**	**2.464,2**	**100,0%**	**838,4**	**51,6%**
Shareholders' equity	1.064,2	65,5%	1.490,2	60,5%	426,0	*40,0%*
Long-term debt	*498,9*	30,7%	*523,7*	21,3%	*24,8*	*5,0%*
Net short-term position	*62,7*	3,9%	*450,3*	18,3%	*387,6*	*618,2%*
Net financial position	561,6	34,5%	974,0	39,5%	412,4	*73,4%*
Total sources of financing	**1.625,8**	**100,0%**	**2.464,2**	**100,0%**	**838,4**	**51,6%**

The net capital employed increased as at 31 December 2005 by Euro 838.4 million, from Euro 1,625.8 million to Euro 2,464.2 million. The return on Investment (ROI) dropped from 10.9% in 2004 to 8.8% in 2005, due to the merger of the Modena-based company, the impact of the rise in net working capital and the consistent number of investments made.

Financial assets increased by over Euro 48 million especially in relation to the need to afford guarantee deposits guaranteeing the post-closure fulfilments of the waste landfills for around Euro 33.3 million: the difference concerns the afore-mentioned Modena merger and a number of share capital increases mainly in relation equity investments in companies establishing electricity generation plants such as Calenia Energia.

Tangible and intangible fixed assets as at 31 December 2005 amounted to Euro 2,407.9 million, up by Euro 746.4 million when compared with 31 December 2004, in relation to the merger of the Modena companies and the investments indicated in detail in the following section.

The net working capital rose from Euro 63.7 million to Euro 261.1 million, mainly in relation to the billing problems linked to the start-up of the new customer computerised information system during the period. It should be noted that with respect to 30 September, the situation has progressively stabilized despite the Modena consolidation, the rise in the cost of raw materials and the seasonal trend which increased the turnover.

Provisions increased both as a result of the merger of the Modena companies and the normal provision made to the Provision for Employee Leaving Indemnities (TFR), as well as mainly as a result of:

- the provision of the portion of post-closure costs for landfills;

- the provision of the portions for restoring the networks and plants granted under use to the Group and owned by the companies spun-off (asset companies).

The shareholders' equity, which rose from Euro 1,064.2 million to Euro 1,490.2 million, includes the share capital increase of 176.9 million shares, relating to the inclusion within the shareholding structure of the Municipal authorities associated with the Modena integration operation.

In relation to the afore-mentioned share capital increases, the net financial position passed from Euro 561.6 million as at 31 December 2004 to Euro 974.0 million at the end of 2005.

By way of supporting the increase in debt, during the first few months of 2006 the Group issued a bond totalling Euro 500 million, which made it possible to obtain a higher ratio between medium/long-term debt and short-term debt.

The reliability of the Group's economic and equity structure is validated by the confirmation by Standard & Poor's of an A+ rating over the long-term and by the concession by Moody's of an A1 rating: Shareholders should note that the Hera Group is the only one of the Italian multi-utility companies with this level of rating awarded by the two leading rating agencies.

A detailed analysis is presented below

	31 Dec. 04	*31 Dec. 05*
Non-current securities and other financial receivables	18.9	53.4
Bank payables – long-term	(489.0)	(521.4)
Sums due to other financial institutions (leasing IAS 17)	(28.7)	(39.9)
Financial derivatives		(15.8)
Medium/long-term debt	**(498.8)**	**(523.7)**
Other financial receivables/payables	(1.2)	(1.2)
Bank payables – short-term	(268.1)	(636.8)
Cash in banks and on hand	172.4	189.1
Sums due to other financial institutions (leasing IAS 17)		(9.8)
Current financial assets	34.5	8.4
Net short-term debt	**(62.8)**	**(450.3)**
Total net debt	**(561.6)**	**(974.0)**

Investments

The tangible and intangible investments of the Group, inclusive of the increase in leased assets dealt with by applying the IAS standards, amounted to Euro 331.3 million, as against Euro 225.4 million last year.
Shareholders are informed that investments in 2005 also include the balances relating to the Modena area (former Meta) for a value of around Euro 54.4 million.
Investments made during 2004 are analyzed below by business area.

Total Investments

(Euro millions)	31 Dec. 04	31 Dec. 05
Gas area	23.4	44.3
Electricity area	3.8	8.4
Integrated water cycle area	67.1	76.2
Waste management area	42.2	100.2
Other services	29.4	24.4
Central structures	59.5	77.8
Total	225.4	331.3

The gas service investments within the area it operates in, mainly refer to extensions, reclamation and enhancement work on the networks and plants and are in line with the same period last year, the area of consolidation being the same; the increase of around Euro 6 million refers to measures in the Modena area. The investments made by the company Medea concern the second section of the work for the methane conversion of Sassari. Plant purchases were made during 2005 for a total of Euro 16.3 million.

Gas

(Euro millions)	31 Dec. 04	31 Dec. 05
Territory	18.1	24.2
Medea	5.3	3.8
Plant acquisitions		16.3
Total Gas	23.4	44.3

The Electricity service investments referred in part to the extension of the service and to the extraordinary maintenance of the plants located within the Imola area already managed in 2004 (Euro 2.9 million) and Modena area (Euro 4.5 million), and in part (Euro 1 million) they concern the Imola co-generation plant currently under construction.

Electricity

(Euro millions)	31 Dec. 04	31 Dec. 05
Territory	2.3	7.4
CCGT	1.5	1.0
Total Electricity	3.8	8.4

The increases in investment in the sphere of the aqueduct and purification sectors are entirely due to the work carried out in the Modena area, and mainly refer to extensions, reclamation and enhancement work on plant. In the sewerage sector, there was also an increase in the sphere of the areas previously managed, particularly in the Bologna area, which derives from the work agreed with the pertinent ATOs (Area Water and Waste Authority Agencies).

Integrated water cycle

(Euro millions)	31 Dec. 04	31 Dec. 05
Aqueduct system	43.2	48.4
Purification system	13.4	13.2
Sewerage system	10.5	14.6
Total water cycle	67.1	76.2

In the Waste Management area, the increase in investments was mainly attributable to Modena (Euro 3.4 million) and to a minimum extent to the area previously managed. The sharp increase in measures carried out by investee companies is attributable to the measures financed by means of leasing on the plants of the Ravenna Ecologic Environmental Centre (Euro 16.1 million) and Akron (Euro 7.9 million). The investments on the waste-to-energy plant at Bologna (FEA) concerned work for the completion of said plant, while Euro 13.2 million was spent on the waste-to-energy plant at Canal Bianco and Euro 15.6 million on the waste-to-energy plant at Modena concerned the start-up of the work relating to the construction of the new waste incineration lines.

Waste management

(Euro millions)	31 Dec. 04	31 Dec. 05
Territory	11.3	15.4
Investee companies	16.5	33.4
FEA	12.3	20.0
WTE Canal Bianco	1.1	13.2
WTE Modena		15.6
Other WTE	1.0	2.6
Total Waste management	42.2	100.2

District heating service investments mainly concerned extension work on the service in the Bologna (Euro 5.2 million), Ferrara (Euro 2.9 million) and Imola (Euro 2 million) areas. Telecommunications investments referred to continuation of the creation of the Regional Telematic interconnection Plan via fibre optics. In the public lighting field, investments concerned the installation of new lighting units and the extraordinary maintenance of the existing ones; the increase refers to the measures carried out in the Modena area (Euro 1.7 million). The investments concerning other services were down considerably and mainly refer to cemetery services and the management of heating plants.

Other services

(Euro millions)	31 Dec. 04	31 Dec. 05
DH	8.9	10.8
TLC	9.8	4.4
Public lighting	2.8	3.4
Other	7.9	5.8
Total other services	29.4	24.4

Once again during 2005, the considerable commitment continued for the bringing onto stream of the corporate information system with particular reference to the SAP-ISU system and the related interfacing with SAP-R3; the increase with respect to the previous year is partly due to the need for integration with the Modena SAP information system. The increase in buildings was effected by the inclusion in 2005 of investments in the Modena area (Euro 5.3 million) and the work relating to the rationalisation and standardisation of the spaces. Within the sphere of other investment, purchases of vehicles and containers took on particular importance (Euro 20 million), mainly finalized at achieving the limits of differentiated waste collection envisaged by current laws and by the agreements with the pertinent ATOs.

Structures

(Euro millions)	31 Dec. 04	31 Dec. 05
Buildings	5.5	12.8
Information systems	24.4	34.8
Other investments	29.6	30.2
Total	59.5	77.8

2.01.02.02 Regulatory Framework

1 - Energy: evolution of the legislative framework

The reference framework of legislative and regulatory evolution in the energy markets has been heavily conditioned by international circumstances and in particular by the strong rise in the price of raw materials and by the Russian-Ukrainian crisis concerning the transit of natural gas from the cultivation and extraction sites to the Western European consumption terminals. This contingency has further emphasized the insufficiencies already apparent in the raw material importation and storage infrastructures, which contribute to the difficulties in transition from the Italian system to an accomplished market model.

The warning level reached in the winter of 2005-2006 in the natural gas procurement policy, which coincided with peak winter consumption and the Ukrainian crisis, has in fact brought the issue of the structural deficiencies in the Italian system to the fore, disproving the fears of an alleged overabundance of future infrastructures arising from the simultaneous pursuit of numerous gas pipeline and GNL plant construction projects.

The limited storage capacity available, which was put to the test by the crisis which arose in the last months of the winter 2004/2005, when it proved necessary to interrupt supply to the uninterruptible customers, to maximise importation and to avail of strategic stockpiles, led the Authority to bring to Parliament's attention the risk of a crisis which was repeated, and exacerbated by the absence of international supplies, between late 2005 and early 2006.

In August 2005 the Authority identified the "outsourcing" of the management of underground storage and the expansion of said storage, as the key elements by which to raise the safety margins of the Italian system for management of consumption peaks. This proposal forms part of a package of measures put forward by the Authority in January 2005 and aimed at encouraging competition and expansion of the Italian procurement system (amongst which, the reduction of the share held by Eni in the share capital of the Snam Rete Gas (SRG) by at least 5%, the simultaneous contribution to SRG of the international transport assets currently under Eni's control, Eni's withdrawal from STOGIT's share capital and the subsequent possible merger of STOGIT with SRG, as well as disposal to third parties of part of Eni's long-term importation contracts).

At the end of legislature Parliament released the conclusions of the investigative inquiry, furthered by the X Permanent Commission of the House of Commons, on the evolution of the domestic energy market.

Referring to the conclusion of previous inquires conducted by the Italian Authority for Electricity and Gas and the Italian Anti-Trust Authority, which had recognised that the enduring oligopolistic structure of the markets which are "upstream" in the energy chain represented an obstacle to the process of liberalisation, the X Commission observes, with regard to the natural gas market, that the current limited importation capacity may be attributed "to a strategy of limiting supply implemented over the last years by the dominant operator" and recognises the urgent need to accomplish the scheduled 15% increase in the importation capacity attributable to expansion of the TAG-TTPC infrastructures, expressing the hope that the "third party independent" operators may play a decisive role in managing the additional capacity.

However the ensuing legislation appears to have reacted in a contradictory manner to the recommendations provided by the sector's regulatory authorities and by Parliament itself. On one hand the law decree has favoured competitiveness by simplifying the authorisation procedures for construction and expansion of GNL terminals, on the other hand the regulations introduced at the end of 2005 (financial bill and the so-called "thousand extensions" decree) have extended from 2007 to 2008 the term within which Eni must reduce its interest in Snam Rete Gas to less than 20%.

Integration of Environmental Aspects in the Energy Market

The adoption of imported applicative orders of primary legislation in favour of the integration of environmental aspects in the rules governing the functioning of the energy markets has contributed to the definition of the current state of renewable sources incentive programmes and to Italy's definitive subscription to the European emission rights market.

Of particular importance is the ruling arising from Law no. 239 of 23 August 2004 (reorder of the energy markets, known as the "Marzano Law") and from Legislative Decree no. 387 of 29 December 2003 (assimilation of the EU laws concerning renewable sources incentive programmes in the domestic energy market).

- In implementation of the provisions of the framework law for reorder of the energy markets, the Italian Authority for Electricity and Gas passed an important resolution, no. 34/2005, which establishes the incentives to withdrawal of electricity produced by renewable sources plants and by smaller sized plants powered by alternative sources. The Ministry of Productive Activities, working with the Department for the Environment, has issued decrees for implementation of regulations which provide for assignment of "green certificates" to co-generated thermal energy distributed through district heating networks.
- In accordance with the provisions of Legislative Decree 387/2003 the decree introducing "Criteria for incentives to the production of electricity through photovoltaic conversion of solar energy" has been approved. Said decree provides for economic contributions for the construction of photovoltaic plants with nominal power of no less than 1 kW and no more than 1,000 kW connected to the electricity grid, for the concession of which AEEG (the Italian Authority for Electricity and Gas) and GRTN (the National Transmission Grid Operator) have prepared the appropriate applicative regulations and launched the selection procedure. Legislative Decree 387/2003 has provided the base for other important legislative provisions, approved in the second half of 2005, which define the framework of incentives for energy produced by waste combustion and by biomass (with the period of recognition of the green certificates being extended by four years, but with application of a quota of 60% of the energy introduced to the network).
- Definition of the rules governing the functioning of the organised market of energy efficient securities (TEE) by the GME (Electricity Market Operator), in association with the AEEG, completed the legislative process prescribed by the decrees of 20 July 2004 which imposed obligatory objectives of energy intensity reduction on the distributors of electricity and natural gas. March 2006 saw the formal start of the exchange of energy efficiency certificates on the

electronic platform set up by GME; the market's effective launch was hindered by delays in certification of the securities.

- Publication in Official Gazette no. 57 of 9 March 2006 of the Decrees of 6 February and 23 February 2006 (respectively concerning the recognition of authorisation to emit greenhouse gas and the issue of the CO_2 quotas for the 2005-2007 period) concluded the process for approval of the national plan for allocation of allowances provided for by Directive 2003/87/EC. The final consent for assignment of certificates to approximately one thousand authorised entities was received from the European Commission on 23 February 2006. The GME subsequently ordered the launch of the exchange of certificates on the market platform.

1.1 - Electricity: regulations and tariff framework

During 2005 and in early 2006 some important orders for integration of the regulatory framework governing the electricity market were adopted. With resolutions 298 and 299 passed on 29 December 2005 in particular, the Authority respectively implemented repeal of the "Ct" parameter (at the base of the regulation of significant economic relations for entities operating in distribution) and updated the reference parameters for the definition of electricity tariffs in the 1st quarter of 2006.

The early months of 2006 saw the launch of the procedure for revision of the transmission and dispatchment code, which will also take into account the corporate transformations experienced by the national transmission company. Further to unification of the ownership and management of the national transmission grid, pursuant to Prime Minister's Decree of 11 May 2004, some regulation and control functions have been split off and assigned to a new legal entity, the Gestore del Sistema Elettrico (the Electricity System Operator), which began operations in November 2005.

Regulation of distribution tariffs is still conditioned by the litigation relating to the Code containing the provisions for electricity (resolution 5/2004) and in particular to the procedure for recognition of specific company equalisation (resolution no. 96/2004). Some operators disputed the ban on use of the acquisition price (for example, of former Enel business units) in the valuation of assets remunerated for the purposes of recognition of greater company costs which give rise to a positive specific equalisation. A preliminary ruling of the administrative court (TAR of 13 May 2005), which was partially favourable to the plaintiffs, was contradicted on appeal by the State Council. While awaiting the outcome of this judicial issue, the Authority has recommenced analysis of the positions of the entities which had requested recognition of the specific company equalisation which had been suspended following the May 2005 ruling. The CCSE (Electricity Equalisation Fund) has received mandate from the Authority to analysis the documentation sent by the companies that did not avail of "historical" stratification of the value of assets, also on the basis of the conclusions of special studies fostered by the Authority in association with the CCSE and partly performed at the companies concerned.

1.2 – Natural Gas: regulations and tariff framework

While the regulatory and tariff framework of the "upstream" segment has achieved relative stability (resolutions 166 and 179 have respectively established the criteria for the economic considerations and approved the transport tariffs for the 2005-2008 regulatory period, while resolution 168 has brought approval of the new criteria for re-gasification tariffs), the natural gas distribution and sales sectors have been heavily conditioned by the litigation ensuing from the introduction of the new criteria for the determination of distribution tariffs for the 2004-2008 period (resolution 179/2004) and of new rules for the revision of the variable consideration relating to wholesale marketing (resolution 248/04, the principles of which were reiterated at the end of 2005 with resolution 298).

Further to judgment no. 531 of 11 March 2005, with which the Lombardy Regional Administrative Court (TAR) partially annulled resolution no. 170/04, the Authority launched the procedure for revision of the tariff regime. Said procedure led to the approval of resolution no. 122/05, through which operators are awarded remuneration of the investments which were not considered by the previous resolution no. 179/04. The Authority is expected to take further action with regard to the other main aspect of the dispute, that is, the quantification of the recovery of productivity (established as 5% p.a. of the entire sum of the operating costs and depreciation/amortisation during the full regulation period), for which even the appeal judges partially admitted the plaintiffs' observations.

On 28 June 2005 the Lombardy TAR also annulled the aforesaid resolution 248/04, by which the Authority had ordered reform of the mechanism of revision of the "raw materials" tariff component (in particular reviewing the reference basket of oil products, the price of which determines the revision and the algorithm for transfer of the international crude oil price trends to the tariff) with the aim of neutralising the effect of the substantial increases in oil prices.

The resolution also contained a mechanism for transfer to the importers/wholesalers of the losses sustained by the sellers who were not able to renegotiate the disparity between the sales prices, adjusted on the short-term, and the procurement costs (which can only be adjusted at intervals of no less than one year).

The order, which affected the method of adjustment of the costs of raw materials, would have limited the tariff increase passed at the end of 2004 to 2%; in the absence of this intervention, the tariff increase would have amounted to 3.7%, equivalent to an average cost increase of €29 p.a. for consumers.

In October 2005 the Authority obtained suspension of the referenced TAR sentence related, however, solely to the appeal presented by Hera Trading (the "Hera Trading Case") from the State Counsel. Hera Trading, currently without end user clients in its portfolio, was not impacted by this sentence. The Authority then proceeded to reiterate the criteria for tariff updates as per Resolution 248/04 in a new provision (Resolution 298 dated December 29th, 2005) in order to prevent any additional increases in final prices. The same resolution 298/05 was, in the end, suspended by TAR as it awaited the final sentence related to the appeal involving the previously mentioned Resolution 248/04.

On March 21st, 2006 the State Counsel sustained the Authority's appeal for the annulment of the first degree sentence related, once again, solely to HERA Trading. In regard to the annulments

requested by the other operators, these are still pending and the discussion of same with the State Counsel should take place next June 6th, the date in which the case related to *Gas delle Concordia* (which, in light of the lengthy appeal process, should result in the passage of the annulment of the Lombardy TAR sentence into final judgement) will also be discussed .
While waiting for definitive resolution of the case, the companies selling to end user clients have opted to base the "raw materials" component of tariffs on the provisions of the current norms (specifically Resolution 195/2002), for both 2005 and first quarter 2006.

On March 28th, 2006 the Authority issued three new resolutions (63/06, 64/06, 65/06) that, in addition to updating fuel prices for the period April – June 2006, introduced criteria and indications that confirmed the operators' expectations regarding the presumed neutrality of Resolution 248/04 and the regulated tariffs applied to end user client sales, as well as the willingness of the Authority itself to re-examine, as part of a specific investigation, the mechanisms applied to the updating of fuel prices provided for in Resolution 248/04 and to introduce instruments designed to safeguard the operators that "manage the natural gas supply through specific negotiations" (Hera Trading, based on the gas release contracts stipulated in 2004, is considered one of these operators).

In regard to any provisions related to 2005 volumes, and in relation to which the State Counsel should rule on the future efficacy of Resolution 248/04, at present the Authority's provisions contained in Resolution 65/06 refer solely to account margins (0.276 Euro cents/mc) that, given the difficult of retroactive application, are applicable solely to volumes sold in second quarter 2006.

In light of the above, the annulment of Resolution 248/04 issued by the Lombardy TAR currently in force and the content of the recent resolutions issued by the Authority mentioned above, the Group has decided not to proceed with any balance sheet provisions or coverage of the possible impact on P&L resulting from application of the above mentioned norms.

2 – Local Public Services: changes in the regulatory framework

On 10 February 2006 the Cabinet definitively approved the draft legislative decree containing the "Environmental Regulations", thus exercising the authority attributed thereto by Law no. 308 of 15 December 2004 which assigned the Government the responsibility for reforming, reorganising and rationalising the entire regulatory framework (waste management, territory and water protection, assessment of environmental impact, large-scale combustion plants) also through assimilation in the Italian order of other directives including the EU framework directive on the protection and management of waters.

The legislative decree on environmental issues, which has not yet been published in the Official Gazette as it has yet to be signed by the President of Italy, assembles, in 318 articles, the provisions previously distributed in special draft decrees relating to various issues covered by the delegated authority (waste management, earth and reclamation, waters, air quality, environmental impact assessment).

The new legislation introduces important new aspects especially with regard to municipal waste management, for which new criteria of assimilation have been provided in addition to the

possibility, under certain conditions, of removing substantial portions of materials conventionally included in the integrated management cycle, if these may be directly recycled in the production process (so-called "secondary prime materials"). The economic and organisational implications are not yet clear and must also be assessed in relation to the secondary legislation of the Government itself and of the local authorities.

The management model which prevails in Emilia Romagna, on the basis of which Hera undersigned the Convention for the management of services, is not called into dispute by the new regulations. While, for example, the legislative decree provides for the obligatory introduction of tenders (by 2006) for selection of integrated operators, it does not repeal the provisions which legitimate the existing assignments (above all, Article 113 of the Consolidation Act of local authorities as reformed by the 2004 finance bill). Hence the public selection procedure is strictly requested for the new assignments.

Among the changes for the waste sector, attention is drawn to the obligation to phase out the tax regime in favour of the application of an environmental hygiene tariff.

The fact that the Regions and local authorities have raised some objections, including appeals to the Constitutional Court for the cases of alleged breach of the distribution of competences and for exceeding delegated authority, leads us to believe that the procedure to enact this legislation shall be taken up again in the next legislature; the very coherence of the definition of "waste" (upon which is based the regulatory framework of the articles pertaining to the management of environmental services) with the community notion, consolidated by the directives and decisions of the court, is doubtful and shall certainly be the subject of jurisprudential intervention. However this does not exonerate the entities and operators from applying the part of the regulations that will be immediately compulsory when the legislative decree will become final state law with publication in the Official Gazette.

During 2005 the grounds for dispute between State and Regions over the attribution of legislative and regulatory powers pertaining to the organisation of local services were manifold. With judgment no. 335 of 27 July 27 2005 the Constitutional Court issued its decision on the ruling of constitutional legitimacy proposed by the Prime Minister in relation to some articles of the Emilia Romagna Region Law No. 7 of April 14, 2004, containing provisions on environmental matters. The government specifically contested the attribution at regional level of the regulatory power in the matter of tariffs; in rejecting the appeal, the Supreme Court confirmed the legitimacy of the regulations made by the regional legislator.

The consequences of the judgment are still not clear. The Court confirmed the supremacy of the State's competence for the substantial part of the tariff regulatory activity which is necessary to the protection of competition and, at the same time, recognised that for the part which does not relate to the protection of competition (of exclusive state competence, where not that of the European Community) the competence of the Region must be admitted.

A balanced reading of the judgment leads us to believe that, although it confirms the State's power to "guide" and where appropriate, standardise the tariff systems as a safeguard to a balanced and competitive economy, it allows the Regions sufficient flexibility to introduce to the regulations tariff

variants and aspects not attributable to competition, such as the protection of the environment and service quality incentives.

In the same judgment the Constitutional Court also ruled against another regulation approved by the Emilia Romagna Region, which introduced an additional tax for the conferment to landfills of solid urban waste. For this matter the Court deemed that the Region did not have the right to intervene on an important taxation matter and one strictly attributed the powers to the State.

2.1 – Regulation and Local Tariff Framework

2005 saw completion of the process for definition of the convention-based relations between Hera, in its capacity as safeguarded operator, and the local Agencies (ATO) in compliance with the provisions of the Emilia Romagna Region law pertaining to regulation of local public services.

Hence, to date Hera manages the urban hygiene services and the integrated water services in six areas corresponding to six provinces (Bologna, Ferrara, Forlì-Cesena, Modena, Rimini and Ravenna). The relative conventions cover the exclusive management of the services for a period which varies between 10 years for environmental services and approximately 20 years for water services. The conventions are accompanied by annexes containing tariff scheduling documents which establish the development of considerations, for the services concerned, for periods of at least three years. Definition of the tariffs for the subsequent period of regulation is on hold until the environmental services in the municipalities which still apply the taxation method TARSU have completed passage to tariff-based methods, and hence should take place at the end of the first period of assignment. It is however possible that the parties will agree to implement tariff revisions during the first three-year period in the face of particular events or significant variations in the quantity and quality of the services managed.

Despite the fact that the CIPE (Interdepartmental Committee for Economic Planning) did not intervene in the last revision of the water tariffs (applying to the 2003-2005 period) prior to full application of the normalised method, the latter has already been applied in the areas under Hera's management.

Any variations to the legislative and regulatory framework, prescribed by the legislative decree concerning environmental issues, should not come into effect prior to conclusion of the first tariff period governed by the Conventions in force. The amendment to the normalised tariff method introduced by the Galli law, replaced by said decree, in fact requires secondary law-making which is not likely to not take place before 2007.

2.01.02.03 Tariffs

1 Gas Distribution: tariff framework

2005 was a year of great uncertainty for the tariff system governing the distribution of gas. In particular the second regulatory period, which began in October 2004 (AEEG Resolution 170/04), provided for a reduction of the remuneration of invested capital from the 8.8% of the previous period to 7.5% and a scheduled recovery of productivity equal to 5% applied only to the operating costs and to technical amortisation of recognised capital (in line with the impact generated by the scheduled recovery of profitability provided by the previous regulatory period).

In February 2005 the TAR of Lombardy accepted the appeal filed by some distributors and suspended resolution 170/04. AEEG applied to the Council of State which, while waiting to examine the reasons for the TAR suspension, ruled in favour of a solution of continuity in the application of the reference tariff regime and decreed the suspension of the TAR judgment and the consequent application of resolution 170/04. In August 2005 AEEG issued resolution 122/05 which admitted part of the motions filed in the appeal. On the base of said resolution the tariffs for gas year (GY) 04/05 were defined as were those for GY 05/06. The tariffs for GY 04/05 are been approved on March 2006 while, as far as the tariffs for GY 05/06 are concerned, further resolution is expected from AEEG which will assimilate the indications of the Council of State aimed at inducing a reduction of the scheduled recovery of productivity and accordingly the subsequent definition of the GY 05/06 tariffs.

Hence Hera's Financial Statements 2005 reflect the effects of Resolution 122/05 and subsequent rulings.

Against this tariff backdrop the revenues from gas distribution in 2005 were equal to approximately Euro 127 million with distributed volumes equal to approximately 2.4 billion m^3 with an average unitary tariff of 5.3 €c/m^3.

Gas Distribution	**2004**	**2005**	**Δ %**
Hera without ex Meta			
- Revenues Ml €	113,3	107,7	-5%
- Volumes Ml cm	1912	2019	6%
- Average tariff (€c/cm)	5,9	5,3	-10%
Hera with ex Meta			
- Revenues Ml €		126,7	
- Volumes Ml cm		2399	
- Average tariff (€c/cm)		5,3	

For the purposes of comparison with 2004 the like-for-like revenues (excluding former Meta) were equal to approximately Euro 108 million (-5% v 2004) with volumes distributed equal to approximately 2 billion cubic meters (+6% v 2004). Hence the year 2005 featured a 10% decrease in average unitary tariffs chiefly due to the tariff revisions induced by the AEEG resolutions 170/04 and thereafter.

2. Electricity Distribution: tariff framework

For the tariff system governing electricity distribution, 2005 was the second year of the current regulatory period *and hence represented a year of considerable tariff stability which saw consolidation and full application of the principles ratified by AEEG resolution 5/04 and namely:*

- *the removal from the distribution tariff for customers with uses other than domestic of the components relating to the services of transmission, metering and marketing, transferred to the sales tariff and applied on the customers of the restricted market (with considerable perimeter variation of the tariff in 2004);*
- *the launch of the general standardisation of revenues, obtained by the application of the D2 and D3 tariffs to domestic customers, using, as reference the D1 tariff;*
- *the transfer to the sales portion of the component covering the costs of dispatchment, activity which, with the launch of the electricity exchange, is performed by Acquirente Unico:*
- *a scheduled productivity recovery level (X-factor) equal to 3.5% pa. for distribution and 2.5% p.a. for transmission.*

Against this tariff backdrop the revenues from electricity distribution in 2005 were equal to approximately Euro 29 million with distributed volumes equal to approximately 1500 Gwh with an average unitary tariff of 1.9 €c/kwh.

Electricity Distribution	**2004**	**2005**	**Δ %**
Hera without ex Meta			
- Revenues Ml €	10,0	9,9	-1,0%
- Volumes Gwh	536	544	1,5%
- Average tariff (€c/kwh)	1,9	1,8	-2,5%
Hera with ex Meta			
- Revenues Ml €		28,6	
- Volumes Gwh		1507	
- Average tariff (€c/kwh)		1,9	

For the purposes of comparison with 2004 the like-for-like revenues (excluding former Meta) were equal to approximately Euro 10 million (-1% v 2004) with volumes distributed equal to approximately 544 Gwh (+1.5% v 2004). Hence the year 2005 featured a 2.5% decrease in average unitary revenues.

3. Integrated Water Cycle: tariff framework

January 2005 saw the new tariffs agreed with the ATOs for the period 2005-2007 enter into effect. The new tariff was the first step towards tariff convergence which will lead to full application of the normalised method.

Against this backdrop Group revenues from integrated water cycle management for 2005 were equal to approximately Euro 293 million with water system volumes sold equal to approximately 228 million m^3 with an average unitary tariff of 1.29 €/m^3.

Water	**2004**	**2005**	**Δ %**
Hera without ex Meta			
- Revenues* Ml €	256,1	263,1	3%
- Volumes** Ml cm	203	201	-1%
- Average tariff (€c/cm)	126	131	4%
Hera with ex Meta			
- Revenues Ml €		293,5	
- Volumes Ml cm		228	
- Average tariff (€c/cm)		129	

* Including the amount related to piani stralcio of 2004
** Adjusted with intercompany

For the purposes of comparison with 2004 the like-for-like revenues (excluding former Meta) were equal to approximately Euro 263 million (+3% v 2004) with volumes sold equal to approximately 201 million cubic meters (-1% v 2004). Hence the year 2005 featured a 4% increase in average unitary tariffs arising from a combination of two effects:

- +3% for the effects arising from application of the tariff increase agreed with the ATOs;
- +1% for the effect of completion of the water cycle in the municipalities where the water system and purification services were provided but not the sewerage service.

4. Urban Hygiene: tariff framework

In 2005 the urban hygiene service was provided to 135 Municipalities in a context characterised by completely disparate application of the Ronchi Decree. Stipulation of the conventions with the ATOs, which was scheduled for 2004, was concluded in 2005.

In this context 2005 as characterised:

- by the application of the tariff only in 28% of the municipalities served, corresponding to 42% of the population served (all of the Regional capitals with the exception of Bologna have already changed to tariffs), in line with the situation of the last two years;
- by the presence of vastly disparate situations of application of the normalised method for the determination of the revenues which led to significant gaps between expected and actual revenues.

Against this backdrop Group revenues from urban hygiene management for 2005 were equal to approximately Euro 281 million with average revenues per served inhabitant equal to 122€/inhabitant.

Waste	**2004**	**2005**	**Δ %**
Hera without ex Meta			
- Revenues Ml €	236,8	242,7	2,5%
- Inhabitants served ('000)	1.930	1.949	1,0%
- Average unit revenues(€/inhabitant)	123	125	1,5%
Hera with ex Meta			
- Revenues Ml €		280,7	
- Inhabitants served ('000)		2.294	
- Average unit revenues(€/inhabitant)		122	

For the purposes of comparison with 2004 the like-for-like revenues (excluding former Meta) were equal to approximately Euro 243 million (+2.5% v 2004) with a 1% increase in population giving rise to an increase in average unitary revenues per served inhabitant equal to 1.5%.

2.01.02.04 Analysis by Business Area

An analysis is presented below of the operating results achieved in the business areas in which the Group operates: (i) sector concerned with the distribution and sale of methane gas and LPG; (ii) sector concerned with the distribution and sale of Electricity, (iii) Integrated Water Cycle sector (Aqueducts, Purification and Sewerage), (iv) Waste Management sector (waste collection and treatment) and other activities (District Heating, Public Lighting, Heat Management and other minor services).

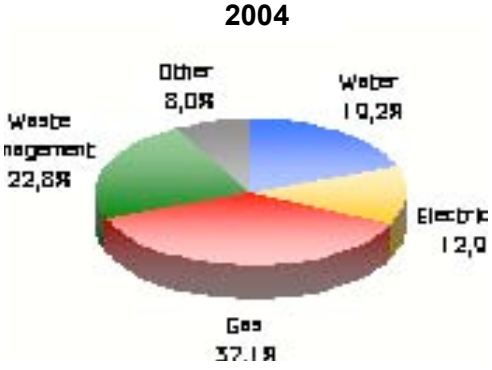
The business areas have basically not changed as a result of the integration of Meta, which operated within the same spheres: by contrast, the electricity area, in which the Modena-based company was leader in its province, emerges as greatly enhanced. Furthermore the Waste Management area has surpassed the Gas area in terms of importance on the EBITDA.

In order to provide more detailed information on the 2005 results, an analysis is shown of the business areas in which the Group operates. The composition and evolution for 2004-2005 in terms of Revenues and EBITDA are shown in the graphs below:

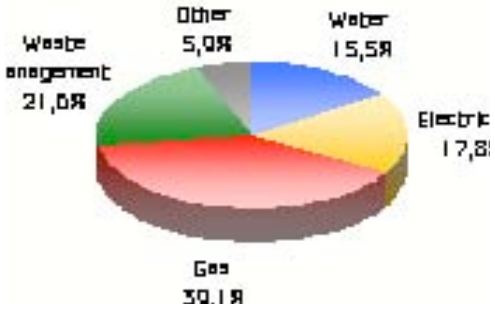
COMPOSITION OF THE BUSINESS PORTFOLIO

REVENU

2004



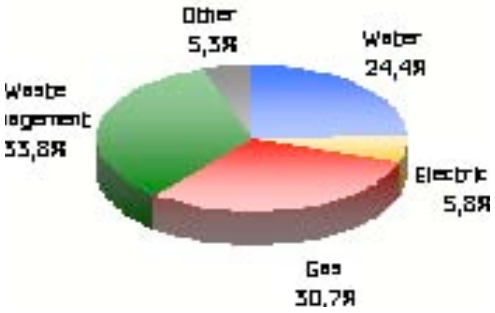
2005



EBITDA

2004

2005



The following sections contain an analysis of the operating results generated by business area. The income statements by business area include structural costs, including inter-divisional transactions valued at current market prices and, for 2005, are inclusive of the figures relating to the integrated Modena area.

It should also be noted that the analysis of the business areas includes the increases in construction on a time and materials basis/work in progress and, therefore, the related costs. This item, as envisaged in the indications of the IAS standards, is indicated by way of adjustment of the costs as costs capitalized in the individual tables.

Gas Area – Distribution and sales activities

Importance of the Gas business for the Group

The importance of the Gas business in 2005 decreased, in line with forecasts, by more than 5 percentage points in favour of the other areas of the Group's business, as a result of the lower profitability of the sector and the increase in the importance of the other areas, in particular that concerning Waste Management. This trend has confirmed the validity of the Hera multi-business model which makes it possible to offset any contrasting trends in the individual areas.

The importance of this business area with respect to total Group activities is illustrated below:

(mln/€)	31-dec-2004	31-dec-2005	Change	Change %
Ebitda	**106,0**	**118,4**	**+12,5**	**+11,8%**
Group Ebitda	292,5	386,4	+93,9	+32,1%
Percentage	*36,2%*	*30,7%*	*-5,6 p.p.*	

Results during the year in the Gas business

During 2005, this business area, involved in the distribution and sale of gas, was that which underwent the greatest changes when compared with last year. The main elements to be taken into account when evaluating the results are:

- the elevated increase in the cost of raw materials, deriving from the high level of oil prices, which caused heavy price tensions and greater attention towards consumption by customers: greater revenues were generated together with a consistent reduction in the percentage margins;
- the increase in the unit price (+ 20% on average), which encouraged and accentuated the commercial aggressiveness of competitors, in particular with regards to business customers and in the main metropolitan areas, involving a contained loss in margins;
- the favourable climate trend during the last two months of 2005 when led to sales rising by more than 10% in volume on the same period last year;
- the measures of the Authority for Electricity and Gas on distribution which, as illustrated in the related section, established an important reduction of the tariffs thereby causing a corresponding loss in margins;
- the intense trading and import activities carried out by the Group which made it possible to partially offset the lower sales margins on the end market.

The results are summarized below:

Income statement (mln/€)	**31-dec-2004**	**Incr.%**	**31-dec-2005**	**Incr.%**	**Change**	**Change %**
Revenues	589,8		871,2		+281,4	+47,7%
Operating costs	(466,2)	-79,1%	(733,5)	-84,2%	-267,2	+57,3%
Personnel costs	(35,0)	-5,9%	(43,5)	-5,0%	-8,5	+24,4%
Capitalized costs	17,4	3,0%	24,3	2,8%	+6,8	+39,1%
Ebitda	**106,0**	**18,0%**	**118,4**	**13,6%**	**+12,5**	**+11,8%**

Revenues in the Gas area rose by 47.7%, passing from Euro 589.8 million to Euro 871.2 million, essentially in relation to the consolidation of activities in the Modena Gas area (for around Euro 115 million), the rise in the cost of raw materials, transferred onto the sale price, and the increase in the volumes sold (for a total of around Euro 130 million), and greater trading activities which contributed by approximately Euro 50 million.

The change in revenues was also effected by the negative change in distribution tariffs, which fell on average by 10%, passing from 5.9 to 5.3 €/cents on average per cubic metre, involving an overall impact of more than Euro 11 million.

Compared with the previous year, the Group reported an increase of 25.5% in volumes distributed, which rose from 1,912 to 2,399 million cubic metres, and an increase in those traded for sale of 35.1%, from 2,062 to 2,786 million cubic metres, as shown in the table below:

Quantitative data	**31-dec-2004**	**31-dec-2005**	**Change**	**Change %**
Number of customers (thousand units)	798,6	939,6	+141,0	+17,7%
Distribuited volumes (million of cm)	1.912,0	2.399,1	+487,1	+25,5%
Volumes sold (million of cm)	2.062,0	2.786,3	+724,3	+35,1%
- of which trading	*176,0*	*447,6*	*+271,6*	*+154,3%*

It should be emphasised that the increase in volumes traded is equally distributed between growth on the internal market and growth of the areas associated with the integration of the Modena area.

The number of customers served reached almost 940 thousand units; the trend is illustrated in the following table:

31 Dec. 2004	Customers lost	Inherent growth	Modena	31 Dec. 2005
798.6	-16.7	+10.6	+147.1	939.6

(Customer No. in thousands)

The EBITDA rose from Euro 106.0 million to Euro 118.4 million (+ 11.8%), involving a decreasing percentage-based incidence of 4.4 percentage points, passing from 18.0% in 2004 to 13.6% in 2005.

Electricity Area – Distribution and sales activities

Importance of the Electricity business for the Group

(mln/€)	31-dec-2004	31-dec-2005	Change	Change %
Ebitda	**7,3**	**22,5**	**+15,2**	**+207,0%**
Group Ebitda	292,5	386,4	+93,9	+32,1%
Percentage	*2,5%*	*5,8%*	*+3,3 p.p.*	

The Electricity area is a sector considered to be strategic by the Group, since it makes it possible to complement and defend the sale of gas to customers in the area the Group operates in; with the Modena integration, these activities, besides more than doubling their percentage-related importance, were further enhanced in March 2006, by means of the acquisition of the former Enel network in the Province of Modena

Results during the year in the Electricity business

The increase in all the income statement figures indicated below, is mainly the consequence of the integration of the Modena-based company:

Income statement (mln/€)	31-dec-2004	Incr.%	31-dec-2005	Incr.%	Change	Change %
Revenues	205,0		396,7		+191,7	+93,5%
Operating costs	(198,2)	-96,7%	(369,6)	-93,2%	-171,4	+86,5%
Personnel costs	(2,7)	-1,3%	(9,2)	-2,3%	-6,5	+236,5%
Capitalized costs	3,3	1,6%	4,6	1,2%	+1,3	+38,0%
Ebitda	**7,3**	**3,6%**	**22,5**	**5,7%**	**+15,2**	**+207,0%**

The revenues in the Electricity area increased by 93.5%, passing from Euro 205.0 million to Euro 396.7 million: more than 80% of this increase is due to the Modena areas which also comprises distribution activities, while the remaining portion is linked to the rise in the price of the raw material.

The breakdown of the revenues by type of customer is shown as follows:

(million of euro)	31-dec-2004	Incr.%	31-dec-2005	Incr.%	Change	Change %
Revenues from non-elegible customers/distribution	25,7	12,5%	95,8	24,2%	+70,1	+272,9%
Revenues from elegible customers	176,0	85,9%	296,4	74,7%	+120,4	+68,4%
Other	3,3	1,6%	4,5	1,1%	+1,2	+36,5%
Total revenues	***205,0***	***100,0%***	***396,7***	***100,0%***	***+191,7***	***+93,5%***

By contrast, the table below summarizes the main quantitative indicators of the electricity sector:

Quantitative data	31-dec-2004	31-dec-2005	Change	Change %
Number of customers (thou. units)	**53,8**	**177,5**	**+123,7**	**+230,1%**
of which non-elegible/only distribution	49,7	165,8	+116,2	+233,8%
of which elegible	4,1	11,6	+7,5	+185,3%
Volumes sold (Gw/h)	**2.282,0**	**3.754,8**	**+1.472,8**	**+64,5%**
Non-elegible customers	196,0	720,1	+524,1	+267,4%
Elegible customers	2.086,0	3.034,7	+948,7	+45,5%

On a similar basis to the Gas sector, the electricity distribution tariffs, regulated by the AEEG, underwent a reduction of 2.5% on average during 2005 when compared with the previous year, passing from 1.866 to 1.820 €/cents per Kw/h. Throughout the entire Group network, the average distribution tariffs came to 1.898 €/cents per Kw/h with the integration of Modena.

The trend in raw material prices caused an increase in the prices of the liberalized market by nearly 25%, while the increase was lower by around 3 percentage points on the restricted market.

The EBITDA rose from Euro 7.3 million to Euro 22.5 million (+ 207%), involving a percentage-based increase of 2.1 points, passing from 3.6% in 2004 to 5.7% in 2005. The growth in absolute terms derives from the integration of the Modena area, which contributed by around Euro 13 million, and from internal growth, which contributed by around Euro 2 million.

Integrated Water Cycle Area

Importance of the Integrated Water Cycle business for the Group

(mln/€)	31-dec-2004	31-dec-2005	Change	Change %
Ebitda	**76,5**	**94,3**	**+17,8**	**+23,2%**
Group Ebitda	292,5	386,4	+93,9	+32,1%
Percentage	*26,2%*	*24,4%*	*-1,8 p.p.*	

By means of the integration of the Modena area, the Group currently operates in the Integrated Water Cycle management sector in 170 municipalities with more than 2.3 million inhabitants, linked up to a network of approximately 24 thousand km and with more or less complete coverage of the area in question.

Hera operates in 6 ATOs coinciding with the Provinces of Ravenna, Ferrara, Forlì-Cesena, Rimini, Modena and Bologna.

Conventions were set up with all the afore-mentioned Agencies, regulating the Integrated Water Service and guaranteeing the Group not only the extension of the concessions on average until 2022, but also the certainty of the tariff development until the end of 2007 and the guarantee of achieving the anticipated return on investment, in accordance with the provisions of the so-called Galli law, when fully up and running as from 2008.

Results during the year in the Integrated Water Cycle business

An analysis of the operating results achieved in the Integrated Water Cycle business is shown below.

P&L account (mln/€)	31-dec-2004	Incr.%	31-dec-2005	Incr.%	Change	Change %
Revenues	304,9		346,2		+41,3	+13,5%
Operating costs	(225,7)	-74,0%	(263,2)	-76,0%	-37,5	+16,6%
Personnel costs	(65,7)	-21,5%	(75,4)	-21,8%	-9,7	+14,8%
Capitalized costs	63,0	20,7%	86,7	25,0%	+23,6	+37,5%
Ebitda	**76,5**	**25,1%**	**94,3**	**27,2%**	**+17,8**	**+23,2%**

During 2005, revenues were generated for a total of Euro 346.2 million, compared with Euro 304.9 million in the previous year, up by 13.5%. Nearly two thirds of this increase is due to the Modena integration whilst the remaining part, equally distributed, concerns the rise in tariffs and the increase in services provided.

The following table summarizes the main quantitative figures of the business area:

Quantitative data	31-dec-2004	31-dec-2005	Change	Change %
Number of customers (thousand units)	800,1	914,0	113,9	+14,2%
Volumes sold (million of cm)				
acqueduct	203,0	228,4	25,4	+12,5%
Sewerage	155,0	199,7	44,7	+28,9%
depuration	181,0	205,8	24,8	+13,7%

Customers in the water cycle sector exceed 900 thousand units, mainly thanks to the contribution from Modena.

The average unit tariff of the integrated water cycle came to 1.29 € per cubic metre.

As far as volumes were concerned, growth was high in all the sectors, also in this case mainly in relation to the inclusion of Modena within the operating area. Without taking into account these volumes, aqueduct activities underwent a slight decrease (- 1%), purification was more or less stable (+ 0.4%), whilst sewerage activities increased by 13.3%. The greater growth of this last indicator reflects the acquisition of sewerage services in 11 new municipalities in the Bologna area, consequently involving the implementation of conventions with the area agencies.

In relation to the trend in volumes of water distributed by the aqueduct network, shareholders are reminded that 2005 experienced an extremely rainy Summer which particularly penalized the areas with high tourist flows. The impact of this climatic trend meant that more than 3 million cubic metres less were sold.

The 16.6% increase in operating costs, rising from Euro 225.7 million to Euro 263.2 million, is linked to both the afore-mentioned consolidation of the Modena water sector (which contributes by around 50%) and the rise in both services managed, particularly in the sewerage area, and in work capitalized, which increased by more than 35% on the original area of the Group. During 2005, a considerable increase was also noted in the cost of the electricity required for the water cycle's operating activities.

The EBITDA increased when compared to 2004 by 23.2%, from Euro 76.5 million to Euro 94.3 million, involving margins which rose by more than one percentage point, passing from 25.1% to 27.2% in 2005. The marginal nature is without doubt influenced by the contribution of the Modena area, whose contribution in absolute value came to around Euro 12 million.

Waste Management Area

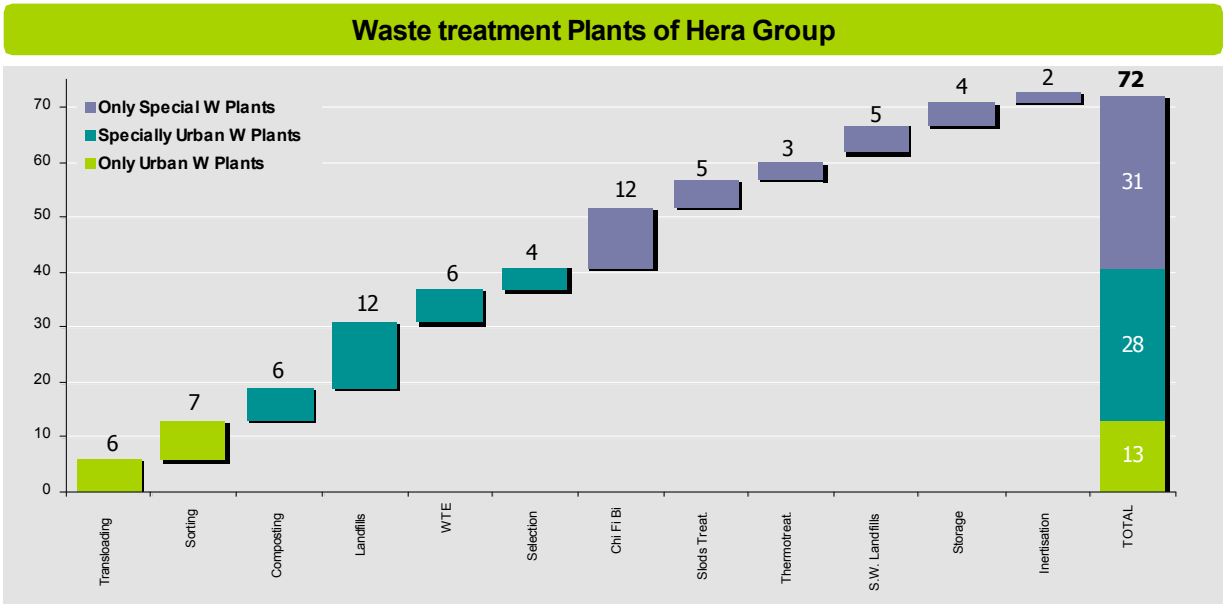
Importance of the Waste Management business for the Group

(mln/€)	31-dec-2004	31-dec-2005	Change	Change %
Ebitda	**85,7**	**130,6**	**+44,8**	**+52,3%**
Group Ebitda	292,5	386,4	+93,9	+32,1%
Percentage	*29,3%*	*33,8%*	*+4,5 p.p.*	

Partly thanks to the contribution of the Modena area, the Waste Management business was the sector which presented the highest levels of growth in 2005, so much so that it became the most important area with regards to the contribution to the overall EBITDA.

The Hera Group proves itself to be one of the most important integrated operators in the sector at European level due to its range of treatment and disposal plants for urban and special waste, and in 2005 it benefited from the full operations of Ravenna's Centro Ecologico plants and the coming onto stream of the new waste-to-energy plant at Bologna.

The graph below shows the Group's plants by type:



As already indicated in the Water Cycle Area, the Group operates within the sphere of the six ATOs of the Provinces of Ravenna, Forlì-Cesena, Rimini, Bologna, Modena and Ferrara. Conventions are active with all the Agencies, regulating the Waste Management Service and guaranteeing the Group not only the extension of the concessions on average until 2012, but also the certainty of the tariff development until the end of 2007 and the guarantee of achieving full application of the tariff system as from 2008, in accordance with the provisions of the Ronchi decree.

The activities performed in the waste management sector are considered strategic for the future development of the Group. In particular, the industrial plan contains important investments for the further strengthening of the waste-to-energy plant capacity, an activity that, in addition to minimising environmental impact on treatment, permits the production of electricity sold at subsidised tariffs (CIP6 and Green Certificates).

Results of the waste management business

Analysis of the results of operations in the Waste Management area is presented below:

Income statement (mln/€)	31-dec-2004	Incr.%	31-dec-2005	Incr.%	Change	Change %
Revenues	362,3		481,7		+119,4	+33,0%
Operating costs	(189,9)	-52,4%	(241,2)	-50,1%	-51,3	+27,0%
Personnel costs	(86,7)	-23,9%	(116,1)	-24,1%	-29,4	+34,0%
Capitalized costs	-	0,0%	6,1	1,3%	+6,1	+0,0%
Ebitda	**85,7**	**23,7%**	**130,6**	**27,1%**	**+44,8**	**+52,3%**

Revenues in the Waste Management area rose from Euro 362.6 to Euro 481.7 million (+ Euro 119.4 million), disclosing an increase of 33.0%. This increase is principally due to three factors:

- the consolidation of the corresponding Modena sector, which lead to an increase of around Euro 65 million;
- the bringing onto stream of the waste-to-energy plant at Bologna and the operations of the Centro Ecologico in Ravenna for the entire year, which contributed by around Euro 37 million;
- the rise in volumes and services by approximately Euro 13 million and the tariff increases for around Euro 5 million.

In relation to operating costs, shareholders are informed that the increase in the quantities treated and the improved plant endowment made it possible to better the management efficiency, involving an increase in this item which was lower than that of the revenues (+ 27.0% compared with + 33.0%).

The volumes of urban waste collected rose by nearly 24% when compared with last year: without taking into consideration the Modena area, the increase came to 4%.

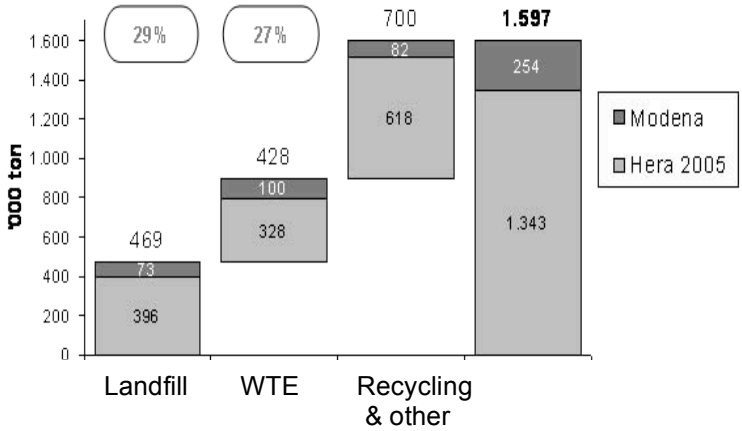
Differentiated waste collection in terms of percentage-based incidence on total volumes collected came to 29.1% (29.5% net of the Modena area), confirming the Group's commitment to increasing the fraction recoverable from waste and reducing the environmental impact.

The volume of urban waste treated in the Group's plants, including the portion from the Modena plants, shown in the table, rose during 2005 by nearly 33%.

Quantitative data	31-dec-2004		31-dec-2005		Change	Change %
Urban waste	1.316,0	49,2%	1.597,2	42,3%	+281,2	+21,4%
Special waste from market	1.360,0	50,8%	2.177,7	57,7%	+817,7	+60,1%
Waste treated in Group plants	**2.676,0**	**100,0%**	**3.774,9**	**100,0%**	**+1.098,9**	**+41,1%**

Once again in 2005, waste treated in landfills decreased in favour of waste-to-energy plants, confirming the Group's strategies which show preference for plants which have a lower environmental impact. The following graph shows the breakdown of the portions disposed of per plant:

Urban Waste treatment breakdown



The portion of waste treated in the waste-to-energy plants increased, making it possible to contain the transfer of the same to landfills, further improving the handling of the waste also in environmental impact terms.

Quantitative data	31-dec-2004		31-dec-2005		Change	Change %
Landfills	919,0	34,3%	1.343,2	35,6%	+424,2	+46,2%
Waste to Energy plants	451,0	16,9%	614,0	16,3%	+163,0	+36,1%
Selection plants	579,0	21,6%	774,8	20,5%	+195,8	+33,8%
Compost plants	67,0	2,5%	300,5	8,0%	+233,5	+348,5%
Inert.chemical plants	660,0	24,7%	742,4	19,7%	+82,4	+12,5%
Waste treated in Group plants	**2.676,0**	**100,0%**	**3.774,9**	**100,0%**	**+1.098,9**	**+41,1%**

The EBITDA for 2005 rose from Euro 85.7 million to Euro 130.6 million (+ 44.8%), involving an increase of 52.3%. Shareholders should note that there was also an increase in the percentage-related marginality from 23.6% to 27.0% made possible by the improved output of the plants and an improved handling of the waste treated. In the Waste Management business area, Modena's contribution towards the increase in EBITDA in absolute terms was limited to a third of the total.

Other Services Area

Importance of the Other Services for the Group

(mln/€)	31-dec-2004	31-dec-2005	Change	Change %
Ebitda	**16,9**	**20,6**	**+3,7**	**+21,7%**
Group Ebitda	292,5	386,4	+93,9	+32,1%
Percentage	*5,8%*	*5,3%*	*-0,5 p.p.*	

During 2005, the Other Services area changed considerably in relation to the progressive reorganisation of the services which are not strategic for the Group: by way of example, during the year just ended, cemetery services where sold off in most areas and the more minor services concerning disinfestation and the management of public parks decreased consistently.

Results of the Other Services Area

The results are summarized in the table below:

Income statement (mln/€)	31-dec-2004	Incr.%	31-dec-2005	Incr.%	Change	Change %
Revenues	126,8		130,8		+4,0	+3,2%
Operating costs	(110,9)	-87,5%	(107,0)	-81,8%	+3,9	-3,5%
Personnel costs	(25,8)	-20,3%	(25,8)	-19,8%	-0,1	+0,3%
Capitalized costs	26,8	21,1%	22,6	17,3%	-4,2	-15,5%
Ebitda	**16,9**	**13,4%**	**20,6**	**15,7%**	**+3,7**	**+21,7%**

The rise in the Area's revenues, from Euro 126.8 million to Euro 130.8 million, is linked to two opposing factors: the integration of the corresponding Modena sector (+ Euro 15 million) and the decrease of the old area of consolidation (- Euro 11 million) in relation to the afore-mentioned disposals.

The EBITDA trend, having risen from Euro 16.9 million to Euro 20.6 million (+ Euro 3.7 million), disclosing an increase of 21.7% and with a percentage-based marginality up by more than two points, from 13.4% to 15.7%, confirms the excellence of the Group's decision to concentrate on specific areas of activities which are complementary to the core business.

Shareholders are informed that, in this business area the Modena company performed activities almost exclusively within the sphere of public lighting which presents the greatest marginality, also within the old area of consolidation of Hera.

The following table analyzes the main quantitative data concerning the Other Services Area:

Quantitative data	31-dec-2004	31-dec-2005	Change	Change %
District Heating				
Heat volumes distribuited (Gwht)	434,0		(434,0)	-100,0%
Public Lighting				
Light tower (thousand)	249,0	293,2	44,2	+17,8%
Municipalities served	51	58	7,0	+13,7%

Shareholders are informed that as far as the district heating area is concerned, the increase net of the contribution from the Modena area would come to around 2% thanks above all else to the more favourable climate trend.

In the public lighting sector, it should be pointed out that the contribution originating from the Modena area totalled 35 thousand lighting units, while the other 9 thousand derive from the new municipalities acquired within the Group's original scope of consolidation.

2.01.03 Commercial Policy and Customer Care

The Hera Group set the following commercial objectives for 2005:

- standardising customer approach systems throughout the territory
- integrating the Ferrara customers in the commercial strategy and preparing for integration of the Modena customers
- commercially exploiting the renewal of the IT systems
- consolidating the system of offer and sales to business customers
- organising a solid and reliable control system
- completing the quality certification process with inclusion of the subsidiary companies, in particular Hera Comm
- organising commercial planning in compliance with market targets

In particular during the first year-half two customer satisfaction surveys were carried out, one on the residential market and one on the business market, aimed at identifying the quality components and processes that have greater impact on satisfaction and subsequently highlighting the operating priorities of Hera. The quality perceived was measured on four fundamental services provided by the Group, environmental hygiene, water, gas, and electricity, and on the customer contact and management channels.
Satisfaction levels were generally found to be good, even if some qualitative differences were observed between territories, which proves that although Hera is now perceived as a group, the level of service is not yet uniform.
Hence during the year a system of procedures for call centre and branch operators was set up which standardised tariffs, procedures and instruments for the management of contacts with the customers using the new Siebel system as base.
During 2005 while competition on the residential gas market was keen it did not create particular problems for the Group, as it lost only 16,770 customers with a total annual consumption of 18.4m m^3, out of a total as at 31.12.2005 of 936,600 customers with a total consumption of 2.3m m^3.
During the year various commercial notices were sent to customers explaining the functioning of the gas chain and the role played by Hera Comm and promoting specific customer loyalty ventures.

2005 also saw the start up of the new SAP ISU information systems at Bologna, Ravenna and Forlì-Cesena. This caused a strong increase in the workload for the call centre and branches, but also raised customer awareness on billing and payments, particularly in the Bologna area. At first service levels were affected, but they quickly returned to normal levels, following the upgrading of the call centre hardware and the reorganisation of some branches.

The Ferrara customers were integrated into the Group's commercial policies and the procedures for call centre and branch operators were standardised as were the customers notices.

On the Business market (large customers) the first year-half saw the launch of dual fuel sales (gas and electricity) through the indirect channels, with master agreements being executed with approximately 30 territorial associations, while the direct channel sales campaign has almost

concluded. Condominiums that were lost during 2004 were also recovered. Important dual fuel supply contracts were also signed outside the territory managed by Hera.
On the business market 300 customers, with a total annual consumption of 10.6 m. m^3, were lost in 2005, but others were acquired "outside the net" for a total consumption of 41m m^3.
In the second half of the year loyalty programmes aimed at "corporate" clients and condominiums were launched. In the condominium segment, in particular, 33 customers lost in previous years were recovered, for a total annual consumption of 2.3m m^3, against customers lost in the year for 0.6m m^3.
For the year-end sales campaign a new offer system was set up, which provides customers with a range of offers that vary according to individual requirements, backed up by new reporting material and new contractual documentations for indirect sales. In particular, the "Future dual" dual fuel offer was designed with standardised forms and contracts for electricity and gas.

Electricity sales closed the year 2005 slightly up on 2004.
Furthermore, an electricity consumption forecast instrument was created for the energy exchange and contracts for precise customer metering were signed. This allowed the Group to market the consumption visualisation web service.

In October the new segmentation of the Hera customer base was formally implemented, which led to the rearrangement of organisational structures and to the creation of structures responsible for the full management cycle of pertinent customers. In particular the Business customers will be managed by the Business Customers and Top Customer structure of Hera Comm and the residential customers by the Mass Market customer structure of Hera Comm, which will coordinate the pertinent commercial activities of the Local Operating Companies.

In September Hera Comm gained its first ISO 9001 certification, as independent company. The management of customer contacts was subjected to particularly in-depth analysis and the procedures and systems were found to be in compliance and appropriate.

2.01.04 Trading and Procurement Policy

Business Analysis – reference scenario

2005 saw the global economy continue the expansion phase which began in 2003, even if the pace differed from one part of the world to another. Indeed all the major economic areas recorded GDP growth rates which were more or less constant, while once again it was largely due to the vivacity of economic activity in the United States and in Asia that international recovery continued at a strong pace.

The growth rate in the Euro area continues to sustain decidedly modest levels, especially if compared to the growth rates of the American and Asian economies (1.4% of the Euro area against the 3.6% forecast for the United States, the 9.3% for China and the 4.6% for the Pacific countries). However the third quarter 2005 witnessed an unexpected acceleration in GDP which concerned all the components of domestic demand and, especially, the growth of investments. In spite of this, a certain degree of uncertainty still surrounds future trends in domestic demand and so it is not possible to foresee a virtuous cycle being triggered within the area.

As far as exchange rates are concerned, 2005 witnessed a further strengthening of the dollar, which experienced a 12.5% appreciation, after having risen as high as 1.35 USD per Euro at the beginning of the year before coming back down to 1.18 USD at the end of December 2005. After a few months of substantial stability, with a €/$ exchange rate in the region of 1.20-1.23 USD per Euro in the months of June-July and an exchange rate in the region of 1.23-1.25 USD per Euro in the months of August-September, the dollar rapidly fell below the 1.20 mark, reaching as low at 1.17 dollars mid-November. The progressive strengthening of the dollar is attributable to various factors amongst which a differential in the reference rates between the EU and the US of 175 basic points (4% fixed by the FED against the 2.25% fixed by the ECB), the different growth prospects, the tax benefits on capital inflow from which the American companies benefited up to the end of 2005.

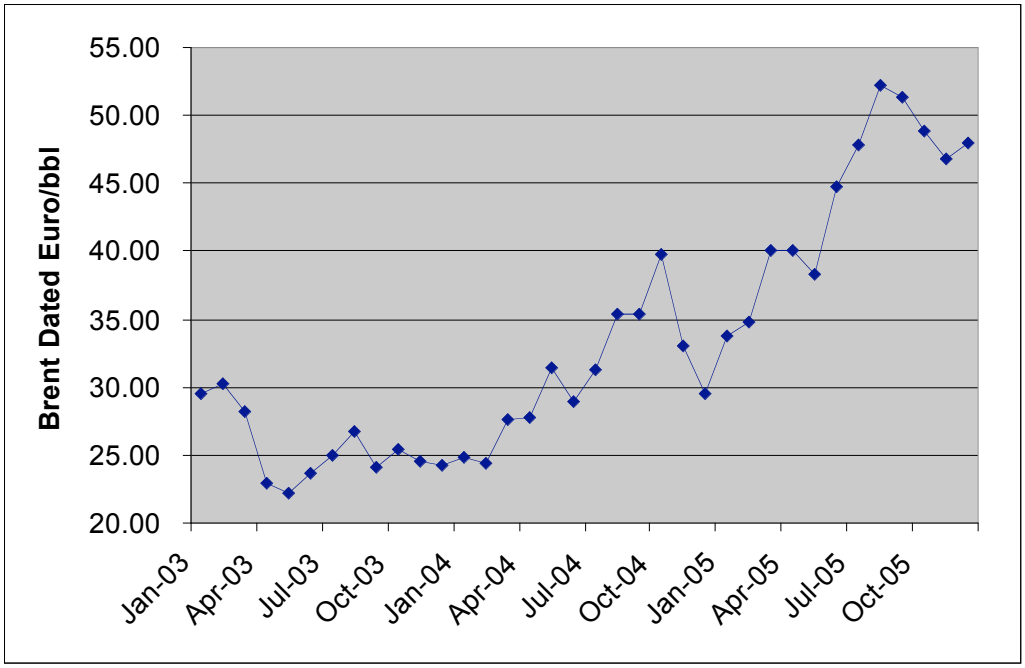
On the inflation front, despite the fact that the price of oil stayed above the 60 dollars/barrel mark, no particular acceleration of inflation was recorded on the end markets. The European Central Bank did however take precautions contrasting any inflationary fears with a modest 25 basic points increase of the reference interest rate. As far as the USA is concerned, this remains the country with the highest risk of inflation from costs: the tendential rate of year-end stands at 3.5%, well above the 2.2% of the Euro area and the 2% of Italy.

Reference Scenario

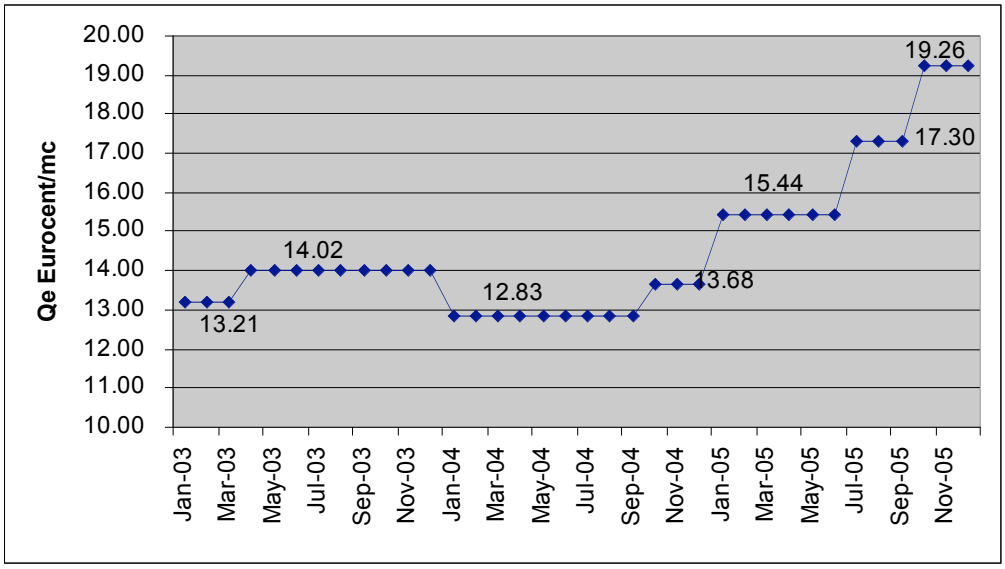
	2005	2004	% variation
$/bbl oil price	54.4	38.2	42.3%
Euro/$ exchange rate	1.24	1.24	-
Euro/bbl oil price	43.7	30.7	42.1%

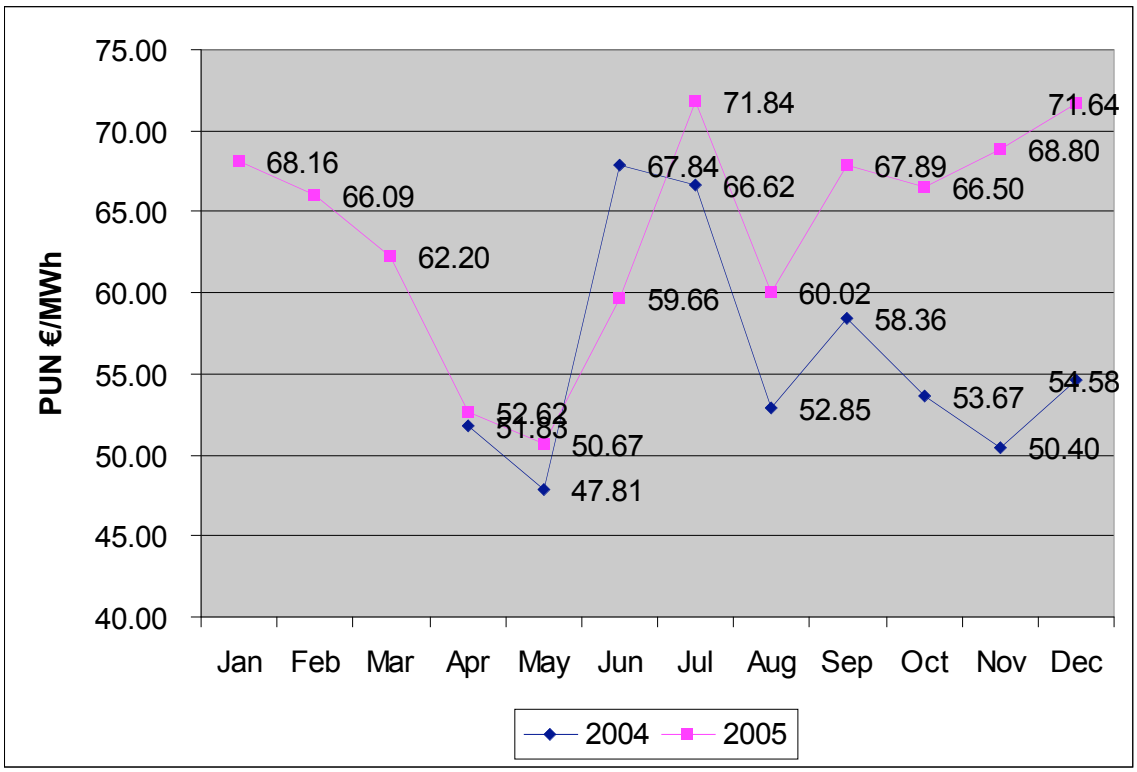
As far as the oil market is concerned, the average Brent price in 2005 was 54.4 dollars a barrel, posting a +42.3% compared to the 2004 average (38.2 dollars a barrel). In 2005 crude oil touched record highs since 1979, reaching a monthly average of almost 64$/barrel in August and almost 63$/barrel in September. Due to the effect of the relative weight of the Euro on the US Dollar calculated on the annual average, the price increase of Brent in Euro was practically the same (+42.1%). In 2005 crude oil price trends took on a structural pattern; experts expect to see a slight drop in prices next year.

The tension in black gold prices is attributable to a series of factors which have profoundly changed the structure of the world oil market, first and foremost the sharp upsurge in consumption (due to China and the other Asian countries, as well as the US) in the face of deficiencies in the additional production capacity and in refining. Secondly, factors of a geopolitical nature have contributed to the belief that the world's crude oil industry no longer has the same capacity to meet the pressures of demand, amongst which the prolonging of the serious situation in Iraq and the problems which have affected producing countries such as Venezuela and Nigeria.



Against this backdrop, as far as gas is concerned, the average value of the QE was equal to 16.858 in 2005, compared to an average value of 13.040 in 2004 and an expected value of 23.770 in 2006. As it is possible to infer from these figures, the full effect of the sharp rise in the price of oil recorded during 2005, has yet to work its way through to gas prices and is destined to have major repercussions through 2006. This is naturally due to the effect of the delays associated with the formulas for updating gas prices.





As far as electricity is concerned, the average exchange sales price (PUN) was equal to 64.00 €/MWh in 2005, which was higher than the previous year.

In 2004, the tariffs established by AEEG equal to an average of 57.34 €/MWh remained in force until March and from April the electricity exchange was launched with an average PUN in 2004 equal to 56.18 €/MWh.

The increase in energy prices in 2005 compared to 2004 was particularly apparent in the second half of the year, the period in which the most notable increases in oil prices were recorded.

GAS DIVISION

As in 2004, the reference scenario for 2005 suffered the effects of a particularly tight market situation due to the limited capacity available for "new operators" on the methane pipelines interconnecting with overseas procurement sources. This situation is destined to continue in the short/medium-term period, at least until the new infrastructures will start operations (upgrading of the TAG and TTPC methane pipelines, the GNL terminals and the GALSI methane pipelines).

In May 2005, the company TTPC (ENI Group), with view to improving ENI's position with regard to the proceedings implemented by the Italian Anti-Trust Authority (ACGM) to investigate whether it had abused its dominant position, implemented a procedure of non-discriminatory allocation of the capacity relating to the first lot of the upgrading of the TTPC methane pipeline (approximately 3.5 BN m^3/year), said capacity to be available as from 1 October 2008.

Participation in this procedure on the part of all the operators, Hera Trading included, essentially proved futile, given that SONOTRACH deemed the preliminary contracts previously signed with EDISON (from 0.7 to 4 BN m^3/p.a.), BRIDAS (0.5 BN m^3/p.a.), COMPAGNIA ITALIANA DEL GAS (0.5 BN m^3/p.a.), WORLDENERGY (0.1 BN m^3/p.a.) during an earlier procedure implemented in 2002 by TTPC in a non-publicised manner and subsequently annulled by TTPC itself, to be valid.

In short, allocation of the capacity relating to the upgrade, effected on the basis of the new non-discriminatory procedure, gave rise to the same outcome as the previously annulled procedure insofar as the only operators able to document the availability of gas proved to be the four which had negotiated the preliminary contracts with SONATRACH during the first procedure.

With the same intention as above, in November 2005, the Company TAG (ENI Group) implemented a similar non-discriminatory procedure for allocation of capacity on a twenty-year basis, with effect from 1 October 2008, for a quantity equal to approximately 3.5 BN m^3/p.a.

Significant Events

With regard to the gas division, the year 2005 clearly highlighted the problems associated with the limited capacity of operative storage and the equally limited capacity of transportation available on the pipeline interconnecting the Italian system with the procurement areas.

As far as storage is concerned, the late cold spell recorded at the end of February/early March 2005, forced the system to make use of the strategic storage to the extent of approximately 800 million m^3.

Hera Trading was also obliged to use strategic storage for 3 days in the month of March and for a volume of 0.9 million m^3, which were however restored in the next 2 days of the same month.

With regard to the limited transportation capacity, the auctions conducted by ENI-CH on Transitgas with "rising" modality, produced transport prices that were 400% higher than the auction base,

which Hera Trading deemed to be unsustainable and hence abstained from executing new contracts for the gas year 2005/2006.

ELECTRICITY

Legislative/Regulatory Framework

2005 was undoubtedly a watershed year for the electricity sector as it witnessed the Electricity Exchange enter into full effect (both offer and demand side).
The full start-up of the Exchange and the abandoning of the old trading contracts increased the complexity of the operators' activity as they had to balance hour by hour rather than by time-band/month, as in 2004, or even by time-band/quarter as in 2003.
The training initiatives and the development/acquisition of the necessary instruments implemented as early as 2004 proved appropriate and allowed Hera Trading to be fully operative right from 1 January 2005.

Significant Events

The full launch of the Electricity Exchange with effect from 2005 allowed more accurate definition of Hera Trading's operating activity which features the activity of "physical" management of the purchase portfolio to cover the sales of Hera Comm, but also the management of a further purchases/sales portfolio targeted at the wholesale market, which is more orientated towards this type of "financial" activity.
In particular, within this second portfolio, the contracts for differences (CDF) with ATEL and Acquirente Unico (AU) were managed.
During the year, with a view to maximising the economic value of the portfolio import capacity, the opportunities arising from the disalignment of prices which occurred in the Italian and French exchanges were exploited with activation of arbitrage transactions.
In December 2005 negotiations were concluded with EGL (Toller) for the contract of supply to Hera Trading of the electricity from the Sparanise power station.

RISK MANAGEMENT

As part of its trading activities Hera Trading is exposed to fluctuating energy prices and exchange risk given the potentially different sale and purchase prices of gas and electricity. The current exposure to other financial risks (counter-party risk, liquidity risk, etc.) is negligible. The objective of Hera Trading is, in fact, to limit volatility risk to the margins foreseen in the budget that are, after all, those dictated by reference market regulations (for example, CIP 6 and transport costs). For this reason several derivative contracts have been stipulated in order to synthetically align the index formulas of the sales prices:

- to the indexing formulas of supply prices when dealing with supply at indexed prices;
- to the fixed prices when these sales are supplied at fixed prices.

Additionally, in terms of electric energy, in order to reduce exposure to the PUN price generated by the ATEL contract, as agreed upon in the course of budget approval, Hera Trading decided to participate in the auctions held by the Acquirente Unico (a joint stock company set up by the Network Operator to assure competitive pricing in a liberalised market) where it successfully bid for 50 MW of oil product, deemed to the most opportune of the products up for auction.

The two differential contracts, even if not perfectly complementary in terms of quantity and price, were structured to be impacted differently by exchange price trends and that is what effectively took place.

2.01.05 Financial Policy and Rating

Once again in 2005 the Group pursued the customary financial policy directed at guaranteeing coverage of corporate requirements and characterised by utmost prudence, economy and balance between long and short term borrowings.
The performance of the financial markets and that of the raw materials used in energy production, which play a key role in the Group's business, made the management of working capital flows particularly delicate. The consistent increase in the costs of raw materials, while lessened by the strengthening of the euro against the dollar, caused a sharp increase in working capital sustained by an increase in short term borrowings. Account must also be taken of the fact that further temporary unbalance was caused by the gradual progress of the project for renewal of the customer system which led to some suspensions/slow-downs in the scheduled billing flow.
In order to further improve the long-term debt position and in view of the substantial investment plan scheduled in the 2005-2008 industrial plan approved in September (approximately Euro1.4 billion), in October 2005 a pool of leading banking institutes Banca IMI, Citigroup and JPMorgan, were commissioned to organise and issue a fixed rate Eurobond with ten year maturity for a maximum amount of Euro 500 million. This project was brought to a very successful conclusion on 16 February 2006.
The Bond was in fact issued for a maximum amount established in the face of a demand of over Euro 2.3 billion, with annual coupon equal to 4.125%.
The success of the financial policy adopted by the Group was rewarded by Standards & Poor's confirmation of the A+ rating on the long term, to which was added Moody's prestigious A1 rating.
Hera has undertaken to maintain

- a solid financial structure
- an adequate level between liquidity and available committed financing, capable of meeting each financial commitment for the next 12 months
- a defensive rather than speculative risk management policy relating to interest rates, currencies and raw materials.

As far as short term debt is concerned, significant savings and an increase in operative efficiency have been achieved.

2.01.06 Research and Development

Group orientation on the matter of research and development is represented by the necessity, on the one hand, to implement initiatives aimed at increasing plant efficiency, reducing physical losses, minimising risks of service management and limiting as much as possible the environmental impact, that is, developing activities that have a direct effect on the business. On the other hand, it also aims to encourage and orientate research on issues of particular interest to Hera, making use of qualified internal resources dedicated to research as well as the external technical-scientific collaboration of institutional bodies (Universities, Research Centres such as ENEA and CNR, other companies and public entities), including through partnerships or simple sponsorships.

Substantial resources have been invested in research with the aim of achieving the following objectives:

- • improving efficiency in management of the products/services offered: projects and studies are aimed at improving the quality and sustainability and increasing the availability of water and energy resources and reducing wastage;
- • preventing and reducing the environmental risks arising from operations;
- • reducing operating costs: by defining specific techniques for materials, services and works, it is possible to spread the use of best practices in management and maintenance of the networks; the common use of the corporate operative model selected by the Group allows for the creation of an internal benchmark which serves to promote tangible improvement of efficiency levels;
- • increasing the industrial margin through:
    - reduction of losses and disservices
    - expansion of volumes of services managed
    - optimisation of the tariff policy.

Major Research Projects carried out in 2005

Environmental Division

• CO_2 Project: launched in 2005, the project involves experimentation of an innovative technology for capturing CO_2 issuing from exhaust gas produced by any combustion process and its use in the process of anaerobic digestion of sewage sludge. The objectives are to:

- reduce CO_2 emissions;
- use the captured CO_2 to reduce the sludge contained in the of the operators of the purification plants;
- produce a greater quantity of methane gas;
- lay the foundations for Hera's future role as leader in innovative technologies for the limiting emissions.

Networks Division (Water and Energy)

• "Polluting Defence" Project: this project concerns the development and application of new instruments for remote monitoring of the quality of drinking and waste waters and gas emissions. The objective is to monitor in real time several important water and air quality parameters, reducing pollution risks and laboratory analysis costs. After the positive experience in on-line monitoring at the water treatment plant of Val di Setta (BO), in 2005 installation of a similar instrument began at the Ravenna plant, for the purpose of monitoring the efficiency of the water treatment processes.

• King Mida Project: "King Mida" is the name given to a series of research activities concerning the sector of energy recovery from sewage sludge, with the intention of effecting medium-long term experimentation of innovative technologies for the low cost disposal of sludge.

• MIG Project: consists of the creation of a fluid dynamics model for management of the water networks, with the aim of optimising the use of current and future aqueduct sources, in terms of:
1. reliability: placing the primary network in a position to guarantee the water volumes necessary to the population even in the event of serious difficulties, such as exceptional drought, or accidental pollution of a water resource;
2. costs: reallocating volumes between the various sources with the aim of optimising the total production cost;
3. quality: so as to guarantee pre-established quality levels, fully exploiting the available resources;
4. environment: limiting the levels taken from the natural water resources (e.g. from water tables).
The model has already been used to simulate strategic scenarios for increasing procurement of water resources. The project was concluded in 2005.

• MIT Project: "MIT" (Technical Hydraulic Model) means the development activity sector which uses the models of hydraulic simulation applied to the networks. This sector is complementary to the MIG sector. The aim of the "MIT" project is to spread the use of the mathematical models in the Local Operating Companies as modern management instrument.

• Ferrara Waters Project: this project involves a series of actions aimed at providing support to the management of the hydraulic network of Ferrara and surrounding countryside through cutting-edge technological solutions, such as mathematical simulation models and foresight models for the rehabilitation of water pipelines.

• Marecchia Project: this project consists in the performance of part of the activities pertaining to a complex study of the alluvial fan of the Marecchia river to aid sustainable management of water resources. Other parties involved in the project, which deal with other correlated study activities, include the Interregional Marecchia-Conca Basin Authority, the Emilia Romagna Region, the Province of Rimini, the Municipality of Rimini, the ATO of the Province of Rimini.

• X-water Project: experimentation of remote reading of waters applied to a pilot section of the distribution network. This project aims to provide indications on the applicability of remote reading to the recording of physical network leakage. By controlling the water balance in a particular section of the network, it is possible to precisely record the volumes of incoming water, that is

introduced to the network and outgoing water, that is, effectively used, and hence allow prompt intervention in the event of breakage and thereof water loss. The project will attempt to assess, through the analysis of more accurately recorded consumption trends, the behavioural patterns of consumers with respect to the resources and any tariff implications linked to said behaviour.
The data gathered has led to some interesting preliminary results in terms of control of water loss. Monitoring of the sample district shall terminate in 2006.

• Meters Project: the project, which was implemented in 2005, aims to analyse samples of the current pool of drinking water meters, in order to identify the best technology available on the market by which to increase the level of service to consumers.

• Fuel Cell Project: construction of plants for distributed production of electricity and heat through combustion cells fuelled by methane or hydrogen. The latter appear particularly suited to guaranteeing the supply of electricity in emergencies. In 2004 three hydrogen Fuel-Cell models were acquired and installed. In 2004 the project obtained funding from the Emilia Romagna Region within the context of the Regional Programme for Industrial Research, Innovation and Technological Transfer.
The initiative forms part of the endeavour to acquire know-how on the issue of alternative and renewable energy sources, in the event that, should the hydrogen market develop, the Group may take on an important role as supplier of raw material or of electricity or heat energy deriving from the transformation of methane into hydrogen.

Other Initiatives

SOV Project : this project began in 2002 and was characterised by intense operating activity in 2005. It concerns the research of volatile organic substances produced in the baking of ceramics and is being carried out in partnership with IPEG SpA, Smaltochimica Srl and Centro Ceramico. For Hera, the interest in the project lies above all in the identification of instruments and methods allowing automatic and continual control of volatile organic substances produced in various processes in the production cycles of Hera, in particular those relating to the treatment of waste.

As the project for "Control of the emission of Volatile Organic Substances (SOV), new systems for continuous monitoring of SOV in gas emissions", constitutes industrial research and pre-competitive development activity, it has been recognised as qualifying for the benefits of Law 46/82 and hence has been funded by the Minister of Productive Activities from the Fund for Technological Innovation (FIT). The research was concluded in 2005.

2.01.07 Human Resources and Organisation

As at 31 December 2005 the employees in the Hera Group totalled 5,904 with the following division by category: Senior Management (93), Managers (245), White-collar (2,458), Blue-collar (3,108). The following movements occurred in the year: new arrivals 90, acquisition of personnel from increased consolidation area 1,027, departures 236. It is noted that the new arrivals essentially related to the change in mix with the insertion of qualified personnel; finally it is noted that the total number of university graduates increased by 85 units (from 461 equal to a percentage of 9.18% of total employees engaged on an open-ended basis, to 546 equal to 9.55%).

Organisation
During 2005, in view of the complexity of the corporate structure and of the sizeable dimensions reached by the Hera Group, the essential organisational structure underwent redefinition. In practical terms:

- the General Management Division, the Local Operating Companies, the Networks, Research & Development, District Heating and Large Plant Engineering and Electricity Grid Coordination Divisions all report to the Managing Director, as do the Purchases and Tenders, Financial Administration and Control, Personnel and Organisation, Quality. Safety and Environment central staff units;

- the Environment, Sales and Marketing and Services Divisions report to the Chairman, as do the Business Development, Legal and Corporate Affairs, External Relations and Investor Relations central staff units;

- the Internal Auditing department reports to the Vice Chairman.

At the same time, in order to supervise the company's social responsibility the organisational position Corporate Social Responsibility, reporting to the Managing Director, was set up.

Furthermore, optimisation of the internal functioning processes continued, with implementation of the SAP-ISU IT system and consequent integration of the customer, activities and billing management processes in the territorial areas of Bologna, Ravenna and Forlì-Cesena, in addition to initiation of implementation of SAP-ISU for Business customers.

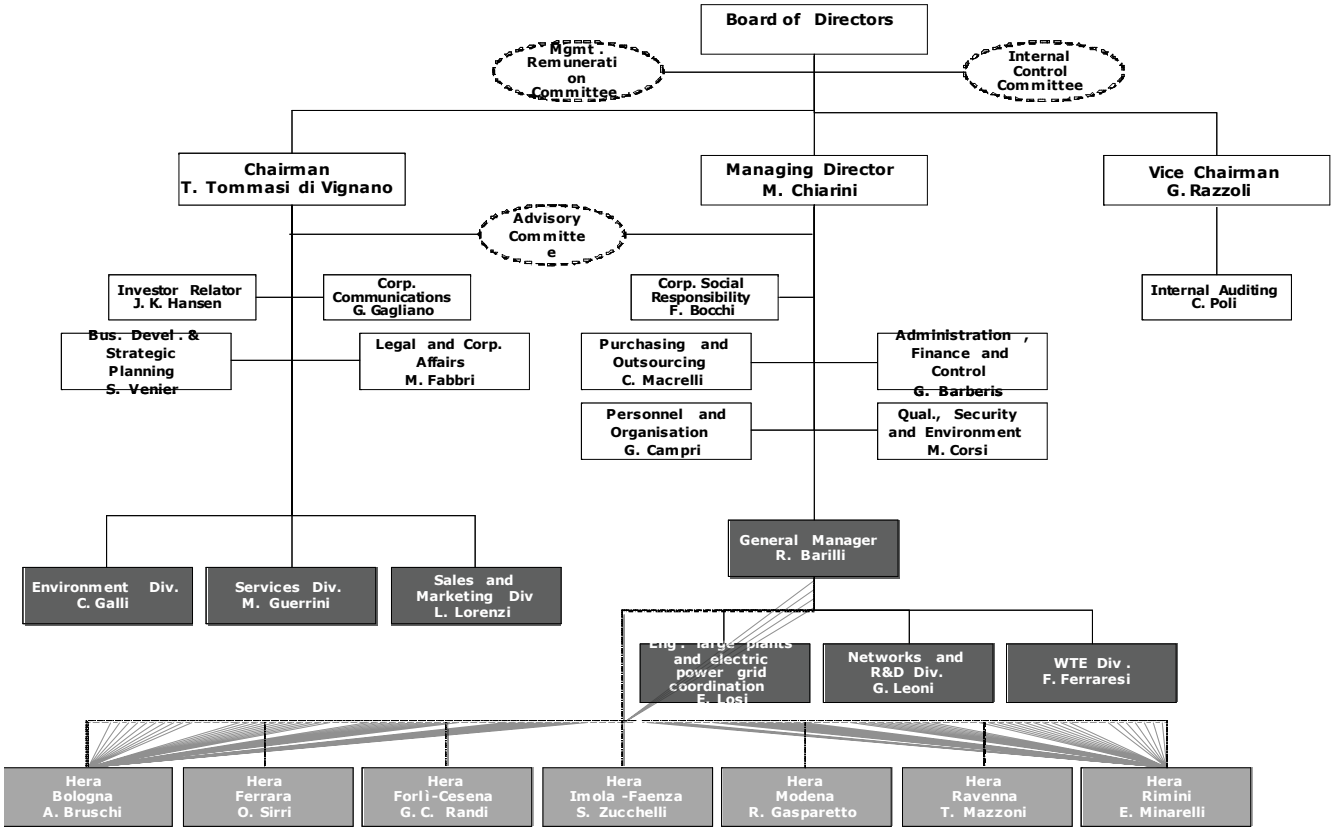
In order to minimise resistance to change caused by system changes, some specific support initiatives were implemented:
- organisation of events to notify and inform the "internal stakeholders" affected by the process changes (directors, department managers, coordinating personnel, trade union organisations, employees, etc.);
- development of IT and process skills, with the provision of over 423 training days and the involvement to date of approximately 1,347 people in 30 ad hoc training programmes.

2005 also saw the launch of the process of integration of the services managed in the territory of Modena and, consequently, the setting up of the Local Company of Hera Modena, which began operations on 1 January 2006, thus confirming the "open entrepreneurial formula" which distinguishes the Hera model.

At year-end 2005 Hera also decided to focus the Electricity Business by setting up a new dedicated Division, and also by planning and constructing large waste-to-energy plants, and by coordinating the Group's electricity grids.

Organisational Macrostructure

The chart below shows the Group's organisational macrostructure, inclusive of the integration of Meta:



Industrial Relations

Trade union activity was largely centred on issues relating to correct allocation, in accordance with Group organisation, of the activities of the former Agea and Acosea companies within subsidiaries companies such as Hera Comm, Famula, Hera Luce and Uniflotte. Important trade union agreements were reached for the purpose of harmonisation of regulatory and economic treatments on the Ferrara and Ravenna territories. At end of September discussion began on a trade union platform containing substantial and important issues. Among these attention is drawn to the following issues, which were also desired and requested by the company: definition of a performance bonus constructed on a single system for both objectives and economic items, definition of the field of application of the various CLA in force in the Group, harmonisation of the economic treatments ensuring from second level negotiations. The trade union negotiations are still underway and it is believed that a conclusion may be reached in the early months of the year.

Training

In addition to accompanying the integration processes underway and to meeting the Group's needs, the primary aim of the training activities implemented during 2005 was also to develop the professional experience present at various levels and to enhance know-how and distinctive skills.
During 2005 103,113 man/hours of training were provided for a total of over 11,800 participations. 4,230 employees (more than 83% of the company roll) were involved in training activities.
On the whole the activity implemented, whether training or professional refresher courses for employees, formed part of several lines of intervention. In addition to intense training activity on the issues of quality, environmental management systems and industrial safety (not only in compliance with provisions of the law), the principle initiatives concerned:

- the launch of the School of Trades aimed at enhancing the specific technical-operative skills of the Hera Group
- update and development of technical-specialist skills
- institutional training to support insertion of resources engaged under the Graduates Project.

The first year-half 2005 also saw completion of a series of training programmes initiated in 2004 (encounters with white and blue collar workers to spread awareness of values and mission, days for senior managers, managers, executives dedicated to the development of collaborators and to communication techniques, specific encounters on the issue of planning and control of managerial activity).
Significant investment continued to be made in support of the implementation of the new company IT systems (approximately 30,000 man/hours).
The overall investment (net of personnel costs for missed production) totals Euro 1,020,840 for the year 2005, up 5.6% on 2004.

The table below quantifies, in terms of man/hours provided, the training scheduled in the 2005 Training Programme:

Training	*Man Hours*
Professional training and specialised courses	45,261
Quality, Safety and Environment	15,010
Managerial training	8,288
Information technology	34,554
Total	**103,113**

2.01.08 Information Systems

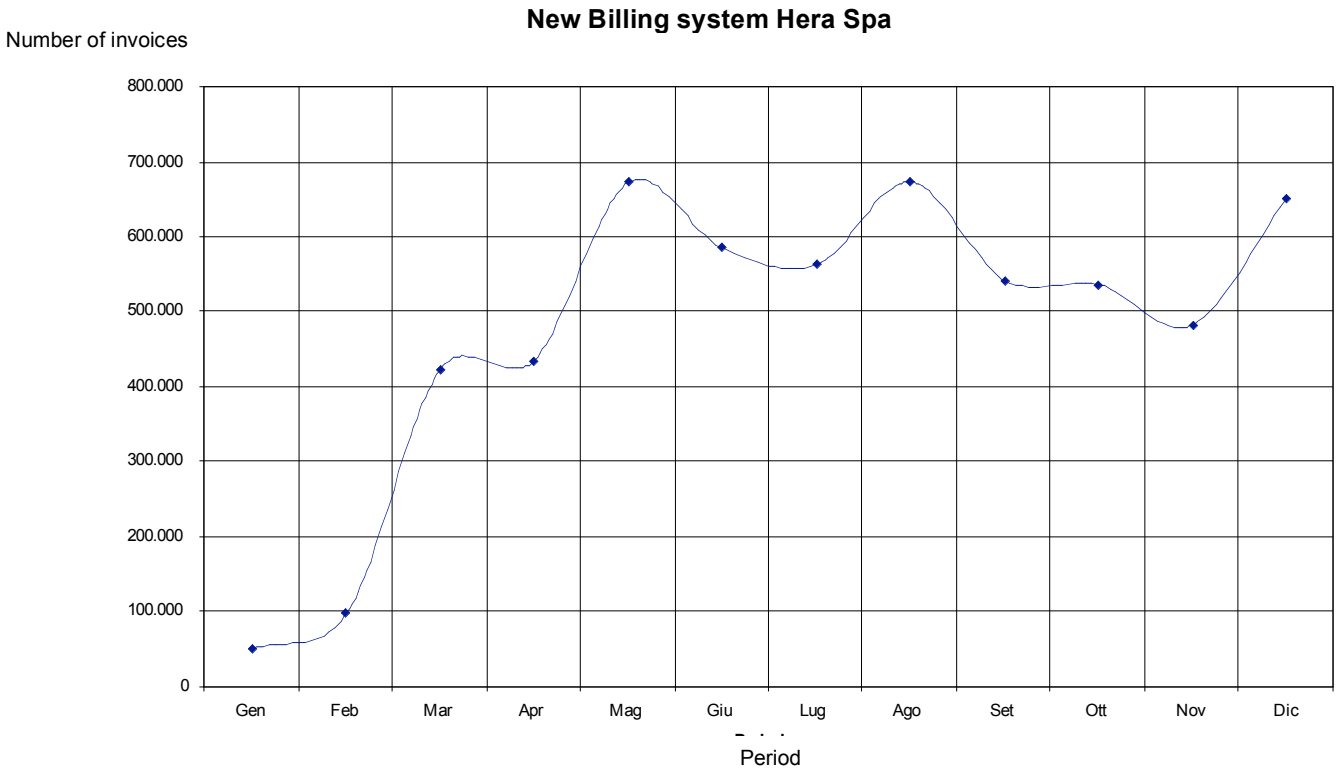
During 2005, the Group continued to optimise internal processes, pursuing the principle of departmental centralisation and rationalisation of all common activities in order to obtain uniform treatment and economies of scale.

The following were the most significant events of the year:

- the full integration of the Ferrara area (former Agea/former Acosea) into the Group
- the beginning of the process of integration of the Modena area (former Meta)
- the revision of the Organisational Macrostructure
- the launch of the new billing system (SAP-ISU) on 70% of the managed territory.

First Phase of SAP-ISU Consolidation

After the introduction of the new billing system, launched in the territories of Rimini (end of 2004) Bologna and Ravenna (February and March 2005) and Forlì/Cesena (June), implementation continued in the territorial area of Imola/Faenza and in the commercial area of Business customers with suspension of billing on the old systems from the month of November.
Trends in invoices issued in 2005, in the territories of Rimini, Bologna, Ravenna, Forlì-Cesena, Imola-Faenza and in the Business customer area, are illustrated in the graph below:



The consequences of suspension of billing in the Imola-Faenza area and Business customer area, for the purposes of implementation of the SAP-ISU system, were reflected in the increase in working capital and in the net financial position as at 31 December 2005 (total impact in the region of Euro 119 million).
However in the first three months of 2006 the billing process in the aforesaid areas has reached full capacity and it is expected that working capital will return to customary levels within the first six months of this year.

The implementation programme has now scheduled application of the new billing system in the Modena area in the first half of 2006 and in Ferrara in 2007.

2.01.09 Quality and Environment

Hera' commitment towards achieving "sustainable quality" progressed strongly in 2005, through a series of actions concerning, among other things, the following:

- stronger emphasis on the sustainability objectives within the 2006-2008 Strategic Plan
- continuation of the integrated Quality Safety Environment certification programme
- setting up of a CRS function (Corporate Social Responsibility)
- creation of a Balanced Scorecard system covering the entire corporate system.

As far as the objective of integrated Group certification is concerned, during 2005, the Quality management system was consolidated and Environment management was implemented in compliance with UNI EN ISO 14001 standards. Hence the final phase of certification of Hera shall occur in the first half of 2006, slightly later than the initial schedule (December 2005).
A further confirmation of Hera's strong commitment to environmental issues was also provided by the approval of the project for EMAS registration, over the 2006-2010 period, of the entire Environment Division of Hera SpA for a total, as at 2005, of 32 sites (corresponding to 53 waste treatment and disposal plants).
The Ecolabel Ecoaudit Committee awarded Hera the international European Emas Award for the aforesaid project.
During 2005, Hera also confirmed its commitment to completing the objective of Group integrated certification with the achievement of the certification of the Safety system, in compliance with the OHSAS 18001 standard, by 2007.
The 2004 Sustainability Report, published during 2005, saw further widening of compliance with the principles defined by the major international reference standards and consolidation of dialogue with the stakeholders, with the involvement of the mayors of the shareholding municipalities, of environmental associations and of employees.
Greater emphasis was given, in the 2004 Sustainability Report, to reporting on progress in the commitments undertaken in the 2003 Report and to defining the commitments for the year 2005.
Tangible evidence of Hera's attention to the two major corporate stakeholders, to customers and to its own employees, was provided in 2005 by the performance of a Customer Satisfaction survey throughout the territory and on all services supplied (which revealed that 88% of customers were satisfied or very satisfied) and by a Corporate Climate survey which involved the full spectrum of Hera employees.
Both surveys, which will be repeated at regular intervals, generated numerous improvement projects involving the majority of corporate functions.
The 2005 Sustainability Report, which will be published in the coming months, shall further continue the improvement process, along the foundations that have been set over the past years.
Hera's commitment to encouraging broader debate and confrontation on the issues of sustainability included the staging of an itinerant photographic exhibition which toured the 8 major towns in the territory throughout the second-half of 2005. In association with this exhibition, the Group held an on-line photographic competition named "Sustainable Glances", open to everyone up to 31 December 2005, with the forwarding of entries and the assessment of the same occurring entirely through the Hera Group website.

2.01.10 Annual Report on Corporate Governance

Introduction

Borsa Italiana S.p.A., has drawn up a Code of Conduct (hereafter the "Code") containing a series of recommendations relating to the procedures and regulations for the management and control of companies listed on regulated markets.

The Code presents a corporate organisational structure in line with the corporate and administrative practices adopted by the majority of companies which have implemented, in recent years, evolved models of corporate governance.

The adoption of the principles contained in the Code has the final objective of reassuring the investors on the existence, in listed companies, of a clear and well-defined organisational structure, with adequate division of responsibility and a correct balance between management and control.

Although the adoption of the principles contained in the Code are not a legal obligation, Hera S.p.A (hereafter the "Company") has considered it appropriate to adhere to the principles of the Code.

The Company adopted the provisions of the Code with a resolution passed by the Board of Directors, with a unanimous vote, on 4 April 2003.

This report illustrates the manner and procedures through which the Company has implemented the provisions of the Code.

Role and Composition of the Board of Directors

The Board of Directors is the central administrative body of the Company. In compliance with the recommendations of the Code, by which the Board of Directors must meet on a regular basis, the Company By-Laws provide that the Board meets periodically, at least on a quarterly basis, and whenever the Chairman considers it necessary or when a request is made by at least one third of its members or by the Board of Statutory Auditors. In addition, in compliance with the recommendations of the Code which provide that the Board must function and operate in such a way as to guarantee the effective and efficient performance of its duties, the Company By-Laws provide that the Board of Directors is vested with the widest powers for the ordinary and extraordinary management of the Company without limitations, with faculty to implement all actions considered necessary or appropriate to the pursuit of corporate objectives, excluding only those that, by law or the By-Laws, are strictly reserved to the Shareholders' Meeting.

In particular, in accordance with the By-Laws resolutions on the following matters are of the exclusive competence of the Board:

(i) appointment and/or revocation of the Chairman and Vice Chairmen;
(ii) appointment and/or revocation of the Managing Director and/or of the General Director;
(iii) constitution and composition of the executive committee, appointment and/or revocation of the members of the Executive Committee;
(iv) determination of the powers delegated to the Managing Director and/or General Director and/or Executive Committee and amendments thereto;
(v) approval and amendments to long-term plans or business plans;
(vi) approval and amendment of the group regulations, if adopted;
(vii) engagement and/or appointment, upon the proposal of the Managing Director, of the managers responsible for each departmental area.
(viii) proposal to place on the agenda of the extraordinary Shareholders' Meeting amendment to article 7 (public majority shareholding), 8 (limits to shareholding), 14 (quorum for constitution and for resolutions of the Shareholders' Meeting and rights of veto) and 17 (procedures for the nomination of members of the Board of Directors) of the By-laws;
(ix) the assumption and disposal of equity investments worth more than Euro 500,000 ;
(x) purchase and/or sales of properties worth more than Euro 500,000;
(xi) the provision of sureties, liens and/or other collateral worth more than Euro 500,000;
(xii) purchase and/or sale of companies and/or business units;
(xiii) the appointment of directors of subsidiary and/or investee companies;
(xiv) participation in tenders and/or public procedures that involve contractual obligations exceeding Euro 25,000,000.

The Company By-Laws, amended by Shareholders' Meeting resolution of 23 September 2005, provide that the Board of Directors is comprised of 18 members. The current Board of Directors will remain in office until the approval of the financial statements relating to 2007.

Name and surname	Office	Position
Tomaso Tommasi di Vignano	Chairman	Executive Director
Maurizio Chiarini	Managing Director	Executive Director
Giorgio Razzoli (2)	Vice Chairman(3)	Non-executive independent director
Mara Bernardini (2)	Director	Non-executive independent director
Filippo Brandolini	Director	Non-executive independent director
Luigi Castagna	Director	Non-executive independent director
Pier Luigi Celli	Director	Non-executive independent director
Piero Collina (1)	Director	Non-executive independent director
Pier Giuseppe Dolcini (1)	Director	Non-executive independent director
Giuseppe Fiorani (2)	Director	Non-executive independent director
Vander Maranini	Director	Non-executive independent director
Nicodemo Montanari	Director	Non-executive independent director
Fabio Roversi Monaco (1)	Director	Non-executive independent director
Roberto Sacchetti	Director	Non-executive independent director
Luciano Sita	Director	Non-executive independent director
Ermanno Vichi	Director	Non-executive independent director
Stefano Zolea	Director	Non-executive independent director

(1) Members appointed by the Shareholders' Meeting of 28 April 2005 on the basis of lists presented by minority shareholders in compliance with the provisions of Law 474/1994.
(2) Members appointed directly by the Municipality of Modena pursuant to Article 2449 of the Italian Civil Code with effect from 31 December 2005.
(3) Member appointed by the Vice Chairman of the Board of Directors on 16 January 2006.

Currently there are 15 directors qualifying as non-executive independent members of the Board, in that:
(i) they do not have, or have recently had, directly, indirectly or on behalf of third parties, economic relations with the Company, its subsidiaries, the executive directors, the shareholder or groups of shareholders which control the company, of such consistency as to influence the autonomy of their judgment;
(ii) they are not holders, directly, indirectly, or on behalf of third parties, of shareholdings of such consistency as to permit them to exercise control or considerable influence over the Company, nor are they party to shareholders' agreements for the control of the Company;
(iii) they are not close family members of executive directors of the Company or of subjects indicated in letters (i) and (ii) above.
The following circumstances do invalidate the requisites for independence of a director: the appointment of the director by the shareholder or group of shareholders that control the Company, holding the office of director of a subsidiary of the Company and relative remuneration, holding the office of member of one of consultative committee described hereunder.

The Board of Directors, in the meeting of 28 April 2005, passed a resolution to confer to the Chairman, in addition to the powers entrusted by Annex 9.2 of the Voting Trust and Share Transfer Rules Agreement, which are fully transcribed below:

a) to preside and manage the Shareholders' Meetings;

b) to establish the agenda of the meetings of the Board of Directors taking into account the proposals of the Managing Director;

c) to supervise the execution of the resolutions passed by the corporate boards of the Company, also based on the periodic reports provided by the internal audit department and on which he shall be obliged to report jointly with the Chairman;

d) to represent the Company before third parties and in court with the power to appoint attorneys and lawyers;

e) in the case of urgency, to take, in association with the Managing Director, all decisions pertaining to the Board of Directors, notifying the Board of Directors thereof in the subsequent meeting;

f) in association with the Managing Director, to propose to the Board of Directors designation of Company representatives on the administrative and control boards of the investee companies;

g) to represent the company in relations with the shareholding public authorities;;

h) to propose to the Board the candidates for members of the Committees that the Board may decide to constitute in compliance with the Stock Exchange regulations by which the Company is bound or may intend to constitute;

the following powers:

1. to execute the decisions of the Shareholders' Meeting and of the Board of Directors as far as his authority permits;
2. to supervise the Company's performance for the purposes of achieving corporate goals and to draw up proposals relating to management of the Company to be submitted to the Board of Directors;
3. to be responsible for the organisation of the services and offices under his authority and also for the subordinate employees;
4. to take, in association with the Managing Director, any urgent decision reserved to the Board of Directors, of which the Board shall be notified in the first meeting thereafter;
5. to supervise operations of the Company and of the subsidiaries, providing the Board of Directors with a monthly report;
6. to draw up the Multi-Year Plans and the Business Plan to be submitted to the Board of Directors; to implement corporate and Group strategies, within the context of directives established by the Board, and to exercise the powers delegated thereto, and in particular those listed hereunder, in compliance with said strategies and directives;
7. to propose to the Board all the initiatives that he may deem useful to the interests of the Company, and of the Group, and to draw up proposals on matters reserved to said Board;
8. to represent the Company in the shareholders' meetings of companies, associations, entities and bodies which do not constitute stock companies, of which said Company is member, with faculty to issue special proxies;
9. to effect deposits on bank and postal current accounts of the Company, and to endorse cheques and drafts for crediting on said accounts;
10. to actively or passively represent the Company before Public and Private Entities and Offices,

Chambers of Commerce, Stock Exchanges, the National Commission for Listed Companies and the Stock Exchange, the Ministry for Foreign Trade, and the Italian Exchange Office as well as any other Public Administration or Authority; by way of example:

a. to sign notices, including notice to the General Register of Shares and to CONSOB, and to fulfil the corporate obligations provided by law and regulations;
b. to submit reports, motions and appeals, to apply for licences and authorisations;

11. to represent the Company in all active and passive lawsuits, in all stages of civil and administrative proceedings, before arbitration boards, with the widest powers to:
    a. bring conservative, restraining and executive actions, request summary judgments and seizure of property and oppose the same, enter civil proceedings, file motions and appeals;
    b. request and oppose any evidence, undergo free or formal examination, elect domicile, appoint lawyers, attorneys and arbitrators and perform all else that proves necessary to the positive outcome of the lawsuits at issue;
12. to confer and revoke powers of attorney within the aforesaid powers, for individual acts or categories of acts, to both employees of the Company and to third parties including legal entities;
13. to stipulate and sign contracts and memorandums of association of companies, associations, and consortiums worth no more than €500,000.00 (Euro five hundred thousand) for each transaction;
14. to establish, in the Company's interest, consulting relations with external experts and professional consultants, specifying terms and conditions of payment, all within the limits of €100,000.00 (Euro one hundred thousand) for each transaction;
15. as far as his authority permits, to stipulate, amend and terminate commercial and service agreements of any nature with companies and entities;
16. to participate, as far as his authority permits, in the capacity of representative of the Company, as lead company or as principal company, in the incorporation of joint ventures, T.A.C. (Temporary Associations of Companies), E.G.E.I. (European Group of Economic Interest), consortiums and other entities, issuing and receiving the relative mandates, for the purpose of participating in tenders for the award of works, service and supplies;
17. to take part, as far as his authority permits, in the Company's name, also in T.A.C. (Temporary Associations of Companies), E.G.E.I. (European Group of Economic Interest), consortiums and other entities, in tenders for contracts or concessions, auctions, private invitations to tender, private treaties, calls for bids and other public auctions at national, community and international level, even admitted to State contribution or aid, for the award of works, supplies of plant, including "turnkey", and/or of goods and/or of studies and/or of research and/or of services in general for any national, community and international public or private entity; submit application for participation from the prequalification stage; submit bids and, in the case of award, sign the relative documents, contracts and commitments, including the issue of guarantees and/or the establishment of deposit money, with full and wide powers to negotiate, settle and/or complete all the clauses that he may deem necessary and/or appropriate and/or useful;
18. to take part, as far as his authority permits, in any type of public or private auction or invitation to bid in Italy and abroad;
19. to stipulate, amend and terminate contracts for insurance policies with expense limit relating to the annual premium;

20. to rent or let out property under lease or sublease and stipulate, amend and terminate the relative contracts;
21. to deliberate the cancellation, reduction, restriction of mortgages or liens registered in favour of the Company, as well as subrogation in favour of third parties, where the aforesaid cancellations and waivers are requested further or subordinate to the full discharge of the credit;
22. as far as his authority permits, to stipulate, with all the appropriate clauses, assign and terminate contracts and agreements in any case pertaining to the corporate purpose – including those referring to know-how, trademarks and patents – even in consortium with other companies;
23. to establish, register and renew mortgages and liens for third parties' account and to the benefit of the Company; permit mortgage cancellations and limitations for third parties' account and to the benefit of the Company for return and reduction of obligations; waive mortgages and mortgage subrogation, including those of a legal nature, and effect any other mortgage transaction, always for third parties' account and to the benefit of the Company, and therefore receivable, exonerating the competent property registrars from each and any responsibility;
24. to appoint lawyers and attorneys in any disputes and for any stage of proceedings; conclude settlements, sign arbitration agreements and arbitration clauses, also proceeding to nominate and appoint arbitrators;
25. to appoint attorneys for single acts, within the powers assigned;
26. to decide the Company's subscription to bodies, associations, entities of a scientific and technical nature or pertaining to studies and research within the Company's field of interest, for which fees do not constitute an interest in the equity of said entity and for which participation does not involve an outlay of more than €100,000.00 (Euro one hundred thousand);

During the same meeting the Board of Directors passed a resolution to vest the Managing Director with the following powers:

1. to execute the decisions of the Shareholders' Meeting and of the Board of Directors as far as his authority permits;
2. to take, in association with the Chairman, any urgent decision reserved to the Board of Directors, of which the Board shall be notified in the first meeting thereafter;
3. to implement corporate and Group strategies, within the context of directives established by the Board, and to exercise the powers delegated thereto, and in particular those listed hereunder, in compliance with said strategies and directives;
4. to propose to the Board all the initiatives that he may deem useful to the interests of the Company, and of the Group, and to draw up proposals on matters reserved to said Board;
5. draw up the annual budget to be submitted to the Board of Directors;
6. to be responsible for the organisation of the services and offices under his authority and also for the subordinate employees;
7. to define the functional structures of the Company and its subsidiaries, within the framework of the general organisation lines established by the Board, specify the criteria for personnel recruitment and management in compliance with the annual budget; propose the engagement of directors to the Board of Directors; engage, appoint and dismiss personnel up to and excluding the rank of General Director, in compliance with the provisions contained in the annual budgets; adopt and implement the disciplinary sanctions, dismissal and any other

measure in respect of workers, office workers, assistants and auxiliaries;

8. to stipulate, amend and terminate contracts for the opening of credit, loans of any type and duration; request the drawdown of tranches of loans, up to the amount of €3,000,000.00 (Euro three million) for each contract;
9. to open and close current accounts with banks and credit institutions, withdraw sums from the accounts held in the Company's name, issuing for this purpose the relative cheques or equivalent credit documents, and order transfers utilising effective availability or credit lines in the current account;
10. to effect deposits on bank and postal current accounts of the Company, and to endorse cheques and drafts for crediting on said accounts;
11. to draw bills on customers, endorse also for discount promissory notes, bills and drafts as well as cheques of any kind and effect any consequential transaction;
12. to actively and passively represent the Company before Financial Administration and Commissions of any nature and rank as well as before Cassa Depositi Prestiti, Bank of Italy, Customs Offices, Post and Telegraphic Offices; by way of example:
    a. to sign tax and VAT returns and to fulfil any tax-related obligation,
    b. to submit reports, motions and appeals, to apply for licences and authorisations;
    c. to issue receipts, in particular for payment orders in relation to credits subject to factoring transactions;
    d. to perform any transaction at Cassa Depositi Prestiti, Bank of Italy, Customs Offices, Post and Telegraphic Offices for shipment, deposit, clearance and collection of goods, credit instruments, parcels and packages, registered and insured letters, issuing receipts in discharge;
13. to represent the Company in all lawsuits pertaining to labour law including the power to:
    a. settle individual labour disputes concerning the categories of officers, white-collar workers, assistants and auxiliaries;
    b. request and oppose any evidence, undergo free or formal examination, elect domicile, appoint lawyers, attorneys and arbitrators and perform all else that proves necessary to the positive outcome of the lawsuits at issue;
14. to represent the Company before the offices of Social Security Institutions for the solution of issues relating to employees of the Company, and also before Trade Unions in negotiations for contracts, agreements and labour disputes, with the power to sign the relative documents;
15. to issue guarantees and grant loans up to the value of €500,000.00 (Euro five hundred thousand) for each transaction; said limit shall not apply to transactions related to participation in tenders; issue, accept and endorse credit instruments;
16. to confer and revoke powers of attorney within the aforesaid powers, for individual acts or categories of acts, to both employees of the Company and to third parties including legal entities;
17. to participate, as far as his authority permits, in the capacity of representative of the Company, as lead company or as principal company, in the incorporation of joint ventures, T.A.C. (Temporary Associations of Companies), E.G.E.I. (European Group of Economic Interest), consortiums and other entities, issuing and receiving the relative mandates, for the purpose of participating in tenders for the award of works, service and supplies;
18. to take part, as far as his authority permits, in the Company's name, also in T.A.C. (Temporary Associations of Companies), E.G.E.I. (European Group of Economic Interest), consortiums

and other entities, in tenders for contracts or concessions, auctions, private invitations to tender, private treaties, calls for bids and other public auctions at national, community and international level, even admitted to State contribution or aid, for the award of works, supplies of plant, including "turnkey" and/or of goods and/or of studies and/or of research and/or of services in general for any national, community and international public or private entity; submit application for participation from the prequalification stage; submit bids and, in the case of award, sign the relative documents, contracts and commitments, including the issue of guarantees and/or the establishment of deposit money, with full and wide powers to negotiate, settle and/or complete all the clauses that he may deem necessary and/or appropriate and/or useful;

19. to take part, as far as his authority permits, in any type of public or private auction or invitation to bid in Italy and abroad;
20. as far as his authority permits, to stipulate, amend and terminate commercial and service agreements of any nature with companies and entities;
21. as far as his authority permits, to stipulate, with all the appropriate clauses, assign and terminate contracts and agreements in any case pertaining to the corporate purpose – including those referring to know-how, trademarks and patents – even in consortium with other companies;
22. to establish, in the Company's interest, consulting relations with external experts and professional consultants, specifying terms and conditions of payment, all within the limits of €100,000,00 (Euro one hundred thousand) for each transaction;
23. to conclude settlements, sign arbitration agreements and arbitration clauses, also proceeding to nominate and appoint arbitrators;
24. to arrange for guarantees to be provided by third parties in favour or in the interest of the Company, both in its position as creditor and as debtor, not exceeding the amount of €100.000,00 (Euro one hundred thousand) for each transaction;
25. to provide for the expenses incurred by the Company for investments; stipulate, amend and terminate the relative contracts, in particular for:
    a. works and supplies necessary to the transformation and maintenance of properties and plants;
    b. purchases and disposals of furniture, fittings, machinery and moveable assets in general, including those enrolled in public registers, as well as finance leases and rentals of said assets, with the cost limit referred to the annual rental;
    c. purchases, also under usage licence with cost limit referred to the annual premium, and job orders relating to EDP programmes;
    d. commercial information;
26. to appoint attorneys for single acts, within the powers assigned;
27. the Managing Director is also assigned the powers and responsibilities set forth in Legislative Decree no. 626 of 19 September 1994 and subsequent amendments and integrations in the matter of workers' health and safety during work, all of which with faculty to delegate;
28. in particular, the Managing Director is assigned the role of "Employer" pursuant to and for the purposes of Legislative Decree no. 626 of 19 September 1994 and subsequent amendments and integrations, with the duties provided for therein with faculty to delegate, as far as is permitted by said decree, the performance of every activity useful and/or necessary to ensuring compliance with provisions of the law;

29. lastly, the Managing Director is assigned the powers and responsibilities set forth in Legislative Decree no. 196 of 30 June 2003 concerning the protection of persons and other entities in respect of the treatment of personal data.

Hence neither the Chairman nor the Managing Director are executive directors.

In compliance with the recommendations of the Code, the delegated offices report to the Board of Directors and to the Board of Statutory Auditors, at least on a quarterly basis, on the activities performed in the exercise of the powers assigned thereto and on the most important economic and financial operations implemented by the Company and by the subsidiaries, with particular reference to atypical, unusual operations or those with related parties.

The Board of Directors in compliance with the provisions of Article 23 of the By-Laws and Article 150 of the Legislative Decree 58/98, regularly reports to the Board of Statutory Auditors, at least on a quarterly basis, normally during the meetings of the Board of Directors or even directly with written report sent to the Chairman of the Board of Statutory Auditors, on the activities performed and on the most important economic and financial operations implemented by the Company and by its subsidiaries, as well as on the operations in which the directors have an interest, on their own behalf or on behalf of third parties or which have been influenced by the party that exercises the activity of direction and coordination. The director, pursuant to Article 2391 of the Italian Civil Code, informs the other directors and the board of statutory auditors of every interest that, on his own behalf or on behalf of third parties, he has in a given operation of the company, indicating the nature, terms, origin and value; if the managing director is involved he must abstain from undertaking the operation entrusting it to the board.

In 2005 the Board of Directors met 22 times. In 5 meetings all of the directors and the statutory auditors participated and in the other 18 meetings almost all of the directors and the entire board of statutory auditors participated, with the exception of four meetings in which one statutory auditor was absent.

The General Director of the company is invited to attend the meetings of the Board of Directors and during 2005 attended 20 meetings.

In relation to the current year, as at 27 March 2006, 4 meetings of the Board of Directors have been held which almost all of the directors and the entire board of statutory directors attended; at present another 5 meeting of the Board of Directors have been scheduled.

The Chairman ensures that each Director and Statutory Auditor has all of the information and documentation necessary to discuss the business on the agenda of the Board meetings at least 3 days before the meeting, except in the cases of necessity and urgency.

Lastly, the Chairman and Managing Director ensure that the Board of Directors is also informed on the most important changes in legislation and regulations relating to the company and corporate offices.

Role and Composition of the Executive Committee

The Board of Directors, as provided by Article 23.3 of the By-Laws, in the meeting of 16 January 2006, set up an Executive Committee, appointing the following members:

- Tomaso Tommasi di Vignano - Chairman,
- Giorgio Razzoli - Vice Chairman,
- Maurizio Chiarini - Member.

The Committee, with regard to the annual definition of the Group Industrial Plan and to the proposals for appointment of 1st level Senior Managers, has the task of expressing an opinion prior to presentation to the Board of Directors and also deliberating:

1. as to contracts and conventions in any way pertaining to the corporate purpose worth more Euro 2 million per single contract;
2. in the interest of the Company consulting relations with external experts and professional consultants, specifying terms and conditions of payment, worth more than Euro100,000 and up to Euro 500,000 and more generally on the overall criteria for use;
3. as to the Company's subscription to bodies, associations, entities of a scientific and technical nature or pertaining to studies and research within the Company's field of interest, for which fees do not constitute an interest in the equity of said entity and for which participation involves an outlay of more than Euro 100,000 and up to Euro 500,000.
4. to settle disputes and/or waive credits of an amount exceeding Euro 1,000,000;
5. as to the activation, amendments and termination of contracts for the opening of credit, loans of any type and duration which involve a commitment of more than Euro 1,000,000 and up to Euro 5,000,000; request the drawdown of tranches of loans, for an amount of more than Euro 3,000,000 and up to Euro 5,000,000 per single contract;
6. as to the stipulation, amendment and termination of contracts relating to:
   - works and supplies necessary to the transformation and maintenance of properties and plants worth more than €15,000,000;
   - *purchase and disposal of furniture, fittings, machinery and moveable assets in general, including those enrolled in public registers worth more than € 8,000,000*

As at 27 March 2006 the Executive Committee has held one meeting, at which all the members were present.

Nomination and Remuneration of Directors

Article 17 of the By-Laws attributes to the local authorities holding shares the faculty to nominate, pursuant to Article 2449 of the Italian Civil Code, 14 members of the Board of Directors. In practice this means that:
the Municipality of Bologna has the right to nominate 4 directors; the Province of Bologna, including on behalf of 47 Municipalities, has the right to nominate 1 director; the Municipality of Cesena, including on behalf of another 25 Municipalities, has the right to nominate 1 director; Con.Ami has the right to nominate 1 director; the Municipality of Forlì has the right to nominate 1 director, the Municipality of Ravenna, including on behalf of another 11 other Municipalities, has the right to nominate 1 director, the Municipality of Rimini, including on behalf of another 26 Municipalities, has the right to nominate 1 director, the Municipality of Ferrara, including on behalf of another 9 Municipalities, has the right to nominate 1 director, the Municipality of Modena, including on behalf of another 30 Municipalities, has the right to nominate 3 director.

The other 4 members of Board of Directors not nominated by local authorities will be nominated by the Shareholders' Meeting on the basis of the list vote system provided for by Article 17 of the By-Laws which specifies that the list must be presented by shareholders representing at least 1% of shares with voting rights and must be filed, at the Company's registered office at least 20 days prior to the date set for the Shareholders' Meeting, together with the curriculum vitae of the candidates, their irrevocable acceptance of the appointment and a certificate verifying that there are no grounds for ineligibility and/or forfeiture.
These lists will be made public through notice published in three national newspapers of which two financial, at least 10 days prior to the Shareholders' Meeting. The local authorities entitled to effect direct nominations pursuant to Article 2499 of the Italian Civil Code must abstain from presenting lists and voting.

The local authorities holding shares have entered into a Voting Trust and Share Transfer Rules Agreement which provides clauses on the composition of the Board of Directors.

There are also two consultation pacts that provide for clauses on the composition of the Board of Directors and in particular:

1) pact of consultation signed on 16 September 2003 and most recently modified on 27 July 2005 by 30 minority shareholders of HERA S.p.A.;
2) pact of consultation signed on 6 November 2003 and most recently modified on 14 September 2005 by 5 minority shareholders of HERA S.p.A .

The Shareholders' Meeting of 28 April 2005 awarded the directors a fixed annual remuneration.

The Board of Directors, in the meetings of 30 May 2005 and 6 February 2006, deliberated to award the Chairman and the Managing Director a remuneration comprising a fixed amount, inclusive of the indemnity due thereto, as well as a further variable annual consideration linked to the Company's operating results or to the reaching of specific targets set by the Remuneration Committee (in this case the Remuneration Committee linked the variable annual consideration to the Company's achievement of set indexes for EBITDA, Net Profit and NFP of the Hera Group).

In the meeting of 30 May 2005, the Board of Directors also awarded, only to the directors holding specific roles, a further fixed annual remuneration over and above the consideration due thereto as directors, for serving on other Boards of Directors of Group companies and/or other boards associated with the Company's Board of Directors.
In the meeting of 16 January 2006, the Board of Directors passed a resolution to award the Vice Chairman a fixed annual remuneration inclusive of the consideration due thereto as director and of any other consideration for offices held within Group companies.

Committees

The Committees constituted are representative of the Board of Directors and fulfil an advisory and consultative role.

a) Remuneration Committee

In the meeting of 4 November 2002, the Board of Directors, in compliance with the provisions of the Code, constituted the Remuneration Committee with the role of formulating proposals to the Board of Directors for the remuneration of the Managing Director, the Chairman and the directors holding particular roles, as well as on the basis of indications provided by the Managing Director, for the adoption of general criteria for the remuneration of management, without prejudice to the Managing Director's duty to define policies and levels of management remuneration.

This Committee is composed of Giorgio Razzoli (appointed on 16 January 2006) as Chairman, Pierluigi Celli (appointed on 11 May 2005), Piero Collina (appointed on 11 May 2005) and of Nicodemo Montanari (appointed on 11 May 2005). The Chairman of the Board of Directors and the Managing Director may attend the Committee meetings upon express invitation of the Chairman of the Committee.

In the year 2005 the Committee held 4 meetings during which it defined the guidelines of the Remuneration Policy for the Management of the Group for the year 2005.

b) Internal Control System and Internal Control Committee

An Internal Auditing function has been set up within the Company, and the person in charge reports directly to the Managing Director.

The person responsible for Internal Auditing provides a report of his activity, on a quarterly basis or whenever he considers it necessary, to the Managing Director, to the Chairman of the Board of Directors, to the Internal Control Committee and to the Board of Statutory Auditors.

In terms of hierarchy he is not subordinate to the heads of the operating divisions.
In compliance with the provisions of the Code, the Board of Directors of the Company, in the meeting of 4 November 2002, passed a resolution to set up an Internal Control Committee with advisory and consultation functions. This committee is composed of Giorgio Razzoli (appointed on 16 January 2006), as Chairman, Ermanno Vichi (appointed on 11 May 2005) and Stefano Zolea

(appointed on 11 May 2005). The Chairman of the Board of Statutory Auditors or another Statutory Auditor designated by the Chairman and, upon express invitation of the Chairman of the Committee, the Managing Director and the Chairman of the Board of Directors, may attend the Committee's meetings. The Committee has been assigned the functions indicated at paragraph 10.2 of the Code.

The Internal Control Committee met 5 times in 2005; 4 meetings were attended by all of the members while 1 meeting was attended by the majority of members.
The Chairman of the Board of Statutory Auditors attended all of the meetings.

During the above-mentioned meetings the audit plan was assessed as were the audit activities performed.

c) Committee for the Proposal of Nominations

A Committee for the proposal of nominations to the office of Director has not been set up as pursuant to the By-Laws the nomination of 14 directors is the responsibility of the local authorities as per Article 2449 of the Italian Civil Code and that of the other 4 directors is the responsibility of the remaining shareholders through the list vote system.

Treatment of Confidential Information

The Board of Directors of the Company, in the meeting of 10 March 2003, passed a resolution to approve the code of conduct for the members of the corporate boards and the employees of the Company and subsidiary companies – "Internal Dealing" – which was adopted by the Company as from the date in which trading commenced (26 June 2003).

The aforesaid code, drawn up on the basis of the Regulations and Instructions of Borsa Italiana S.p.A., governs the reporting obligations relating to transactions on financial instruments carried out by Directors, the General Director and the Statutory Auditors of the Company, as well as by any other person who has access, by virtue of the office held in the Company and in its main subsidiaries, to information on facts such as to determine significant variations in the economic and financial prospects of the Company and of the Group and capable, if made public, of significantly influencing the price of the relative financial instruments (so called "significant persons" or "internal dealers").

The provisions of the code of conduct are binding for "significant persons". The persons considered as such are:
(i) the Directors, Standing Auditors and General Director;
(ii) General Management and Divisional Managers;
(iii) persons in the Company and its main subsidiaries (that is, the companies whose revenues exceed 10% of the total consolidated revenues), identified by the Managing Director, each in relation to his area of competence, who, by virtue of the role held in the pertinent company, may have access to information on facts such as to determine significant variations in the economic and

financial prospects of the Company and the Group and capable, if made public, of significantly influencing the price of the relative listed financial instruments issued by the Company.

Communications from significant persons must be sent to the person responsible for the Legal and Corporate Affairs Department. This person will liaise with the person responsible for investor relations for disclosure to the market of the information through the electronic system NIS (Network Information System).

The Code of Conduct is published on the Company's website www.gruppohera.it

Transactions with Related Parties

In relation to the recommendations contained in Articles 5 and 11 of the Code of Conduct and in order to guarantee that any significant transactions with related parties are implemented in compliance with the criteria of substantial and procedural correctness, the Board of Directors on 27 May 2003 adopted the following procedure:

1) The Board identified the related parties as:
a) parties that control, are controlled by, or are subject to common control with the issuer;
b) the parties subscribing, even indirectly, to the shareholders' agreements as set forth in Article 122, sub-section 1 of the Finance Act 58/1998, referring to the exercise of the voting right, if these agreements are vested with a total controlling interest;
c) the parties related to the issuer and those which exercise a significant influence on the issuer;
d) those who are assigned powers and responsibilities pertaining to the exercise of functions of administration, direction and control of the issuer;
e) close family members of the individual persons included in letters a), b), c), and d);
f) the parties controlled by the individual persons included in letters b), c), d) and e) and over which the individual persons included in letters a), b), c), d) and e) exercise a significant influence;
g) the entities that share the majority of the directors with the issuer.

2) The Board of Directors approves in advance the transactions with related parties, including inter-group transactions, except typical or usual transactions or those to be concluded under arm's length conditions as per point 3) below.

3) Typical or usual transactions are those that, due to their subject matter or nature, are not unrelated to the normal business of the Company and those that do not feature critical elements due to their characteristics or risks relating to the nature of the counterpart, or to the time of their fulfilment. Arm's length transactions are those concluded at conditions applied by the Group to any party.

4) The Board of Directors, through the delegated bodies, receives adequate information on the nature of the relation, on the procedures for execution of the transaction, on the conditions, including those of an economic nature, for its implementation, on evaluation procedures followed, on the interests and on the underlying reasons, and on any risks for the Company. Where the

relation is with a Director or with a party related through a Director, the Director in question will do no more than provide clarification and absent himself from the meeting during deliberation.

5) Based on the nature, value and other characteristics of the transaction, the Board of Directors, in order to avoid that the transaction is carried out at inappropriate conditions, may be assisted by one or more experts who express an opinion, as the case may be, on the economic conditions and/or on the legitimacy and/or on technical aspects of the transaction.

6) For the transactions with related parties, including inter-group transactions, that are not submitted to the Board of Directors, in that typical or usual and/or at arm's length conditions, the delegated bodies, without prejudice to compliance with procedures as per Article 150, sub-section 1, of the Finance Act 58/1998, gather and conserve, including by type or groups of transactions, adequate information on the nature of the relation, on the procedures for execution of the transaction, on the conditions, including those of an economic nature, for its implementation, on the evaluation procedures followed, on the interests, and on the underlying reasons and on any risks for the Company.
One or more experts may also be nominated for these transactions, in accordance with the above procedures.

7) The experts selected must be recognised professionals and experts on the subject matter, of whom the independence and the absence of conflicts of interest will be carefully assessed.

The most important transactions with related parties during 2005 are specifically reported in the Directors Report.

Relations with Shareholders

In order to favour a more detailed knowledge of the Company on the part of the shareholders, the Company has set up a special structure dedicated to investors relations. On 11 March 2003, Mr. Jens Klint Hansen was appointed as head of investor relations (Investor Relations may be contacted through the telephone number + 39 051 287737 or the email address ir@gruppohera.it).

The Shareholders' Meeting of 29 April 2003 approved the Shareholders' Meeting Regulations. These regulations indicate the procedures to be followed in order to permit the orderly and proper functioning of meetings, without prejudice to the right of each shareholder to express his opinion on the matters under discussion.

The Shareholders' Meeting Regulations are published on the Company's website www.gruppohera.it

Statutory Auditors

The Board of Statutory Auditors is composed of three standing members. Two alternative members have also been appointed. The Board of Statutory Auditors will remain in office until approval of the financial statements for the year ended 2007.

Composition of the Board of Statutory Auditors

Name and surname	Office
Antonio Venturini	Chairman
Fernando Lolli	Standing Auditor
Sergio Santi (*)	Standing Auditor
Stefano Ceccacci (*)	Alternate Auditor
Roberto Picone	Alternate Auditor

(*) appointed by the Shareholders' Meeting of 28 April 2005 on the basis of the only list presented by the minority shareholders in compliance with the provisions of legislation in force.

The By-Laws provide that the Statutory Auditors must possess the requirements of integrity and professionalism established by legislation in force.

For the purposes of the provisions of legislation in force concerning the requirements of professionalism of the members of the Board of Statutory Auditors of listed companies, subject matter and sectors of activity strictly relating to the activities carried out by the company are intended to mean the subject matters and sectors connected or relating to the activity exercised by the company and set forth in Article 4 of the By-Laws.

The office of statutory auditor is not compatible with that of councillor or alderman in local public authorities, or with that of statutory auditor in more than 3 listed companies with the exclusion of the subsidiaries of the Company pursuant to Articles 2359 of the Italian Civil Code and 93 of the Legislative Decree 58/98. In this latter case, the statutory auditor that subsequently exceeds said limit automatically falls from office as statutory auditor of the company.

The statutory auditors are nominated by the Shareholders' Meeting on the basis of the list vote system provided by Article 26 of the By-Laws which specifies that (i) the Municipalities, the Provinces and the Consortiums constituted pursuant to Article 31 of the Legislative Decree 267/2000 and the consortiums or the joint-stock companies controlled by these may present a single list and (ii) the shareholders other than those indicated in point (i) may present lists provided they represent at least 3% of the shares with voting rights. The lists must be filed at the registered office at least 20 days prior to the date of the Shareholders' Meeting, together with the declaration of the individual candidates certifying the inexistence of grounds for ineligibility or incompatibility provided by law, as well as existence of requirements of integrity and professionalism as required by law for the members of the Board of Statutory Auditors.
These lists will be made public through notification in three national newspapers of which two financial newspapers, at least 10 days prior to the Shareholders' Meeting.

The Shareholders' Meeting of 28 April 2005 appointed the new members of the Board of Statutory Auditors designated by a list presented by Public Shareholders representing over 3% of the shares with voting rights and from a minority list in order to comply with the obligations of the law.

The Board of Statutory Auditors held 14 meetings, of which 11 were attended by all the members and 3 by the majority of members.

The local authorities holding shares have entered into a Voting Trust and Share Transfer Rules Agreement which provides clauses on the composition of the Board of Statutory Auditors.

There are also two consultation pacts that provide for clauses on the composition of the Board of Statutory Auditors and in particular:

1) pact of consultation signed on 16 September 2003 and most recently modified on 27 July 2005 by 30 minority shareholders of HERA S.p.A.;
2) pact of consultation signed on 6 November 2003 and most recently modified on 14 September 2005 by 5 minority shareholders of HERA S.p.A .

Administrative Responsibility of the Company

Legislative Decree 231/2001 introduced into Italian legislation the administrative responsibility of legal entities, companies and associations. In particular, the law introduced the penal responsibility of entities for certain offences committed in the interest or to the advantage of the same by persons fulfilling roles of representation, administration or management of the entity or one of its organisational units with financial and operating independence, as well as persons who exercise, even de facto, management and control thereof and, lastly, persons subject to the direction or supervision of one of the above mentioned parties. The important offences are the offences against Public Administration and corporate offences committed in the interest of the companies.

However, Articles 6 and 7 of Legislative Decree 231/2001 provides for a form of exoneration from the responsibility where (i) the entity proves that it adopted and efficiently implemented, prior to commitment of the act, organisational, management and control models appropriate to preventing the perpetration of the offences considered by said decree; and (ii) the duty of supervising the effectiveness of and compliance with the models, as well as providing for their revision, is entrusted to a board of the entity vested with autonomous powers of initiative and control.
For this purpose, on 16 February 2004, the Board of Directors of Hera SpA approved the organisational, management and control model pursuant to Legislative Decree 231/2001 with the aim of creating a structured and organic system of procedures and control activities directed at preventing the offences referred to in the aforesaid decree, through identification of activities exposed to the risk of offence and the consequent implementation of procedures therein.

Hence the Board of Directors set up the supervision board composed of the Head of Internal Auditing of Hera SpA as the Chairman, the Head of Legal and Corporate Affairs of Hera SpA and an external member to which it entrusted the aforesaid duties including the periodic reporting to the corporate boards of Hera SpA on the implementation of the said model.

The Supervision Board met 6 times in 2005; all the meetings were attended by all the members.

The Supervision Board provided for the revision of the organisational model which was extended to the other Group companies. The Supervision Board also applied and analysed the information flows that permits the Board to supervise the effectiveness of and compliance with the models.
In order to carry out the verifications and controls, the Supervision Board drew up a schedule of interventions to verify compliance with the protocols adopted.

The Company also adopted an Ethical Code which was approved by the Board of Directors on 16 February 2004 and was widely circulated to both employees and stakeholders.

TABLE 1 : STRUCTURE OF THE BOD AND OF THE COMMITTEES

UP TO 28.04.2005

Board of Directors

Office	Members	executive	non-executive	independent	****	Number of other offices **	Internal Control committee ***	Internal Control committee ****	Remuneration Committee ***	Remuneration Committee ****	Nomination Committee (where present) ◊ ***	Nomination Committee (where present) ◊ ****	Executive Committee (where present) ***	Executive Committee (where present) ****
Chairman	Tomaso Tommasi di Vignano		X	X	100%									
Managing Director	Stefano Aldrovandi	X			100%									
Director	Aleardo Benuzzi		X	X	100%				X	100%				
Director	Enrico Biscaglia		X	X	71%		X	100%						
Director	Filippo Brandolini		X	X	100%						Not present		Not present	
Director	Piero Collina *		X	X	100%				X	100%				
Director	Pier Giuseppe Dolcini *		X	X	86%									
Director	Nicodemo Montanari		X	X	86%									
Director	Fabio Roversi Monaco *		X	X	57%		X	100%						
Director	Roberto Sacchetti		X	X	86%									
Director	Giovanni Tamburini		X	X	71%									
Director	Fulvio Vento		X	X	86%									
Director	Ermanno Vichi		X	X	86%		X	100%						

_ Summary of the reasons fo r absence (where applicable) of the Committee or composition differing from Code recommendations:

_ Summary of the reasons for absence (where applicable) of the Committee or composition differing from Code recommendations:

◊ Summary of the reasons for ab sence (where applicable) of the Committee or composition differing from Code recommendations: **the Committee was not set up insofar as pursuant to the By -Laws 11 directors are to be appointed by the public authorities as per Article 2449 Italian Civil Code and the other 3 through the list vote system**

Number of meetings held during the period under review (up to 28.04.2005)	BOD: 7	Internal Control Committee: 1	Remuneration Committee: 1	Nomination Committee: /	Executive Committee: /

NOTE

* The presence of asterisks indicates whether the director was appointed through lists presented by minority shareholders

** This column indicates the number of offices as director or statutory auditor the party concerned holds in other companies listed on regulated markets, including foreign markets, in financial, banking, insurance companies or large enterprises

*** In this column an "X" indicates the Board member's membership of the Committee

**** This column indicates the percentage of attendance of the directors in the Board meetings and Committee meetings respectively

TABLE 1 : STRUCTURE OF THE BOD AND OF THE COMMITTEES FROM 28.04.2005

Board of Directors							Internal Control Committee _		Remuneration Committee _		Nomination Committee (where present) ◊		Executive Committee from 6.01.2006	
Office	Members	esecutive	non-esecutive	independent	****	Number of other offices **	***	****	***	****	***	****	***	****
Chairman	Tomaso Tommasi di Vignano	X			100%								X	-
Managing Director	Maurizio Chiarini	X			93%								X	-
Director	Giorgio Razzoli (from 31.12.2005)		X	X	-		X	-	X	-			X	-
Director	Mara Bernanrdini (from 31.12.2005)		X	X	-									
Director	Filippo Brandolini		X	X	93%						Not present			
Director	Luigi Castagna		X	X	100%									
Director	Pier Luigi Celli		X	X	73%				X	67%				
Director	Piero Collina *		X	X	87%				X	100%				
Director	Pier Giuseppe Dolcini *		X	X	87%									
Director	Giuseppe Fiorani (from 31.12.2005)		X	X	-									
Director	Vander Maranini		X	X	93%		X	75%						
Director	Nicodemo Montanari		X	X	93%				X	100%				
Director	Fabio Roversi Monaco *		X	X	87%									
Director	Roberto Sacchetti		X	X	100%									
Director	Luciano Sita		X	X	80%									
Director	Ermanno Vichi		X	X	100%		X	100%						
Director	Stefano Zolea		X	X	100%		X	100%						

_ Summary of the reasons for absence (where applicable) of the Committee or composition differing from Code recommendations:
_ Summary of the reasons for absence (where applicable) of the Committee or composition differing from Code recommendations:
◊ Summary of the reasons for absence (where applicable) of the Committee or composition differing from Code recommendations: **the Committee was not set up insofar as pursuant to the By -Laws 14 directors are to be appointed by the public authorities as per Article 2449 Italian Civil Code and the other 4 through the list vote system**

Number of meetings held during the period under review (from 28.04.2005)	BOD: 15	Internal Control Committee: 4	Remuneration Committee: 3	Nomination Committee: /	Executive Committee: -

NOTE
* The presence of asterisks indicates whether the director was appointed through lists presented by minority shareholders
** This column indicates the number of offices as director or statutory auditor the party concerned holds in other companies listed on regulated markets, including foreign markets, in financial, banking, insurance companies or large enterprises
*** In this column an "X" indicates the Board member's membership of the Committee
**** This column indicates the percentage of attendance of the directors in the Board meetings and Committee meetings respectively

TABLE 2 : BOARD OF STATUTORY AUDITORS

Office	Members	Percentage attendance of Board meetings	Number of other offices **
Chairman	Venturini Antonio	100%	-
Standing Auditor	Fernando Lolli	93%	-
Standing Auditor *	Sergio Santi	93%	2
Alternate Auditor *	Stefano Ceccacci	-	-
Alternate Auditor	Roberto Picone	-	-

Number of meetings held in the calendar year: 14

Indicate the quorum required for the presentation of lists on the part of minority shareholders for the election of one or more standing members: Article 26 of the By - Laws specifies that (i) the Municipalities, the Provinces and the Consortiums pursuant to Article 31 of Legislative Decree no. 267/2000 as well as the consortiums and joint -stock companies in any case controlled by said entities may present a single list and (ii) the shareholders other than those indicated at point (i) may present lists provided that the y represent at least 3% of the shares with voting right .

NOTE
* The asterisk indicates whether the statutory auditor has been designated through lists presented by minority shareholders.
**This column indicates the number of offices as director or stat utory auditor the party concerned holds in other companies listed on regulated Italian markets.

TABLE 3: OTHER PROVISIONS OF THE CODE OF CONDUCT

	YES	NO	Summary of the reasons for any deviation from the Code recommendations
System of delegated powers and transactions with related parties			
Has the BOD delegated powers defining:			
a) limits	X		
b) procedures for exercise	X		
c) frequency of reporting?	X		
Has the BOD reserved the right to examine and approve the transactions of particular importance in financial and economic terms (including transactions with related parties)?	X		
Has the BOD defined guidelines for the identification of "important" transactions?		X	The BOD has not defined the guidelines and criteria for the identification of "important" transactions, however the delegated bodies provide prior report to the BOD and spontaneously submit to the approval thereof the transactions of greater importance in economic, strategic and financial terms.
Are the above guidelines described in the report?		X	
Has the BOD defined special procedures for approval of the transactions with related parties?	X		
Are procedures for approval of the transactions with related parties described in the report?	X		
Procedures for the most recent nomination of directors and statutory auditor			
Were the nominations for the office of director filed at least 10 days in advance?	X		
Were the nominations for the office of director accompanied by exhaustive information?	X		
Were the nominations for the office of director accompanied by specification of suitability to qualify as independent?		X	The By-Laws do not make provision for this, however following appointment, the directors have filed appropriate declaration certifying the existence of the requirement of independence.
Were the nominations for the office of statutory auditor filed at least 10 days in advance?	X		
Were the nominations for the office of statutory auditor accompanied by exhaustive information?	X		

	YES	NO	Summary of the reasons for any deviation from the Code recommendations
Shareholders' Meetings			
Has the company approved Shareholders' Meeting Regulations?	X		
Are the Regulations attached to the report (or is it specified where they may be obtained/downloaded?)	X		
Internal Control			
Has the company appointed the persons in charge of internal control?	X		
In terms of hierarchy are the persons in charge non-subordinate to the heads of the operating divisions?	X		
Organisational unit in charge of internal control (pursuant to Article 9.3 of the Code)	X		
Investor relations			
Has the company appointed a person responsible for investor relations?	X		
Organisational unit and references (address/telephone/fax/e-mail) of the person responsible for investor relations	*Jens Klint Hansen (HERA S.p.A. V.le Carlo Berti Pichat 2/4, 40127 Bologna / telephone +39 051 287737 / fax 051 287224 / e-mail ir@gruppohera.it.*		

2.01.11 Holdings of Directors, Statutory Auditors and General Director

HOLDINGS OF DIRECTORS, STATUTORY AUDITORS AND GENERAL DIRECTOR (ART. 79 CONSOB REGULATIONS)

NAME	OFFICE HELD IN HERA S.p.A.	COMPANY	NUMBER OF SHARES HELD AS AT DECEMBER 31, 2004	NUMBER OF SHARES ACQUIRED	NUMBER OF SHARES SOLD	NUMBER OF SHARES HELD AS AT 31 DECEMBER 2005
Tomaso Tommasi di Vignano (1)	Chairman	Hera S.p.A.	8.000	2.000	-	10.000
Maurizio Chiarini	Managing Director	Hera S.p.A.	-	-	-	-
Giorgio Razzoli	Vice Chairman	Hera S.p.A.	-	-	-	-
Mara Bernardini	Director	Hera S.p.A.	-	-	-	-
Filippo Brandolini	Director	Hera S.p.A.	2.750	-	-	2.750
Luigi Castagna (1)	Director	Hera S.p.A.	250	1.700	-	1.950
Pier Luigi Celli	Director	Hera S.p.A.	-	-	-	-
Piero Collina	Director	Hera S.p.A.	-	-	-	-
Pier Giuseppe Dolcini	Director	Hera S.p.A.	2.750	-	-	2.750
Giuseppe Fiorani	Director	Hera S.p.A.	-	-	-	-
Vander Maranini	Director	Hera S.p.A.	-	-	-	-
Nicodemo Montanari	Director	Hera S.p.A.	-	-		-
Fabio Alberto Roversi Monaco	Director	Hera S.p.A.	-	36.000	-	36.000
Roberto Sacchetti	Director	Hera S.p.A.	-	-	-	-
Luciano Sita	Director	Hera S.p.A.	-	-	-	-
Vichi Ermanno	Director	Hera S.p.A.	-	-	-	-
Stefano Zolea	Director	Hera S.p.A.	-	-	-	-
Antonio Venturini	Chairman Board of Statutory Auditors	Hera S.p.A.	-	-	-	-
Fernando Lolli	Member Board of Statutory Auditors	Hera S.p.A.	-	-	-	-
Sergio Santi	Member Board of Statutory Auditors	Hera S.p.A.	-	-	-	-
Roberto Barilli	General Manager	Hera S.p.A.	-	25.000	-	25.000
Stefano Aldrovandi (in carica fino al 28.4.2005)	Managing Director	Hera S.p.A.	-	-	-	-
Aleardo Benuzzi (in carica fino al 28.4.2005)	Vice Chairman	Hera S.p.A.	2.750	-	-	2.750
Enrico Biscaglia (in carica fino al 28.4.2005)	Director	Hera S.p.A.	-	-	-	-
Giovanni Tamburini (in carica fino al 28.4.2005)	Director	Hera S.p.A.	-	10.895	-	10.895
Fulvio Vento (in carica fino al 28.4.2005)	Director	Hera S.p.A.	-	-	-	-

(1) held indirectly through spouse

2.01.12 Significant Events after Year-End

The most important events for the activities of the Group in the first months of 2006 are summarised below.

- ***A1 Rating from Moody's***

  On 27 January 2006 Moody's, the leading international rating agency, assigned the Hera Group A1 rating, with stable outlook, for the first time.

  Standard & Poor's also confirmed the Group's A+ rating, passing the outlook from stable to negative in the event of further acquisitions being planned for Hera, which however is not a circumstance envisaged by the Group's Industrial Plan.

  Hence Hera has become the only Italian public utility that can boast the double rating assigned by these two prestigious agencies.

  The rating level achieved reflects the Group's financial solidity and assumes even greater value in connection with the subsequent bond issue on the international markets. The principal grounds for the award of this rating lie in the fact that the company features a strong business profile, with a very balanced portfolio, provides excellent service levels in one of Europe's richest regions and enjoys share solidity and financial liquidity.

- ***First bond issue of the Hera Group***

  On 17 February 2006, with admission to trading on the Luxembourg Stock Exchange, the Group took the last step in the procedure, which began on the 27 January 2006 with the launch of the international roadshow to present the transaction to the market, which led Hera to its first bond issue.

  The issue, which has a 10 year duration and annual coupon detachment at a fixed rate of 4.125%, concluded with a success rate that surpassed even the most optimistic previsions. Demand was in the region of €2.2 billion (4.4. times higher than the offer of €500 million) and allowed Hera to reduce the credit spread to 47 basic points, above the mid-swap rate for the period, compared to the initial indications of 50 base points.

  The placement was implemented by the merchant banks JPMorgan, Citibank and Banca IMI.

- ***Purchase of own shares***

  On 16 January 2006, the Board of Directors of Hera approved an initiative for the repurchase of own shares for a counter-value of up to €45 million. This initiative will be submitted to the approval of the Shareholders' Meeting and shall be valid for 18 months.

  The shares purchased may be used within the scope of acquisitions transactions which involve share trades.

  The purchase will be effected on the market managed by Borsa Italiana S.p.A. at a price per share no lower than the nominal value and no higher than 5% compared to the reference price recorded in the market day preceding each purchase.

  To date Hera does not hold own shares and the maximum number of own shares that may be purchased is equal to 15,000,000 ordinary shares, the equivalent of approximately 1.5% of share capital.

- ***Merger through incorporation of Geat Distribuzione Gas***

  On 16 January 2006, the Board of Directors of Hera approved the project for merger through incorporation in the Hera Group of Geat Distribuzione Gas, the company which operates in the distribution of gas in the Riccione area and, through its subsidiary Gas Riccione, in the sales to end customers.

  The transaction, of which the value has been established as €12.5 million, allows Hera to continue the process of consolidation with its own reference territory, which in 2005 saw integration of Meta and acquisition of three local operators serving the municipalities of Ro Ferrarese, Castello d'Argile and Monghidoro for a total of approximately 147,000 customers.

  The transaction with Geat Distribuzione Gas represents a strategic element which allows the Group to create, together with the equity investment already held in the company SGR Servizi, a core unit in the province of Rimini with significant opportunities for synergy.

  The company Geat has over 20,000 customers and achieves sales to the order of approximately 40 million m^3 of natural gas. The transaction is scheduled to be concluded next summer, while the effects will commence as from 1 January 2006.

- ***Increase of the equity investment held in Hera Luce S.r.l.***

  On 17 January 2006 Hera S.p.A. acquired the share held by Gemmo S.p.A. (equal to 18% of share capital) in Hera Luce S.r.l., the company which manages the public lighting service activities, hence bringing its interest to 87.3%.

- ***Purchase from Enel of the electricity grid of 18 Municipalities of the Province of Modena***

  On 13 March 2006 Hera and Enel signed the preliminary agreement for disposal of the Enel distribution grid of 18 Municipalities of the Province of Modena for a total consideration of approximately Euro 107.5 million. The business unit at issue includes 80,000 customers and over 3,700 km serving the Municipalities of Castelnuovo Rangone, Fanano, Fiumalbo, Guiglia, Lama Mocogno, Marano sul Panaro, Montecreto, Contese, Pavullo nel Frignano, Pievepelago, Polinago, Riolunato, San Cesario sul Panaro, Sestola, Spilamverto, Vignola and Zocca.

- ***Disposal of minority investments in no-core areas***

  The activity of rationalisation of the Group's corporate investments in no-core areas continued and particular mention is given to the following: sale to the Municipalities of Piano di Sorrento and of Meta, of 48% of Penisola Verde S.P.A., a company which supplies environmental services in Campania and sale, to the Municipality of Ferrara, of 20% of Ferrara T.U.A. S.p.A., a company which provides paying parking services.

As far as progress in the projects relating to the new waste-to-energy (WTE) and electricity generating plants is concerned, the following is reported:

- the new WTE plant of Frullo, after having concluded the first year of industrial operation with a total quantity of disposed waste equal to 188.1 Kton (+ 4.7% compared to 2004) and an electricity production equal to 92,09 Gwh (+ 308% compared to 2004), in the first two months of 2006 disposed of a total of 35,000 tonnes of waste and produced over 24,000,000 Kwh, in addition to 12,000,000 of Mcal for district heating;
- the WTE plant of Ferrara (Canalbianco) is under construction and all the orders have been issued; the plant is scheduled to start operations at the end of the first year-half 2007;
- the WTE plant of Forlì was granted final authorisation in September 2005 and all the orders were issued by the end of 2005; the work site is scheduled to open in the forthcoming month of May and plant start-up is scheduled for September 2007;
- the WTE plant of Modena is under construction, all the orders have been issued and plant start-up is scheduled for the end of the second year-half 2007;
- for the WTE plant of Rimini the authorisation process is scheduled to be completed in the forthcoming May; all the orders have been subjected to pre-contract and plant start-up is scheduled for the first year-half 2008;
- the co-generation plant of Imola (80 MW) has been granted final authorisation by the Ministry of the Environment and all the orders have been defined; plant start-up is scheduled for halfway through the second year-half of 2007;
- as far as the Sparanise plant is concerned (800 MW of which Hera holds a 15% interest), the construction works are progressing according to plan and plant start-up is confirmed for the first year-half 2007;
- lastly, as far as the Teverola plant is concerned (400 MW of which Hera holds a 39% interest), the construction activities are nearing completion and plant start-up is confirmed for the end of 2006.

2.02 Attachments to the Consolidated Financial Statements pro-forma of Hera Group

2.02.01 Income statement pro-forma

HERA Group - Consolidated Financial Statement pro-forma as at Dec. 31, 2005
Income Statement

	Note	Dec. 31, 2005 € /000	Dec. 31, 2004 € /000 (Adjusted)
Income statement			
Net sales	4	2.100.508	1.492.572
Change in inventories of finished products and products in work in progress		2.190	9.187
Other operating revenues	5	44.908	27.106
Consumption of raw materials and consumable materials (net of the change of the inventories of raw materials and stocks)	6	-1.014.815	-622.006
Service costs	7	-496.192	-416.930
Personnel costs	8	-270.066	-215.863
Depreciation, amortisation and provisions		-170.674	-115.256
Other operating expenses	9	-124.430	-92.152
Capitalised costs	9,1	144.279	110.599
Operating profit		**215.708**	**177.257**
Adjustments to technical fixed assets	10	15.518	0
Quota of profits/(losses) of associated companies	11	-620	-3.029
Financial income	12	35.025	6.071
Financial charges	12	-76.351	-32.755
Pre-tax result		**189.280**	**147.544**
Income taxes	13	-80.524	-61.083
Discontinued activities			
Profit from discontinued activities			
Net profit/(loss) for the period		**108.756**	**86.461**
Attributable:			
To the shareholders of the Parent Company		101.398	80.994
To the minority shareholders		7.358	5.467
EBITDA		**386.382**	**292.513**

2.02.02 Balance sheet pro-forma

HERA Group - Consolidated Financial Statement pro-forma as at Dec. 31, 2005
Balance sheet

	Notes	Dec. 31, 2005 €/000	Dec. 31, 2004 €/000 (Adjusted)
Tangible fixed assets	14	1.914.946	1.298.867
Intangible fixed assets	15	212.847	210.947
Goodwill and consolidation differences	16	280.127	151.610
Equity instruments and securities	17	91.831	78.385
Financial assets	18	66.478	18.903
Deferred tax assets	19	27.480	35.079
Financial instruments - derivatives	20	3.413	0
Other non current assets	21	35.756	43.804
		2.632.878	**1.837.595**
Current assets			
Inventaries	22	35.751	41.513
Trade receivables	23	895.657	597.452
Contract work in progress	24	20.688	14.671
Financial assets	25	16.039	36.827
Other current assets	26	143.406	44.922
Cash and cash equivalents	27	189.107	172.372
		1.300.648	**907.757**
Assets classifed as available for sale			
TOTAL ASSETS		**3.933.526**	**2.745.352**
SHAREHOLDERS' EQUITY AND LIABILITIES			
Share capital and reserves	28		
Share capital		1.016.752	839.903
Reserves		345.663	114.988
Reserve for derivative instruments valued at fair value		-4.185	0
Retained earnings/(Accumulated losses)		0	0
Net profit/(loss) for the period		101.398	80.994
Group shareholders' equity		**1.459.628**	**1.035.885**
Minority interest share		30.603	28.346
Total shareholders' equity		**1.490.231**	**1.064.231**
Non-current liabilities			
Loans - payable beyond one year	29	534.518	489.063
Employee leaving indemnity and other benefits	30	100.902	82.634
Provisions for risk and charges	31	119.923	79.206
Deferred tax liabilities	32	94.614	53.036
Debiti per locazioni finanziarie – scadenti oltre l'esercizio successivo	33	39.859	28.668
Financial instruments - derivatives	20	19.225	
Other non-current liabilities	34	105.344	91.135
		1.014.385	**823.742**
Current liabilities			
Banks and financing - payable within one year	29	645.628	271.832
Lease finance payables - payable within one year	33	9.784	62
Trade payables	35	670.051	432.923
Taxes payable	36	32.545	86.670
Other current liabilities	37	70.902	65.892
Financial instruments - derivatives		0	0
		1.428.910	**857.379**
Liabilities directly associated with assets classified as available for sale			
Total liabilities		**2.443.295**	**1.681.121**
TOTAL SHAREHOLDERS' EQUITY & LIABILITIES		**3.933.526**	**2.745.352**

3 – CONSOLIDATED FINANCIAL STATEMENTS OF THE HERA GROUP

3.01 Directors' report

3.01.01 Corporate Events and Group Structure

The year 2005 saw continuation of the intense activity of rationalisation of the Group's corporate equity investments, which led to the disposal or liquidation of 23 investee companies and to the merger or split-off of two further companies, as scheduled in the disposal programme.
In the course of 2004 the Group had already effected the disposal or liquidation of 12 investee companies, and the merger of four companies operating in the environmental sector.
Further corporate rationalisation transactions have already been scheduled for 2006, chiefly relating to equity investments acquired with the integration of Meta into Hera SpA, and it is with this acquisition, the most important of last year, that the report of the M&A transactions implemented in 2005 opens.

Merger of Meta SpA into Hera SpA
On 29 November 2005, with the execution of the deed of merger of Meta SpA into Hera SpA, the process of integration of the two major multi-utilities of the Emilia Romagna Region, both listed on the Milan Stock Exchange, was completed.
The transaction was implemented through the launch of a partial Public Purchase Offer on the ordinary shares representing 29% of the share capital of Meta, which began on 31 October and was completed on 22 November with a 22% subscription and a capital increase of Euro 176,848,148, with exchange ratio of 1.286 Hera shares to each Meta share.
Hence, as from 31 December 2005, the date of statutory effect of the aforesaid merger deed, the share capital of Hera SpA rose by Euro 839,903,881 to Euro 1,016,752,029, while the accounting and tax effects of the transaction are retro-effective from 1 January 2005.

Acquisition of Tecnometano Srl and Gas Gas Srl
The month of July saw formal completion of the acquisition on the part of Hera of 100% of Tecnometano Srl, a company operating in the natural gas distribution sector within the municipality of Ro Ferrarese (FE), and of 100% of Gasgas Srl, active in natural gas sales in the same territory.
The transaction allows Hera to continue the process of consolidation which it has been pursuing for some time within its own territory and, in particular, in the province of Ferrara, in which there are numerous small operators in the gas business.

Acquisition of Argile Gas Srl
The month of June saw execution of the agreement with the company Gastecnica Galliera Srl for acquisition on the part of Hera Comm of 100% of the company Argilegas Srl, which operates in the natural gas sales sector in the area of Castello d'Argile, in the province of Bologna, where Hera already provides water and environmental services.
The transaction forms part of the process of consolidation launched by Hera in its own territory.

Acquisition of TS Distribuzione Srl and TS Energia Srl

In the month of December Hera SpA acquired 100% of the company TS Distribuzione gas Srl, which operates in the distribution of natural gas in the area of Monghidoro, in the province Bologna, while Hera Comm acquired 100% of the company TS Energia Srl, which operates in the sales of natural gas in the same area.

Incorporation of Hera Energie Bologna Srl

On 30 June Hera Comm Srl, sales company of the Hera Group, set up Hera Energie Bologna Srl, a company which supplies electricity and heat management services to third parties, in which it holds 67% of the share capital.

Further Transactions

Towards the end of 2005 a number of other transactions involving companies which were already members of the Hera Group were implemented.

- On 9 November 2005 Hera SpA acquired from Capital Service Srl 48% of the share capital of Uniflotte Srl, a company which operates in the management and maintenance of equipment, thus increasing its interest from 51% to 99%.
- On 27 December 2005 Hera SpA increased its interest in ASA SpA, from 20% to 51% of the share capital, acquiring 23% from the municipality of Castemaggiore and 8% from UNIECO Soc. coop. ASA SpA operates in the territory of Bologna in the environmental sector and is owner of a landfill for dangerous waste.

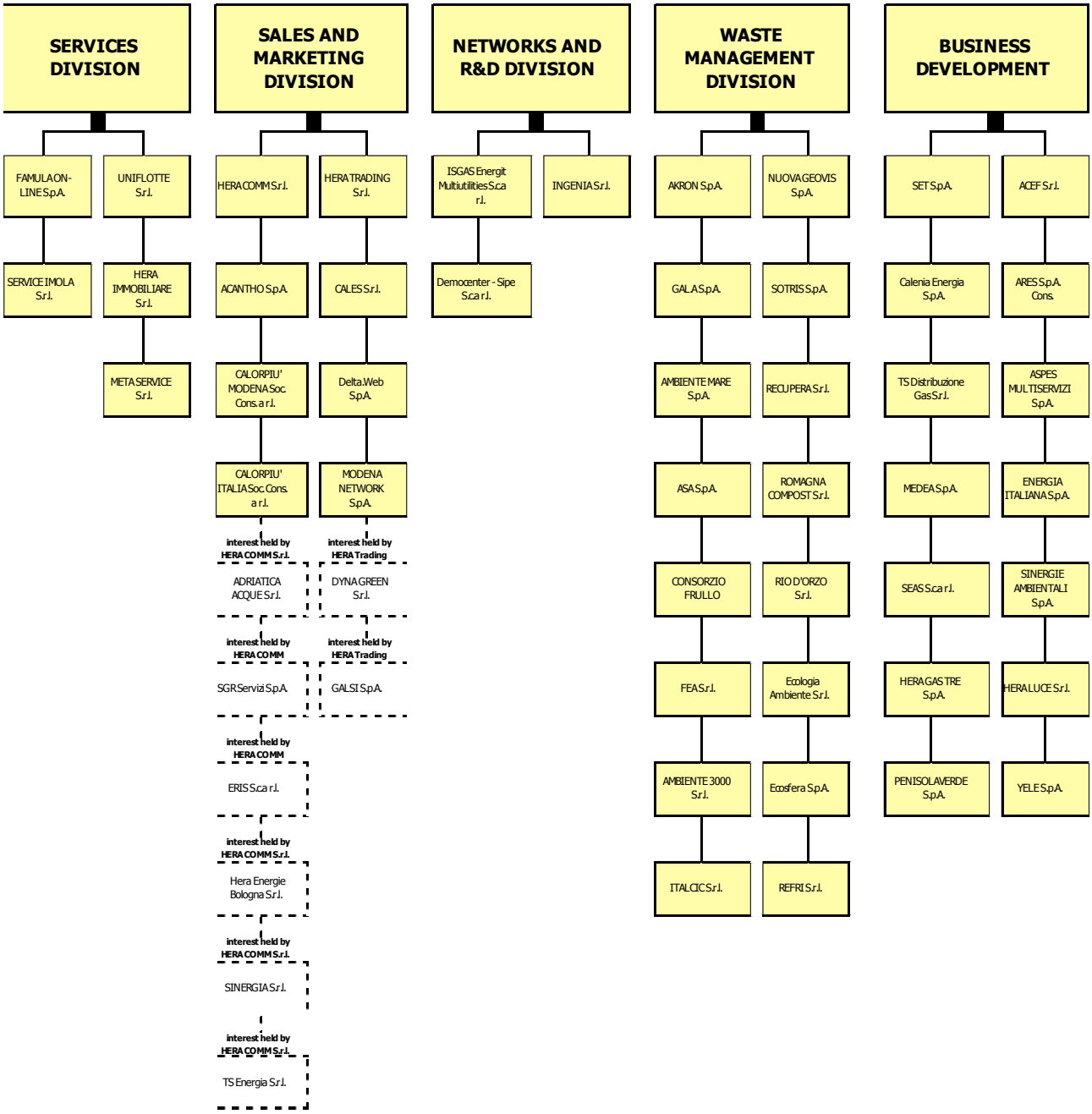
Memorandum of Understanding between Aspes Multiservizi SpA, Aset, Megas and Megas Trade.

On 15 February 2005 a memorandum was signed by the local utilities operating in the province of Pesaro-Urbino (Aspes Multiservizi, Aset, Megas and Megas Trade), the objective of which is to set up a single public service company. The memorandum provides that Hera will be the new company's industrial partner, fulfilling the role that it currently holds in Aspes Multiservizi. Development of the project is currently being examined by the various stakeholders.

Hera-Vng Agreement

On 21 February 2005 VNG – Verbundnetz Gas AG – of Leipzig and Hera SpA, at the signing of the new natural gas supply contract, also signed an agreement to establish a joint company for the trading of methane gas capable of developing its trading capacities on the European energy market. The procedures for incorporation of the company are under completion and the company shall commence operations by June 2006.

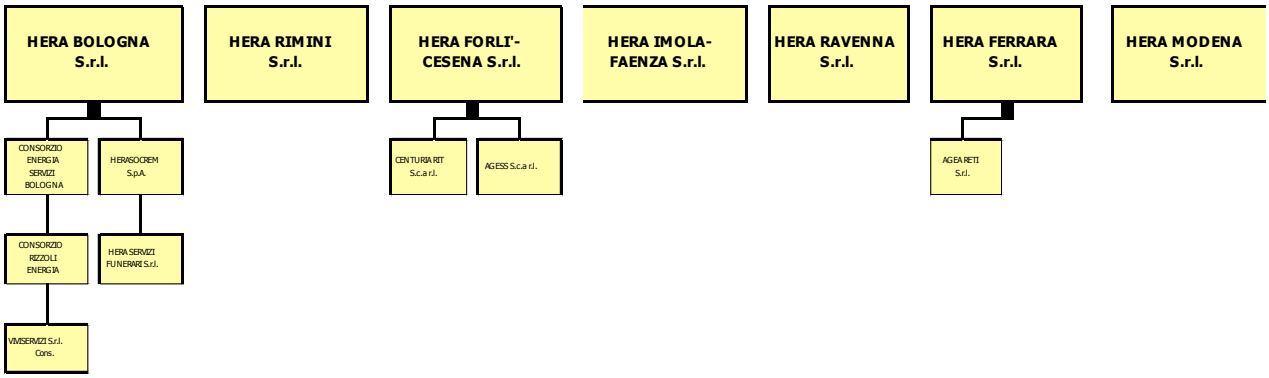
HERA SPA



Disposal of the following equity investments is scheduled: 4 Italy S.r.l. Energy & Environment, Ferrara T.U.A. - Traffico Urbano Autoparking S.p.A., Estense Global Service S.c.a r.l., acquired through the merger/split of AGEA and ACOSEA into HERA S.p.A.

Disposal of the following equity investments is also scheduled: Agenzia per l'Energia e lo Sviluppo Sostenibile, Modena Formazione S.r.l., AV2 Ecosistema S.p.A., Bio Energy S.r.l., Metaenergy S.r.l. and SO.SEL S.p.A., acquired through the merger of META S.p.A. into HERA S.p.A.

HERA SPA


HERA BOLOGNA S.r.l.
HERA RIMINI S.r.l.
HERA FORLI'-CESENA S.r.l.
HERA IMOLA-FAENZA S.r.l.
HERA RAVENNA S.r.l.
HERA FERRARA S.r.l.
HERA MODENA S.r.l.
CONSORZIO ENERGIA SERVIZI BOLOGNA
HERASOCREM S.p.A.
CENTURIA RIT S.c.a r.l.
AGESS S.c.a r.l.
AGEA RETI S.r.l.
CONSORZIO RIZZOLI ENERGIA
HERA SERVIZI FUNERARI S.r.l.
VMSERVIZI S.r.l. Cons.

3.01.02 Performance of the Hera Group in 2005:

3.01.02.01 Financial and Economic Results

As already mentioned previously, 2005 was a particularly intense year for the Group which saw an important expansion of the area in which it operates.

Following the positive conclusion of the transactions for the integration of the Ferrara companies - Agea Spa and Acosea Spa – which took place at the end of 2004, the related organisational integration was also completed by means of the creation of the territorial operating company Hera Ferrara srl at the beginning of 2005.

During the last few months of 2005, the process for the integration of Meta Spa of Modena was therefore launched, concluding with the merger within Hera spa on 31 December 2005; the transaction was however effective retroactively for tax and accounting purposes as of 1 January 2005.

During 2005, the process for the recovery of efficiency which had contributed to the Group's growth over the last few years continued, thus allowing the Group to close the accounting period with an improvement in all the main economic-financial figures.

2005 featured several events which had both positive and negative effects on the performance of operations:

- the particularly rigid climate trend helped gas sales, and the fully operative status of the new disposal plants started up or acquired in 2004, such as the new waste-to-energy plant at Bologna and the Ravenna Ecologic Centre, supported the satisfactory result of the Environment sector;
- by contrast, the 2004 tariff adjustments of the Authority for Electricity and Gas had a negative impact, especially in the distribution sector, together with the rise in competitive pressure in the gas and electricity sectors, particularly in the metropolitan areas. It should also be pointed out that the Summer was extremely wet and, penalizing the tourist season, had a significant effect on sales of the water cycle in coastal areas.

When interpreting the results, it should also be borne in mind that the Group, between the end of 2004 and 2005, entered into agreements with all the areas agencies in its territory, both for the waste management sector and the water cycle and that, just like all the other companies in the sector, it felt the effect of the important increase in prices of raw energy materials.

The above matters will be looked at in more depth further on, when analyzing the individual business areas.

A summary of the principal results in the period, followed by a more detailed analysis of the results by business area, is shown below:

Income statement (mln/€)	31-Dec-04	Incr.%	31-Dec-05	Incr.%	Change	Change %
Net sales	1,492.6		1,730.7		238.2	+16.0%
Change in inventories of finished products and products in work in progress	9.2	0.6%	2.5	0.1%	(6.7)	-73.2%
Other operating costs	27.1	1.8%	34.8	2.0%	7.7	+28.3%
Raw materials and consumable materials	(622.0)	-41.7%	(809.6)	-46.8%	(187.6)	+30.2%
Service costs	(416.9)	-27.9%	(440.1)	-25.4%	(23.2)	+5.6%
Other operating expenses	(92.2)	-6.2%	(108.0)	-6.2%	(15.9)	+17.2%
Personnel costs	(215.9)	-14.5%	(227.6)	-13.2%	(11.8)	+5.5%
Capitalized costs	110.6	7.4%	138.5	8.0%	27.9	+25.2%
EBITDA	**292.5**	**19.6%**	**321.0**	**18.5%**	**28.5**	**+9.8%**
Amm. & Depr.	(115.3)	-7.7%	(142.7)	-8.2%	(27.4)	+23.8%
EBIT	**177.3**	**11.9%**	**178.4**	**10.3%**	**1.1**	**+0.6%**
Adjustments to technical fixed assets	-	0.0%	15.5	0.9%	15.5	+0.0%
Quota of profits/(losses) of associated companies	(3.0)	-0.2%	(0.4)	0.0%	2.6	-85.3%
Net financial charges	(26.7)	-1.8%	(39.7)	-2.3%	(13.1)	+48.9%
Pre-tax profit	**147.5**	**9.9%**	**153.7**	**8.9%**	**6.2**	**+4.2%**
Tax	(61.1)	-4.1%	(66.1)	-3.8%	(5.0)	+8.1%
Net profit	**86.5**	**5.8%**	**87.7**	**5.1%**	**1.2**	**+1.4%**
of which:						
Minorities	5.5		7.3		1.8	+33.8%
Group net profit	81.0		80.3		(0.6)	-0.8%

The increase in **Revenues**, from Euro 1,492.6 million to Euro 1,730.7million, should chiefly be placed in relation to the rise in prices/volumes of energy commodities and to the significant increase in the Waste Management sector which produced a rise in revenues of approximately Euro 55 million.

In conclusion, with regards to the tariff trend, as described in more detail in the specific section, against scheduled increases in the Integrated Water Cycle and Waste Management areas there were the awaited tariff reductions, as well as in the Gas Distribution areas and, to a lesser extent, in the area of Electricity Distribution.

The rise in the **Costs of raw materials**, equating to Euro 187.6 million (+ 30.2%), derives from the increase in the costs associated with energy materials.

Service costs rose from Euro 416.9 million to Euro 440.1 million, disclosing an increase of 5.6%.

The increase in the item **Other operating charges**, from Euro 92.2 million to Euro 108.0 million (+ 17.2%), is due to the additional costs associated with the application of the conventions stipulated with the area agencies, in particular for the Integrated Water Service.

Mention should be made of the fact that the total increase in the items “Service costs” and “Other operating charges” amounted to Euro 39.1 million, and together with the increase in the item “Capitalized costs”, produced a total increase which was completely negligible. If one takes into account the increase in the services provided, especially in the Integrated Water Cycle area and

the new plants of the Waste Management area, the endeavour made by the Group to seek maximum efficiency and containment of the operating costs emerges as evident.

The **Personnel costs** rose from Euro 215.9 million to Euro 227.6 million in 2005 (+ 5.5%); as a percentage of Revenues, the figure improved by 1.3 percentage points, passing from 14.5% in 2004 to 13.2% in 2005. The increase in absolute terms concerns both the personnel in service at the new Waste Management plants and the extraordinary commitment required by the start-up of the new customer computerised information system which led to the use of temporary staff (on average 70 units over the year) as well as a heavier commitment of the customer contact structures.

The item **Capitalized costs** rose from Euro 110.6 million to Euro 138.5 million (+ Euro 27.9 million, or 25.2%) due to the effect of application to the Ferrara area of the Group organisation which provides for implementation of works on the part of Local Operating Companies and, accordingly, the recording in the income statement of most of the capitalised costs .

The Group's consolidated **EBITDA** at the end of 2005 rose by 9.8%, passing from Euro 292.5 million to Euro 321.0 million. This result was essentially obtained thanks to the positive performance of the Waste Management, Water Cycle and, to a lesser extent, Electricity sectors, while the marginal nature of the Gas business was down despite the favourable climate trend during the last few months of the year.

The percentage-based incidence of the Ebitda dropped from 19.6% to 18.5%, in relation to the afore-mentioned increase in energy commodities' prices.

Amortisation, depreciation and provisions rose from Euro 115.3 million in 2004 to Euro 142.7 million in 2005 (+ 23.8%), with an increase in the percentage-based incidence on revenues from 7.7% to 8.2%. The aforesaid increase is associated with the consistent investment plan sustained and some changes in the consolidation area.

In light of the above, the year 2005 closed with **EBIT** of Euro 178.4 million, up by 0.6% when compared with last year thanks above all to the positive performance of the activities for improving efficiency and reducing costs pursued during the year and the satisfactory results of the new plants in the Waste Management area.

The item **Writeback of values of tangible fixed assets** refers to the revaluation of assets written down at the time of the changeover to the new IAS/IFRS accounting standards, passing from reserves which, in relation to the Modena acquisition and a number of contractual changes, saw the reinstatement of the original value in the impairment test at the end of 2005.

The increase in **Financial charges**, rising from Euro 26.7 million to Euro 39.7 million, mainly reflects the rise in figurative charges linked to the application of the financial method to the provisions (IAS Nos. 17, 19 and 37) and the increase in indebtedness associated with (i) the transaction for the purchase of Meta shareholdings, (ii) the investment plan carried out and (iii) the

increase in working capital, associated with both the rise in total turnover and the implementation of the new SAP billing system.

The year closed with a **Pre-tax profit** of Euro 153.7 million, an improvement of 4.2 % on the previous year.

Group **Taxation** for 2005 amounted to Euro 66.1 million, with a ratio to Revenues of 3.8% and to pre-tax profits of 43.0%, compared with 4.1% and 41.4% respectively last year.

Hence the **Net profit** for 2005 came to Euro 87.7 million, compared with Euro 86.5 in the previous year, involving a percentage based increase of 1.4%.

The **Net profit pertaining to the Group** went from Euro 81.0 to Euro 80.3 million in 2005: the minority interest share increased (from Euro 5.5 to Euro 7.3 million) in 2005 thanks to the improved results of a number of consolidated investee companies, in particular Fea Srl.

The table below presents a reclassification of the Group balance sheet at 31 December 2005 presented on a comparative with the results for 2004, showing the evolution of the net capital employed and the sources of financing:

Analysis of the capital employed and the sources of financing of the Group

(milioni di euro)	**31 Dec. 04**	**%**	**31 Dec. 05**	**%**	**Change**	**Change %**
Intangible assets	*362,6*	*22,3%*	*486,3*	19,8%	*123,7*	*34,1%*
Tangible assets	*1.298,9*	*79,9%*	*1.914,9*	77,9%	*616,0*	*47,4%*
Financial assets	*13,0*	*0,8%*	(44,9)	(1,8%)	(57,9)	*-445,4%*
Total fixed assets	1.674,5	103,0%	2.356,3	95,9%	681,8	*40,7%*
Net working capital	113,1	7,0%	322,0	13,1%	208,9	*184,7%*
(Provisions)	(161,8)	(10,0%)	(220,8)	(9,0%)	(59,0)	*36,5%*
Net capital employed	**1.625,8**	**100,0%**	**2.457,5**	**100,0%**	**831,7**	**51,2%**
Shareholders' equity	1.064,2	65,5%	1.483,5	60,4%	419,3	*39,4%*
Long-term debt	*498,9*	30,7%	*523,7*	21,3%	*24,8*	*5,0%*
Net short-term position	*62,7*	3,9%	*450,3*	18,3%	*387,6*	*618,2%*
Net financial position	561,6	34,5%	974,0	39,6%	412,4	*73,4%*
Total sources of financing	**1.625,8**	**100,0%**	**2.457,5**	**100,0%**	**831,7**	**51,2%**

The net capital employed increased as at 31 December 2005 by Euro 831.7 million, from Euro 1,625.8 million to Euro 2,457.5 million. The return on Investment (ROI) dropped from 10.9% in 2004 to 8.8% in 2005, due to the merger of the Modena-based company, the impact of the rise in net working capital and the consistent number of investments made.

The non-current asset/liability balance, which in 2004 takes into account the reclassification of the provision for deferred tax liabilities, has dropped by Euro 57.9 million, chiefly due to the change in this provision, arising above all from the acquisition of the Modena area.

Tangible and intangible fixed assets as at 31 December 2005 amounted to Euro 2,401.2 million, up by Euro 739.7 million when compared with 31 December 2004, in relation to the merger of the Modena companies and the investments indicated in detail in the following section.

The net working capital, which in 2004 changed in relation to the above-mentioned reclassification, rose from Euro 113.1 million to Euro 322.0 million, mainly in relation to the billing problems linked to the start-up of the new customer computerised information system during the period. It should be noted that with respect to 30 September, the situation has progressively stabilized despite the Modena consolidation, the rise in the cost of raw materials and the seasonal trend which increased the turnover.

Provisions increased, not only due to the merger of the Modena companies and the normal provision made to the Provision for Employee Leaving Indemnities (TFR), but also mainly as a result of:

- the provision of the portion of post-closure costs for landfills;

- the provision of the portions for restoring the networks and plants granted under use to the Group and owned by the companies spun-off (asset companies).

The shareholders' equity, which rose from Euro 1,064.2 million to Euro 1,483.5 million, includes the share capital increase of 176.9 million shares, relating to the inclusion within the shareholding structure of the Municipal authorities associated with the Modena integration operation.

In relation to the afore-mentioned share capital increases, the net financial position passed from Euro 561.6 million as at 31 December 2004 to Euro 974.0 million at the end of 2005.

By way of supporting the increase in debt, during the first few months of 2006 the Group issued a bond totalling Euro 500 million, which made it possible to obtain a higher ratio between medium/long-term debt and short-term debt.

The reliability of the Group's economic and equity structure is validated by the confirmation by Standard & Poor's of an A+ rating over the long-term and by the concession by Moody's of an A1 rating. Shareholders should note that the Hera Group is the only one of the Italian multi-utility companies with this level of rating awarded by the two leading rating agencies.

A detailed analysis is presented below

	31 Dec. 04	*31 Dec. 05*
Non-current securities and other financial receivables	18.9	53.4
Bank payables – long-term	(489.0)	(521.4)
Sums due to other financial institutions (leasing IAS 17)	(28.7)	(39.9)
Financial derivatives		(15.8)
Medium/long-term debt	**(498.8)**	**(523.7)**
Other financial receivables/payables	(1.2)	(1.2)
Bank payables – short-term	(268.1)	(636.8)
Cash in banks and on hand	172.4	189.1
Sums due to other financial institutions (leasing IAS 17)		(9.8)
Current financial assets	34.5	8.4
Net short-term debt	**(62.8)**	**(450.3)**
Total net debt	**(561.6)**	**(974.0)**

Investments

The tangible and intangible investments of the Group, inclusive of the increase in leased assets dealt with by applying the IAS standards, amounted to Euro 276.9 million, as against Euro 225.4 million last year, posting a 22.4% increase.

Investments made during 2004 are analyzed below by business area.

Total Investments

(Euro millions)	31 Dec. 04	31 Dec. 05
Gas area	23.4	38.2
Electricity area	3.8	3.9
Integrated water cycle area	67.1	68.1
Waste management area	42.2	81.2
Other services	29.4	21.9
Central structures	59.5	63.7
Total	225.4	277.0

The gas service investments within the area it operates in, mainly refer to extensions, reclamation and enhancement work on the networks and plants and are in line with the same period last year, the area of consolidation being the same. The investments made by the company Medea concern the second section of the work for the methane conversion of Sassari. Plant purchases were made during 2005 for a total of Euro 16.3 million.

Gas

(Euro millions)	31 Dec. 04	31 Dec. 05
Territory	18.1	18.1
Medea	5.3	3.8
Plant acquisitions		16.3
Total Gas	23.4	38.2

The Electricity service investments referred in part to the extension of the service and to the extraordinary maintenance of the plants located within the Imola area (Euro 2.9 million) and in part (Euro 1 million) they concern the Imola co-generation plant currently under construction.

Electricity

(Euro millions)	31 Dec. 04	31 Dec. 05
Territory	2.3	2.9
CCGT	1.5	1.0
Total Electricity	3.8	3.9

As in the previous year, the investments mainly refer to extensions, reclamation and enhancement work on plant. In the sewerage sector, there was an increase in the Bologna area, due to the increase in the number of municipalities served.
The work performed was scheduled and agreed with the pertinent ATOs (Area Water and Waste Authority Agencies).

Integrated water cycle

(Euro millions)	31 Dec. 04	31 Dec. 05
Aqueduct system	43.2	41.3
Purification system	13.4	12.9
Sewerage system	10.5	13.9
Total water cycle	67.1	68.1

In the Waste Management area, the considerable increase in measures carried out by investee companies is attributable to the measures financed by means of leasing on the plants of the Ravenna Ecologic Environmental Centre (Euro 16.1 million) and Akron (Euro 7.9 million). The investments on the waste-to-energy plant at Bologna (FEA) concerned work for the completion of said plant, while the Euro 13.2 million spent on the waste-to-energy plant at Canal Bianco concern the start-up of the work relating to the construction of the new waste incineration line.

Waste management

(Euro millions)	31 Dec. 04	31 Dec. 05
Territory	11.3	12.0
Investee companies	16.5	33.4
FEA	12.3	20.0
WTE Canal Bianco	1.1	13.2
Other WTE	1.0	2.6
Total Waste management	42.2	81.2

District heating service investments mainly concerned extension work on the service in the Bologna (Euro 5.2 million), Ferrara (Euro 2.9 million) and Imola (Euro 2 million) areas. Telecommunications investments referred to continuation of the creation of the Regional Telematic interconnection Plan via fibre optics. In the public lighting field, investments concerned the installation of new lighting units and the extraordinary maintenance of the existing ones. The investments concerning other services were down considerably and mainly refer to cemetery services and the management of heating plants.

Other services

(Euro millions)	31 Dec. 04	31 Dec. 05
DH	8.9	10.6
TLC	9.8	3.9
Public lighting	2.8	1.6
Other	7.9	5.8
Total other services	29.4	21.9

Once again during 2005, the considerable commitment continued for the bringing onto stream of the corporate information system with particular reference to the SAP-ISU system and the related interfacing with SAP-R3; the increase with respect to the previous year is partly due to the need for integration with the Modena SAP information system. The increase in buildings was affected by the work relating to the rationalisation and standardisation of the spaces. Within the sphere of other investment, purchases of vehicles and containers took on particular importance (Euro 20 million), mainly finalized at achieving the limits of differentiated waste collection envisaged by current laws and by the agreements with the pertinent ATOs.

Structures

(Euro millions)	31 Dec. 04	31 Dec. 05
Buildings	5.5	7.4
Information systems	24.4	33.0
Other investments	29.6	23.3
Total	59.5	63.7

3.01.02.02 Regulatory Framework

1 - Energy: evolution of the legislative framework

The reference framework of legislative and regulatory evolution in the energy markets has been heavily conditioned by international circumstances and in particular by the strong rise in the price of raw materials and by the Russian-Ukrainian crisis concerning the transit of natural gas from the cultivation and extraction sites to the Western European consumption terminals. This contingency has further emphasised the insufficiencies already apparent in the raw material importation and storage infrastructures, which contribute to the difficulties in transition from the Italian system to an accomplished market model.

The warning level reached in the winter of 2005-2006 in the natural gas procurement policy, which coincided with peak winter consumption and the Ukrainian crisis, has in fact brought the issue of the structural deficiencies in the Italian system to the fore, disproving the fears of an alleged overabundance of future infrastructures arising from the simultaneous pursuit of numerous gas pipeline and GNL plant construction projects.

The limited storage capacity available, which was put to the test by the crisis which arose in the last months of the winter 2004/2005, when it proved necessary to interrupt supply to the uninterruptible customers, to maximise importation and to avail of strategic stockpiles, led the Authority to bring to Parliament's attention the risk of a crisis which was repeated, and exacerbated by the absence of international supplies, between late 2005 and early 2006.

In August 2005 the Authority identified the "outsourcing" of the management of underground storage and the expansion of said storage, as the key elements by which to raise the safety margins of the Italian system for management of consumption peaks. This proposal forms part of a package of measures put forward by the Authority in January 2005 and aimed at encouraging competition and expansion of the Italian procurement system (amongst which, the reduction of the share held by Eni in the share capital of the Snam Rete Gas (SRG) by at least 5%, the simultaneous contribution to SRG of the international transport assets currently under Eni's control, Eni's withdrawal from STOGIT's share capital and the subsequent possible merger of STOGIT with SRG, as well as disposal to third parties of part of Eni's long-term importation contracts).

At the end of legislature Parliament released the conclusions of the investigative inquiry, furthered by the X Permanent Commission of the House of Commons, on the evolution of the domestic energy market.

Referring to the conclusion of previous inquires conducted by the Italian Authority for Electricity and Gas and the Italian Anti-Trust Authority, which had recognised that the enduring oligopolistic structure of the markets which are "upstream" in the energy chain represented an obstacle to the process of liberalisation, the X Commission observes, with regard to the natural gas market, that the current limited importation capacity may be attributed "to a strategy of limiting supply implemented over the last years by the dominant operator" and recognises the urgent need to accomplish the scheduled 15% increase in the importation capacity attributable to expansion of the TAG-TTPC infrastructures, expressing the hope that the "third party independent" operators may play a decisive role in managing the additional capacity.

However the ensuing legislation appears to have reacted in a contradictory manner to the recommendations provided by the sector's regulatory authorities and by Parliament itself. On one hand the law decree has favoured competitiveness by simplifying the authorisation procedures for construction and expansion of GNL terminals, on the other hand the regulations introduced at the end of 2005 (financial bill and the so-called "thousand extensions" decree) have extended from 2007 to 2008 the term within which Eni must reduce its interest in Snam Rete Gas to less than 20%.

Integration of Environmental Aspects in the Energy Market

The adoption of imported applicative orders of primary legislation in favour of the integration of environmental aspects in the rules governing the functioning of the energy markets has contributed to the definition of the current state of renewable sources incentive programmes and to Italy's definitive subscription to the European emission rights market.

Of particular importance is the ruling arising from Law no. 239 of 23 August 2004 (reorder of the energy markets, known as the "Marzano Law") and from Legislative Decree no. 387 of 29 December 2003 (assimilation of the EU laws concerning renewable sources incentive programmes in the domestic energy market).

- In implementation of the provisions of the framework law for reorder of the energy markets, the Italian Authority for Electricity and Gas passed an important resolution, no. 34/2005, which establishes the incentives to withdrawal of electricity produced by renewable sources plants and by smaller sized plants powered by alternative sources. The Ministry of Productive Activities, working with the Department for the Environment, has issued decrees for implementation of regulations which provide for assignment of "green certificates" to co-generated thermal energy distributed through district heating networks.
- In accordance with the provisions of Legislative Decree 387/2003 the decree introducing "Criteria for incentives to the production of electricity through photovoltaic conversion of solar energy" has been approved. Said decree provides for economic contributions for the construction of photovoltaic plants with nominal power of no less than 1 kW and no more than 1,000 kW connected to the electricity grid, for the concession of which AEEG (the Italian Authority for Electricity and Gas) and GRTN (the National Transmission Grid Operator) have prepared the appropriate applicative regulations and launched the selection procedure. Legislative Decree 387/2003 has provided the base for other important legislative provisions, approved in the second half of 2005, which define the framework of incentives for energy produced by waste combustion and by biomass (with the period of recognition of the green certificates being extended by four years, but with application of a quota of 60% of the energy introduced to the network).
- Definition of the rules governing the functioning of the organised market of energy efficient securities (TEE) by the GME (Electricity Market Operator), in association with the AEEG, completed the legislative process prescribed by the decrees of 20 July 2004 which imposed obligatory objectives of energy intensity reduction on the distributors of electricity and natural gas. March 2006 saw the formal start of the exchange of energy efficiency certificates on the

electronic platform set up by GME; the market's effective launch was hindered by delays in certification of the securities.

- Publication in Official Gazette no. 57 of 9 March 2006 of the Decrees of 6 February and 23 February 2006 (respectively concerning the recognition of authorisation to emit greenhouse gas and the issue of the CO_2 quotas for the 2005-2007 period) concluded the process for approval of the national plan for allocation of allowances provided for by Directive 2003/87/EC. The final consent for assignment of certificates to approximately one thousand authorised entities was received from the European Commission on 23 February 2006. The GME subsequently ordered the launch of the exchange of certificates on the market platform.

1.1 - Electricity: regulations and tariff framework

During 2005 and in early 2006 some important orders for integration of the regulatory framework governing the electricity market were adopted. With resolutions 298 and 299 passed on 29 December 2005 in particular, the Authority respectively implemented repeal of the "Ct" parameter (at the base of the regulation of significant economic relations for entities operating in distribution) and updated the reference parameters for the definition of electricity tariffs in the 1st quarter of 2006.

The early months of 2006 saw the launch of the procedure for revision of the transmission and dispatchment code, which will also take into account the corporate transformations experienced by the national transmission company. Further to unification of the ownership and management of the national transmission grid, pursuant to Prime Minister's Decree of 11 May 2004, some regulation and control functions have been split off and assigned to a new legal entity, the Gestore del Sistema Elettrico (the Electricity System Operator), which began operations in November 2005.

Regulation of distribution tariffs is still conditioned by the litigation relating to the Code containing the provisions for electricity (resolution 5/2004) and in particular to the procedure for recognition of specific company equalisation (resolution no. 96/2004). Some operators disputed the ban on use of the acquisition price (for example, of former Enel business units) in the valuation of assets remunerated for the purposes of recognition of greater company costs which give rise to a positive specific equalisation. A preliminary ruling of the administrative court (TAR of 13 May 2005), which was partially favourable to the plaintiffs, was contradicted on appeal by the State Council. While awaiting the outcome of this judicial issue, the Authority has recommenced analysis of the positions of the entities which had requested recognition of the specific company equalisation which had been suspended following the May 2005 ruling. The CCSE (Electricity Equalisation Fund) has received mandate from the Authority to analysis the documentation sent by the companies that did not avail of "historical" stratification of the value of assets, also on the basis of the conclusions of special studies fostered by the Authority in association with the CCSE and partly performed at the companies concerned.

1.2 – Natural Gas: regulations and tariff framework

While the regulatory and tariff framework of the "upstream" segment has achieved relative stability (resolutions 166 and 179 have respectively established the criteria for the economic considerations and approved the transport tariffs for the 2005-2008 regulatory period, while resolution 168 has brought approval of the new criteria for re-gasification tariffs), the natural gas distribution and sales sectors have been heavily conditioned by the litigation ensuing from the introduction of the new criteria for the determination of distribution tariffs for the 2004-2008 period (resolution 179/2004) and of new rules for the revision of the variable consideration relating to wholesale marketing (resolution 248/04, the principles of which were reiterated at the end of 2005 with resolution 298).

Further to judgment no. 531 of 11 March 2005, with which the Lombardy Regional Administrative Court (TAR) partially annulled resolution no. 170/04, the Authority launched the procedure for revision of the tariff regime. Said procedure led to the approval of resolution no. 122/05, through which operators are awarded remuneration of the investments which were not considered by the previous resolution no. 179/04. The Authority is expected to take further action with regard to the other main aspect of the dispute, that is, the quantification of the recovery of productivity (established as 5% p.a. of the entire sum of the operating costs and depreciation/amortisation during the full regulation period), for which even the appeal judges partially admitted the plaintiffs' observations.

On 28 June 2005 the Lombardy TAR also annulled the aforesaid resolution 248/04, by which the Authority had ordered reform of the mechanism of revision of the "raw materials" tariff component (in particular reviewing the reference basket of oil products, the price of which determines the revision and the algorithm for transfer of the international crude oil price trends to the tariff) with the aim of neutralising the effect of the substantial increases in oil prices.

The resolution also contained a mechanism for transfer to the importers/wholesalers of the losses sustained by the sellers who were not able to renegotiate the disparity between the sales prices, adjusted on the short-term, and the procurement costs (which can only be adjusted at intervals of no less than one year).

The order, which affected the method of adjustment of the costs of raw materials, would have limited the tariff increase passed at the end of 2004 to 2%; in the absence of this intervention, the tariff increase would have amounted to 3.7%, equivalent to an average cost increase of €29 p.a. for consumers.

In October 2005 the Authority obtained suspension of the referenced TAR sentence related, however, solely to the appeal presented by Hera Trading (the "Hera Trading Case") from the State Counsel. Hera Trading, currently without end user clients in its portfolio, was not impacted by this sentence. The Authority then proceeded to reiterate the criteria for tariff updates as per Resolution 248/04 in a new provision (Resolution 298 dated December 29th, 2005) in order to prevent any additional increases in final prices. The same resolution 298/05 was, in the end, suspended by TAR as it awaited the final sentence related to the appeal involving the previously mentioned Resolution 248/04.

On March 21st, 2006 the State Counsel sustained the Authority's appeal for the annulment of the first degree sentence related, once again, solely to HERA Trading. In regard to the annulments requested by the other operators, these are still pending and the discussion of same with the State Counsel should take place next June 6th, the date in which the case related to *Gas delle Concordia* (which, in light of the lengthy appeal process, should result in the passage of the annulment of the Lombardy TAR sentence into final judgement) will also be discussed .
While waiting for definitive resolution of the case, the companies selling to end user clients have opted to base the "raw materials" component of tariffs on the provisions of the current norms (specifically Resolution 195/2002), for both 2005 and first quarter 2006.

On March 28th, 2006 the Authority issued three new resolutions (63/06, 64/06, 65/06) that, in addition to updating fuel prices for the period April – June 2006, introduced criteria and indications that confirmed the operators' expectations regarding the presumed neutrality of Resolution 248/04 and the regulated tariffs applied to end user client sales, as well as the willingness of the Authority itself to re-examine, as part of a specific investigation, the mechanisms applied to the updating of fuel prices provided for in Resolution 248/04 and to introduce instruments designed to safeguard the operators that "manage the natural gas supply through specific negotiations" (Hera Trading, based on the gas release contracts stipulated in 2004, is considered one of these operators).

In regard to any provisions related to 2005 volumes, and in relation to which the State Counsel should rule on the future efficacy of Resolution 248/04, at present the Authority's provisions contained in Resolution 65/06 refer solely to account margins (0.276 Euro cents/mc) that, given the difficult of retroactive application, are applicable solely to volumes sold in second quarter 2006.

In light of the above, the annulment of Resolution 248/04 issued by the Lombardy TAR currently in force and the content of the recent resolutions issued by the Authority mentioned above, the Group has decided not to proceed with any balance sheet provisions or coverage of the possible impact on P&L resulting from application of the above mentioned norms.

2 – Local Public Services: changes in the regulatory framework

On 10 February 2006 the Cabinet definitively approved the draft legislative decree containing the "Environmental Regulations", thus exercising the authority attributed thereto by Law no. 308 of 15 December 2004 which assigned the Government the responsibility for reforming, reorganising and rationalising the entire regulatory framework (waste management, territory and water protection, assessment of environmental impact, large-scale combustion plants) also through assimilation in the Italian order of other directives including the EU framework directive on the protection and management of waters.

The legislative decree on environmental issues, which has not yet been published in the Official Gazette as it has yet to be signed by the President of Italy, assembles, in 318 articles, the provisions previously distributed in special draft decrees relating to various issues covered by the

delegated authority (waste management, earth and reclamation, waters, air quality, environmental impact assessment).

The new legislation introduces important new aspects especially with regard to municipal waste management, for which new criteria of assimilation have been provided in addition to the possibility, under certain conditions, of removing substantial portions of materials conventionally included in the integrated management cycle, if these may be directly recycled in the production process (so-called "secondary prime materials"). The economic and organisational implications are not yet clear and must also be assessed in relation to the secondary legislation of the Government itself and of the local authorities.

The management model which prevails in Emilia Romagna, on the basis of which Hera undersigned the Convention for the management of services, is not called into dispute by the new regulations. While, for example, the legislative decree provides for the obligatory introduction of tenders (by 2006) for selection of integrated operators, it does not repeal the provisions which legitimate the existing assignments (above all, Article 113 of the Consolidation Act of local authorities as reformed by the 2004 finance bill). Hence the public selection procedure is strictly requested for the new assignments.

Among the changes for the waste sector, attention is drawn to the obligation to phase out the tax regime in favour of the application of an environmental hygiene tariff.

The fact that the Regions and local authorities have raised some objections, including appeals to the Constitutional Court for the cases of alleged breach of the distribution of competences and for exceeding delegated authority, leads us to believe that the procedure to enact this legislation shall be taken up again in the next legislature; the very coherence of the definition of "waste" (upon which is based the regulatory framework of the articles pertaining to the management of environmental services) with the community notion, consolidated by the directives and decisions of the court, is doubtful and shall certainly be the subject of jurisprudential intervention. However this does not exonerate the entities and operators from applying the part of the regulations that will be immediately compulsory when the legislative decree will become final state law with publication in the Official Gazette.

During 2005 the grounds for dispute between State and Regions over the attribution of legislative and regulatory powers pertaining to the organisation of local services were manifold. With judgment no. 335 of 27 July 27 2005 the Constitutional Court issued its decision on the ruling of constitutional legitimacy proposed by the Prime Minister in relation to some articles of the Emilia Romagna Region Law No. 7 of April 14, 2004, containing provisions on environmental matters. The government specifically contested the attribution at regional level of the regulatory power in the matter of tariffs; in rejecting the appeal, the Supreme Court confirmed the legitimacy of the regulations made by the regional legislator.

The consequences of the judgment are still not clear. The Court confirmed the supremacy of the State's competence for the substantial part of the tariff regulatory activity which is necessary to the protection of competition and, at the same time, recognised that for the part which does not relate to the protection of competition (of exclusive state competence, where not that of the European Community) the competence of the Region must be admitted.

A balanced reading of the judgment leads us to believe that, although it confirms the State's power to "guide" and where appropriate, standardise the tariff systems as a safeguard to a balanced and competitive economy, it allows the Regions sufficient flexibility to introduce to the regulations tariff variants and aspects not attributable to competition, such as the protection of the environment and service quality incentives.

In the same judgment the Constitutional Court also ruled against another regulation approved by the Emilia Romagna Region, which introduced an additional tax for the conferment to landfills of solid urban waste. For this matter the Court deemed that the Region did not have the right to intervene on an important taxation matter and one strictly attributed the powers to the State.

2.1 – Regulation and Local Tariff Framework

2005 saw completion of the process for definition of the convention-based relations between Hera, in its capacity as safeguarded operator, and the local Agencies (ATO) in compliance with the provisions of the Emilia Romagna Region law pertaining to regulation of local public services.

Hence, to date Hera manages the urban hygiene services and the integrated water services in six areas corresponding to six provinces (Bologna, Ferrara, Forlì-Cesena, Modena, Rimini and Ravenna). The relative conventions cover the exclusive management of the services for a period which varies between 10 years for environmental services and approximately 20 years for water services. The conventions are accompanied by annexes containing tariff scheduling documents which establish the development of considerations, for the services concerned, for periods of at least three years. Definition of the tariffs for the subsequent period of regulation is on hold until the environmental services in the municipalities which still apply the taxation method TARSU have completed passage to tariff-based methods, and hence should take place at the end of the first period of assignment. It is however possible that the parties will agree to implement tariff revisions during the first three-year period in the face of particular events or significant variations in the quantity and quality of the services managed.

Despite the fact that the CIPE (Interdepartmental Committee for Economic Planning) did not intervene in the last revision of the water tariffs (applying to the 2003-2005 period) prior to full application of the normalised method, the latter has already been applied in the areas under Hera's management.

Any variations to the legislative and regulatory framework, prescribed by the legislative decree concerning environmental issues, should not come into effect prior to conclusion of the first tariff period governed by the Conventions in force. The amendment to the normalised tariff method introduced by the Galli law, replaced by said decree, in fact requires secondary law-making which is not likely to not take place before 2007.

3.01.02.03 Tariffs

1 Gas Distribution: tariff framework

2005 was a year of great uncertainty for the tariff system governing the distribution of gas. In particular the second regulatory period, which began in October 2004 (AEEG Resolution 170/04), provided for a reduction of the remuneration of invested capital from the 8.8% of the previous period to 7.5% and a scheduled recovery of productivity equal to 5% applied only to the operating costs and to technical amortisation of recognised capital (in line with the impact generated by the scheduled recovery of profitability provided by the previous regulatory period).

In February 2005 the TAR of Lombardy accepted the appeal filed by some distributors and suspended resolution 170/04. AEEG applied to the Council of State which, while waiting to examine the reasons for the TAR suspension, ruled in favour of a solution of continuity in the application of the reference tariff regime and decreed the suspension of the TAR judgment and the consequent application of resolution 170/04. In August 2005 AEEG issued resolution 122/05 which admitted part of the motions filed in the appeal. On the base of said resolution the tariffs for gas year (GY) 04/05 were defined as were those for GY 05/06. The tariffs for GY 04/05 are currently undergoing approval while, as far as the tariffs for GY 05/06 are concerned, further resolution is expected from AEEG which will assimilate the indications of the Council of State aimed at inducing a reduction of the scheduled recovery of productivity and accordingly the subsequent definition of the GY 05/06 tariffs.

Hence Hera's Financial Statements 2005 reflect the effects of Resolution 122/05 and subsequent rulings.

Against this tariff backdrop the revenues from gas distribution in 2005 were equal to approximately Euro 108 million -4.9% v 2004) with distributed volumes equal to approximately 2 billion m^3 (+5.6% v 2004) with an average unitary tariff of 5.3 €c/m^3.

Gas Distribution	2004	2005	% change
Hera			
- Revenues €/m	113.3	107.7	-4.9%
- Volumes m^3/m	1912	2019	5.6%
- Average tariff (€c/m^3)	5.9	5.3	-10.0%

Hence the year 2005 featured a 10% decrease in average unitary tariffs chiefly due to the tariff revisions induced by the AEEG resolutions 170/04 and thereafter.

2. Electricity Distribution: tariff framework

For the tariff system governing electricity distribution, 2005 was the second year of the current regulatory period *and hence represented a year of considerable tariff stability which saw consolidation and full application of the principles ratified by AEEG resolution 5/04 and namely:*

- *the removal from the distribution tariff for customers with uses other than domestic of the components relating to the services of transmission, metering and marketing, transferred to the sales tariff and applied on the customers of the restricted market (with considerable perimeter variation of the tariff in 2004);*
- *the launch of the general standardisation of revenues, obtained by the application of the D2 and D3 tariffs to domestic customers, using, as reference the D1 tariff;*
- *the transfer to the sales portion of the component covering the costs of dispatchment, activity which, with the launch of the electricity exchange, is performed by Acquirente Unico:*
- *a scheduled productivity recovery level (X-factor) equal to 3.5% pa. for distribution and 2.5% p.a. for transmission.*

Against this tariff backdrop the revenues from electricity distribution in 2005 were equal to approximately Euro 9.9 million with distributed volumes equal to approximately 544 Gwh with an average unitary tariff of 1.8 €c/kwh.

Electricity Distribution	2004	2005	% change
- Revenues €/m	10.0	9.9	-1.0%
- Volumes Gwh	536	544	1.5%
- Average tariff (€c/kwh)	1.9	1.8	-2.5%

Hence the year 2005 featured a 2.5% decrease in average unitary revenues.

3. Integrated Water Cycle: tariff framework

January 2005 saw the new tariffs agreed with the ATOs for the period 2005-2007 enter into effect. The new tariff was the first step towards tariff convergence which will lead to full application of the normalised method.

Against this backdrop Group revenues from integrated water cycle management for 2005 were equal to approximately Euro 263.1 million with water system volumes sold equal to approximately 201 million m^3 with an average unitary tariff of 1.31 €/m^3.

Water Cycle	2004	2005	% change
- Revenues* €/m	256.1	263.1	3%
- Volumes** m^3/m	203	201	-1%
- Average tariff (€c/m^3)	126	131	4%

* Inclusive of the "piani stralcio" quota for 2004
** Adjusted by intercompany items

In comparison with 2004 revenues have increased by 3% with volumes sold down by 1%. Hence the year 2005 featured a 4% increase in average unitary tariffs arising from a combination of two effects:

- +3% for the effects arising from application of the tariff increase agreed with the ATOs;
- +1% for the effect of completion of the water cycle in the municipalities where the water system and purification services were provided but not the sewerage service.

4. Urban Hygiene: tariff framework

In 2005 the urban hygiene service was provided to 135 Municipalities in a context characterised by completely disparate application of the Ronchi Decree. Stipulation of the conventions with the ATOs, which was scheduled for 2004, was concluded in 2005.

In this context 2005 as characterised:

- by the application of the tariff only in 28% of the municipalities served, corresponding to 42% of the population served (all of the Regional capitals with the exception of Bologna have already changed to tariffs), in line with the situation of the last two years;
- by the presence of vastly disparate situations of application of the normalised method for the determination of the revenues which led to significant gaps between expected and actual revenues.

Against this backdrop Group revenues from urban hygiene management for 2005 were equal to approximately Euro 242.7 million with average revenues per served inhabitant equal to 125 €/inhabitant.

Urban Hygiene	2004	2005	% change
- Revenues €/m	236.8	242.7	2.5%
- Served inhabitants ('000)	1,930	1,949	1.0%
- Average unitary revenues (€/inhabitant)	123	125	1.5%

In comparison with 2004 revenues increased by 2.5% with a 1% increase in population, giving rise to an increase in average unitary revenues per served inhabitant equal to 1.5%.

3.01.02.04 Analysis by Business Area

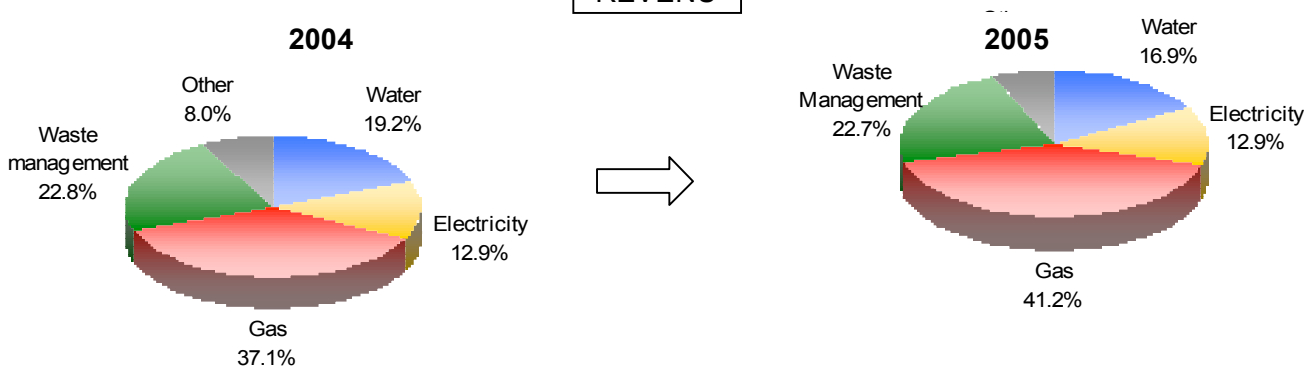
An analysis is presented below of the operating results achieved in the business areas in which the Group operates: (i) sector concerned with the distribution and sale of methane gas and LPG; (ii) sector concerned with the distribution and sale of Electricity, (iii) Integrated Water Cycle sector (Aqueducts, Purification and Sewerage), (iv) Waste Management sector (waste collection and treatment) and other activities (District Heating, Public Lighting, Heat Management and other minor services).

The analysis by business area highlights the increased importance of the Waste Management business area which in terms of contribution to EBITDA has become the most important Group business area, surpassing the Gas area which predominated in 2004..

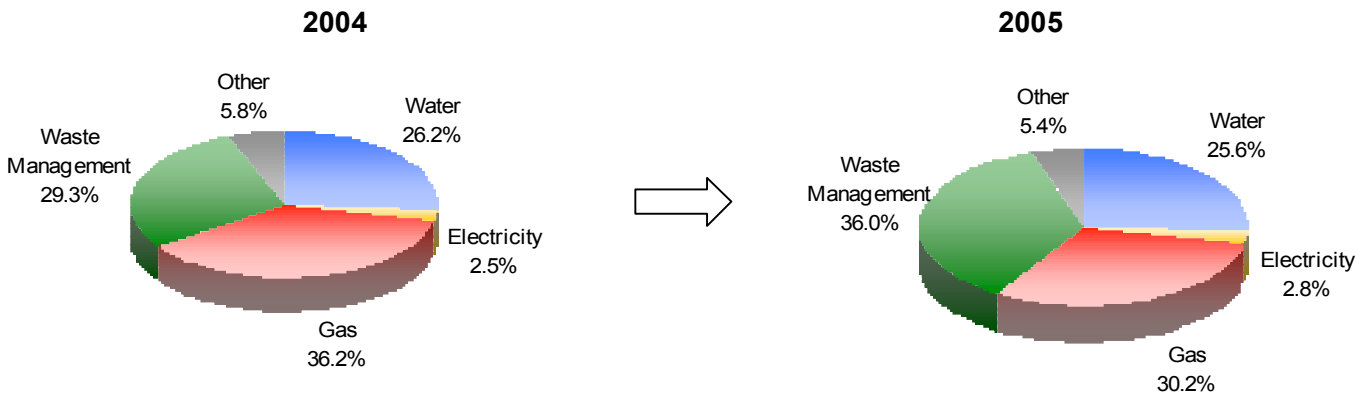
In order to provide more detailed information on the 2005 results, an analysis is shown of the business areas in which the Group operates. The composition and evolution for 2004-2005 in terms of Revenues and EBITDA are shown in the graphs below:

COMPOSITION OF THE BUSINESS PORTFOLIO

REVENU



EBITDA



The following sections contain an analysis of the operating results generated by business area. The income statements by business area include structural costs, including inter-divisional transactions valued at current market prices.

It should also be noted that the analysis of the business areas includes the increases in construction on a time and materials basis/work in progress and, therefore, the related costs. This item, as envisaged in the indications of the IAS standards, is indicated by way of adjustment of the costs as costs capitalized in the individual tables.

Gas Area – Distribution and sales activities

Importance of the Gas business for the Group

The importance of the Gas business in 2005 decreased, in line with forecasts, by more than 5 percentage points in favour of the other areas of the Group's business, as a result of the lower profitability of the sector and the increase in the importance of the other areas, in particular that concerning Waste Management. This trend has confirmed the validity of the Hera multi-business model which makes it possible to offset any contrasting trends in the individual areas.

The importance of this business area with respect to total Group activities is illustrated below:

(mln/€)	31-Dec-04	31-Dec-05	Change	Change %
Ebitda	**106.0**	**97.0**	**(9.0)**	**-8.5%**
Group Ebitda	292.5	321.0	28.5	+9.8%
Percentage	*36.2%*	*30.2%*	*-6.0 p.p.*	

Results during the year in the Gas business

During 2005, this business area, involved in the distribution and sale of gas, was that which underwent the greatest changes when compared with last year. The main elements to be taken into account when evaluating the results are:

- the elevated increase in the cost of raw materials, deriving from the high level of oil prices, which caused heavy price tensions and greater attention towards consumption by customers: greater revenues were generated together with a consistent reduction in the percentage margins;
- the increase in the unit price (+ 20% on average), which encouraged and accentuated the commercial aggressiveness of competitors, in particular with regards to business customers and in the main metropolitan areas, involving a contained loss in margins;
- the favourable climate trend during the last two months of 2005 when led to sales rising by more than 10% in volume on the same period last year;
- the measures of the Authority for Electricity and Gas on distribution which, as illustrated in the related section, established an important reduction of the tariffs thereby causing a corresponding loss in margins;
- the intense trading and import activities carried out by the Group which made it possible to partially offset the lower sales margins on the end market.

The results are summarized below:

Income statement (mln/€)	**31-Dec-04**	**Incr.%**	**31-Dec-05**	**Incr.%**	**Change**	**Change %**
Revenues	589.8		756.6		166.8	+28.3%
Operating costs	(466.2)	-79.1%	(644.9)	-85.2%	(178.7)	+38.3%
Personnel costs	(35.0)	-5.9%	(37.5)	-5.0%	(2.5)	+7.1%
Capitalized costs	17.4	3.0%	22.8	3.0%	5.4	+30.9%
Ebitda	**106.0**	**18.0%**	**97.0**	**12.8%**	**(9.0)**	**-8.5%**

Revenues in the Gas area rose by 28.3%, passing from Euro 589.8 million to Euro 756.6 million, due to the rise in the cost of raw materials, transferred onto the sale price, and the increase in the volumes sold (for a total of around Euro 130 million), and greater trading activities which contributed by approximately Euro 50 million.

The change in revenues was also effected by the negative change in distribution tariffs, which fell on average by 10%, passing from 5.9 to 5.3 €/cents on average per cubic metre, involving an overall impact of more than Euro 11 million.

Compared with the previous year, the Group reported an increase of 5.6% in volumes distributed, which rose from 1,912 to 2,019 million cubic metres, and an increase in those traded for sale of 18.3%, from 2,062 to 2,439 million cubic metres, as shown in the table below:

Dati Quantitativi	**31-Dec-04**	**31-Dec-05**	**Var. Ass.**	**Var. %**
Number of customers (thousand units)	798.6	792.5	(6.1)	-0.8%
Distributed volumes (million of cm)	1,912.0	2,019.2	107.2	+5.6%
Volumes sold (million of cm)	2,062.0	2,438.7	376.7	+18.3%
- of which Trading	*176.0*	*447.6*	*271.6*	*+154.3%*

The number of customers served reached almost 940 thousand units; the trend is illustrated in the following table:

31 Dec. 2004	Customers lost	Inherent growth	31 Dec. 2005
798.6	-16.7	+10.6	792.5

(Customer No. in thousands)

The EBITDA dropped from Euro 106.0 million to Euro 97.0 million (-8.5%), involving a decreasing percentage-based incidence of 5.2 percentage points, passing from 18.0% in 2004 to 12.8% in 2005.

Electricity Area – Distribution and sales activities

Importance of the Electricity business for the Group

(mln/€)	31-Dec-04	31-Dec-05	Change	Change %
Ebitda	**7.3**	**9.1**	**1.7**	**+23.7%**
Group Ebitda	292.5	321.0	28.5	+9.8%
Percentage	*2.5%*	*2.8%*	*+0.3 p.p.*	

The Electricity area is a sector considered to be strategic by the Group, since it makes it possible to complement and defend the sale of gas to customers in the area the Group operates in; with the Modena integration, these activities, besides more than doubling their percentage-related importance, were further enhanced in March 2006, by means of the acquisition of the former Enel network in the Province of Modena

Results during the year in the Electricity business

The improvement in the income statement figures for this area is highlighted in the table below which, it must be remembered, does not take in account the effects of the integration of the Modena-based company:

Income statement (mln/€)	31-Dec-04	Incr.%	31-Dec-05	Incr.%	Change	Change %
Revenues	205.0		236.4		31.4	+15.3%
Operating costs	(198.2)	-96.7%	(228.0)	-96.5%	(29.8)	+15.0%
Personnel costs	(2.7)	-1.3%	(2.2)	-0.9%	0.5	-18.1%
Capitalized costs	3.3	1.6%	2.9	1.2%	(0.4)	-11.4%
Ebitda	**7.3**	**3.6%**	**9.1**	**3.8%**	**1.7**	**+23.7%**

The revenues in the Electricity area increased by 15.3%, passing from Euro 205.0 million to Euro 236.4 million: this increase is due to the rise in the price of the raw material.

The breakdown of the revenues by type of customer is shown as follows:

(million Euro)	31-Dec-04	31-Dec-05	Incr.%	Change	Change %
Revenues from non-elegible customers/distribution	25.7	27.0	11.4%	+1.3	+4.9%
Revenues from elegible customers	176.0	206.5	87.3%	+30.5	+17.3%
Other	3.3	3.0	1.2%	-0.3	-9.9%
Total revenues	***205.0***	***236.4***	**100.0%**	***+31.4***	***+15.3%***

By contrast, the table below summarizes the main quantitative indicators of the electricity sector:

Dati Quantitativi	31-Dec-04	31-Dec-05	Change	Change %
Number of customers (thou. units)	**53.8**	**60.4**	**+6.6**	**+12.3%**
of which non-elegible/only distribution	49.7	50.4	+0.7	+1.5%
of which elegible	4.1	9.9	+5.9	+144.3%
Volumes sold (Gw/h)	**2,282**	**2,329**	**+46.5**	**+2.0%**
Non-elegible customers	196.0	189.5	-6.5	-3.3%
Elegible customers	2,086	2,139.0	+53.0	+2.5%

On a similar basis to the Gas sector, the electricity distribution tariffs, regulated by the AEEG, underwent a reduction of 2.5% on average during 2005 when compared with the previous year, passing from 1.866 to 1.820 €/cents per Kw/h.

The trend in raw material prices caused an increase in the prices of the liberalized market by nearly 25%, while the increase was lower by around 3 percentage points on the restricted market.

The EBITDA rose from Euro 7.3 million to Euro 9.1 million (+ 23.7%), involving a percentage-based increase, passing from 3.6% in 2004 to 3.8% in 2005. The growth in absolute terms derives from internal growth and margin recovery in commercial operations.

Integrated Water Cycle Area

Importance of the Integrated Water Cycle business for the Group

(mln/€)	31-Dec-04	31-Dec-05	Change	Change %
Ebitda	**76.5**	**82.1**	**5.6**	**+7.3%**
Group Ebitda	292.5	321.0	28.5	+9.8%
Percentage	*26.2%*	*25.6%*	*-0.6 p.p.*	

By means of the integration of the Modena area, the Group currently operates in the Integrated Water Cycle management sector in 170 municipalities with more than 2.3 million inhabitants, linked up to a network of approximately 24 thousand km and with more or less complete coverage of the area in question.

Hera operates in 6 ATOs coinciding with the Provinces of Ravenna, Ferrara, Forlì-Cesena, Rimini, Modena and Bologna.

Conventions were set up with all the afore-mentioned Agencies, regulating the Integrated Water Service and guaranteeing the Group not only the extension of the concessions on average until 2022, but also the certainty of the tariff development until the end of 2007 and the guarantee of achieving the anticipated return on investment, in accordance with the provisions of the so-called Galli law, when fully up and running as from 2008.

Results during the year in the Integrated Water Cycle business

An analysis of the operating results achieved in the Integrated Water Cycle business is shown below.

Income statement (mln/€)	31-Dec-04	Incr.%	31-Dec-05	Incr.%	Change	Change %
Revenues	304.9		310.5		5.6	+1.8%
Operating costs	(225.7)	-74.0%	(246.0)	-79.2%	(20.2)	+9.0%
Personnel costs	(65.7)	-21.5%	(67.2)	-21.6%	(1.5)	+2.3%
Capitalized costs	63.0	20.7%	84.8	27.3%	21.8	+34.5%
Ebitda	**76.5**	**25.1%**	**82.1**	**26.4%**	**5.6**	**+7.3%**

During 2005, revenues were generated for a total of Euro 310.5 million, compared with Euro 304.9 million in the previous year, up by 1.8%. This increase is due to the rise in tariffs and in services provided.

The following table summarizes the main quantitative figures of the business area:

Quantitative data	31-Dec-04	31-Dec-05	Change	Change %
Number of customers (thousand units)	800.1	780.7	(19.4)	-2.4%
Volumes sold (million of cm)				
acqueduct	203.0	201.0	(2.0)	-1.0%
sewerage	155.0	175.6	20.6	+13.3%
depuration	*181.0*	*181.7*	*0.7*	*+0.4%*

Customers in the water cycle sector exceed 800 thousand units and the average unit tariff of the integrated water cycle came to 1.29 € per cubic metre.

As far as volumes were concerned, aqueduct activities underwent a slight decrease (- 1.0%), purification was more or less stable (+ 0.4%), whilst sewerage activities increased by 13.3%. The greater growth of this last indicator reflects the acquisition of sewerage services in 11 new municipalities in the Bologna area, consequently involving the implementation of conventions with the area agencies.

In relation to the trend in volumes of water distributed by the aqueduct network, shareholders are reminded that 2005 experienced an extremely rainy Summer which particularly penalized the areas with high tourist flows. The impact of this climatic trend meant that more than 3 million cubic metres less were sold.

The 9.0% increase in operating costs, rising from Euro 225.7 million to Euro 246.0 million, is linked to the rise in both services managed, particularly in the sewerage area, and in work capitalized, which increased by approximately 35%. During 2005, a considerable increase was also noted in the cost of the electricity required for the water cycle's operating activities.

The EBITDA increased when compared to 2004 by 7.3%, from Euro 76.5 million to Euro 82.1 million, involving margins which rose by 1.3 percentage point, passing from 25.1% to 26.4% in 2005.

Waste Management Area

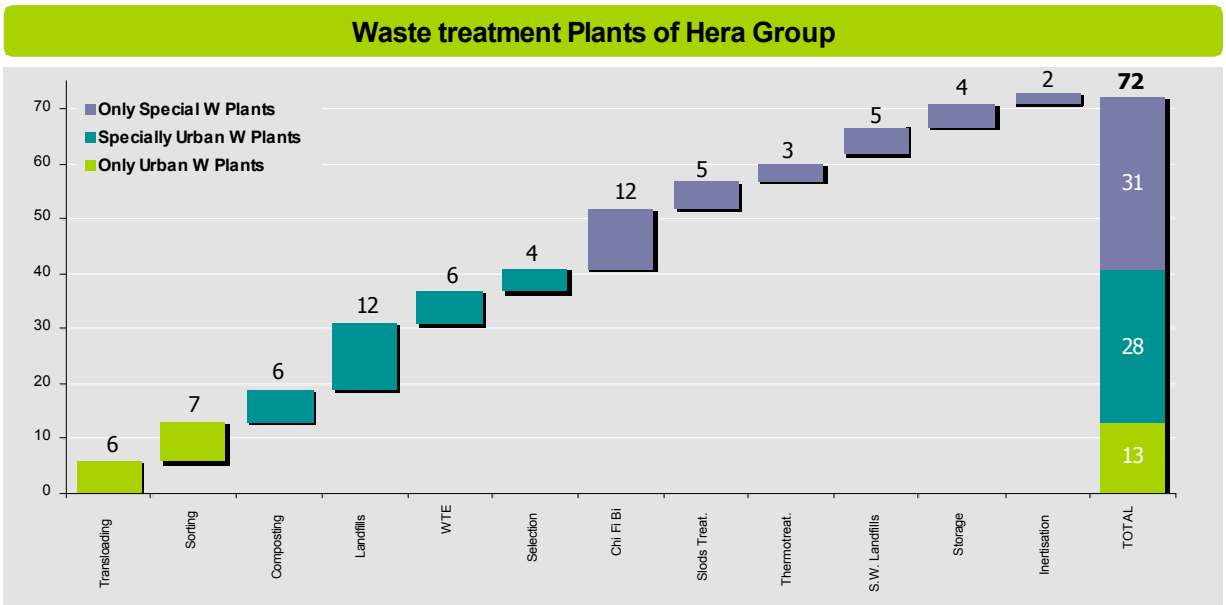
Importance of the Waste Management business for the Group

(mln/€)	31-Dec-04	31-Dec-05	Change	Change %
Ebitda	**85.7**	**115.5**	**29.8**	**+34.8%**
Group Ebitda	292.5	321.0	28.5	+9.8%
Percentage	*29.3%*	*36.0%*	*+6.7 p.p.*	

The Waste Management business, as mentioned above, was the sector which presented the highest levels of growth in 2005, so much so that it became the most important area with regards to the contribution to the overall EBITDA.

The Hera Group proves itself to be one of the most important integrated operators in the sector at European level due to its range of treatment and disposal plants for urban and special waste, and in 2005 it benefited from the full operations of Ravenna's Centro Ecologico plants and the coming onto stream of the new waste-to-energy plant at Bologna.

The graph below shows the Group's plants by type as at 31 December 2005:



As already indicated in the Water Cycle Area, the Group operates within the sphere of the six ATOs of the Provinces of Ravenna, Forlì-Cesena, Rimini, Bologna, Modena and Ferrara. Conventions are active with all the Agencies, regulating the Waste Management Service and guaranteeing the Group not only the extension of the concessions on average until 2012, but also the certainty of the tariff development until the end of 2007 and the guarantee of achieving full

application of the tariff system as from 2008, in accordance with the provisions of the Ronchi decree.
The activities performed in the waste management sector are considered strategic for the future development of the Group. In particular, the industrial plan contains important investments for the further strengthening of the waste-to-energy plant capacity, an activity that, in addition to minimising environmental impact on treatment, permits the production of electricity sold at subsidised tariffs (CIP6 and Green Certificates).

Results of the waste management business

Analysis of the results of operations in the Waste Management area is presented below:

Income statement (mln/€)	31-Dec-04	Incr.%	31-Dec-05	Incr.%	Change	Change %
Revenues	362.3		416.7		54.4	+15.0%
Operating costs	(189.9)	-52.4%	(208.9)	-50.1%	(19.0)	+10.0%
Personnel costs	(86.7)	-23.9%	(97.9)	-23.5%	(11.3)	+13.0%
Capitalized costs	-	0.0%	5.6	1.4%	5.6	+0.0%
Ebitda	**85.7**	**23.7%**	**115.5**	**27.7%**	**29.8**	**+34.8%**

Revenues in the Waste Management area rose from Euro 362.6 to Euro 416.7 million (+ Euro 54.4 million), disclosing an increase of 15.0%. This increase is principally due to two factors:

- the bringing onto stream of the waste-to-energy plant at Bologna and the operations of the Centro Ecologico in Ravenna for the entire year, which contributed by around Euro 37 million;
- the rise in volumes and services by approximately Euro 13 million and the tariff increases for around Euro 5 million.

In relation to operating costs, shareholders are informed that the increase in the quantities treated and the improved plant endowment made it possible to better the management efficiency, involving an increase in this item which was lower than that of the revenues (+ 10.0% compared with + 15.0%).

The volumes of urban waste collected rose by 2% when compared with last year.

Differentiated waste collection, net of volumes arising from sweeping activity (as provided by the DPCM project on differentiated collection of 5/6/1997), in terms of percentage-based incidence on total volumes collected came to 31.72% against the 30% of the previous year, confirming the Group's commitment to increasing the fraction recoverable from waste and reducing the environmental impact.

The volume of urban waste treated in the Group's plants, without the portion from the Modena plants, shown in the table, rose during 2005 by over 25%.

Quantitative data	31-Dec-04		31-Dec-05		Change	Change %
Urban waste	1,316.0	49.2%	1,342.7	40.1%	+26.7	+2.0%
Special waste from market	1,360.0	50.8%	2,007.2	59.9%	+647.2	+47.6%
Waste treated in Group plants	**2,676.0**	**100.0%**	**3,349.9**	**100.0%**	**+673.9**	**+25.2%**

Once again in 2005, waste treated in landfills decreased in favour of other plants, confirming the Group's strategies which show preference for solutions which have a lower environmental impact. The following table shows the breakdown of the portions disposed of per plant:

Quantitative plants	31-Dec-04		31-Dec-05		Var. Ass.	Var. %
Landfills	919.0	34.3%	1,080.2	32.2%	+161.2	+17.5%
Waste to Energy plants	451.0	16.9%	507.0	15.1%	+56.0	+12.4%
Selection plants	579.0	21.6%	774.8	23.1%	+195.8	+33.8%
Compost plants	67.0	2.5%	300.5	9.0%	+233.5	+348.5%
Inert. Chemical plants	660.0	24.7%	687.4	20.5%	+27.4	+4.1%
Waste treated in Group plants	**2,676.0**	**100.0%**	**3,349.9**	**100.0%**	**+673.9**	**+25.2%**

The EBITDA for 2005 rose from Euro 85.7 million to Euro 115.5 million (+ 27.7%), involving an increase of 34.8%. Shareholders should note that there was also an increase in the percentage-related marginality from 23.7% to 27.7% made possible by the improved output of the plants and an improved handling of the waste treated.

Other Services Area

Importance of the Other Services for the Group

(mln/€)	31-Dec-04	31-Dec-05	Change	Change %
Ebitda	**16.9**	**17.3**	**0.4**	**+2.2%**
Group Ebitda	292.5	321.0	28.5	+9.8%
Percentage	*5.8%*	*5.4%*	*-0.4 p.p.*	

During 2005, the Other Services area changed considerably in relation to the progressive reorganisation of the services which are not strategic for the Group: by way of example, during the year just ended, cemetery services where sold off in most areas and the more minor services concerning disinfestation and the management of public parks decreased consistently.

Results of the Other Services Area

The results are summarized in the table below:

Income statement (mln/€)	31-Dec-04	Incr.%	31-Dec-05	Incr.%	Change	Change %
Revenues	126.8		115.8		(11.0)	-8.7%
Operating costs	(110.9)	-87.5%	(98.0)	-84.6%	12.9	-11.6%
Personnel costs	(25.8)	-20.3%	(22.8)	-19.7%	3.0	-11.6%
Capitalized costs	26.8	21.1%	22.3	19.2%	(4.5)	-16.9%
Ebitda	**16.9**	**13.4%**	**17.3**	**14.9%**	**0.4**	**+2.2%**

The decrease in the Area's revenues, from Euro 126.8 million to Euro 115.8 million, is chiefly linked to the progressive disposal of the services mentioned above.

The EBITDA trend, having risen from Euro 16.9 million to Euro 17.3 million (+ Euro 0.4 million), disclosing an increase of 2.2% and with a percentage-based marginality up by more than two points, from 13.4% to 14.9%, confirms the excellence of the Group's decision to concentrate on specific areas of activities which are complementary to the core business.

The following table analyzes the main quantitative data concerning the Other Services Area:

Quantitative data	31-Dec-04	31-Dec-05	Change	Change %
District Heating				
Heat volumes distribuited (Gwht)	434.0	440.9	6.9	+1.6%
Public Lighting				
Light tower (thousand)	249.0	258.6	9.6	+3.9%
Municipalities served	51	53	2.0	+3.9%

Shareholders are informed that as far as the district heating area is concerned, the increase comes to around 2% thanks above all else to the more favourable climate trend.

In the public lighting sector, it should be pointed out that the increase in lighting points derives from both the new municipalities acquired and the increased lighting points in the municipalities already under contract.

3.01.03 Commercial Policy and Customer Care

The Hera Group set the following commercial objectives for 2005:

- standardising customer approach systems throughout the territory
- integrating the Ferrara customers in the commercial strategy and preparing for integration of the Modena customers
- commercially exploiting the renewal of the IT systems
- consolidating the system of offer and sales to business customers
- organising a solid and reliable control system
- completing the quality certification process with inclusion of the subsidiary companies, in particular Hera Comm
- organising commercial planning in compliance with market targets

In particular during the first year-half two customer satisfaction surveys were carried out, one on the residential market and one on the business market, aimed at identifying the quality components and processes that have greater impact on satisfaction and subsequently highlighting the operating priorities of Hera. The quality perceived was measured on four fundamental services provided by the Group, environmental hygiene, water, gas, and electricity, and on the customer contact and management channels.
Satisfaction levels were generally found to be good, even if some qualitative differences were observed between territories, which proves that although Hera is now perceived as a group, the level of service is not yet uniform.
Hence during the year a system of procedures for call centre and branch operators was set up which standardised tariffs, procedures and instruments for the management of contacts with the customers using the new Siebel system as base.
During 2005 while competition on the residential gas market was keen it did not create particular problems for the Group, as it lost only 16,770 customers with a total annual consumption of 18.4m m^3, out of a total as at 31.12.2005 of 936,600 customers with a total consumption of 2.3m m^3.
During the year various commercial notices were sent to customers explaining the functioning of the gas chain and the role played by Hera Comm and promoting specific customer loyalty ventures.

2005 also saw the start up of the new SAP ISU information systems at Bologna, Ravenna and Forlì-Cesena. This caused a strong increase in the workload for the call centre and branches, but also raised customer awareness on billing and payments, particularly in the Bologna area. At first service levels were affected, but they quickly returned to normal levels, following the upgrading of the call centre hardware and the reorganisation of some branches.

The Ferrara customers were integrated into the Group's commercial policies and the procedures for call centre and branch operators were standardised as were the customers notices.

On the Business market (large customers) the first year-half saw the launch of dual fuel sales (gas and electricity) through the indirect channels, with master agreements being executed with approximately 30 territorial associations, while the direct channel sales campaign has almost

concluded. Condominiums that were lost during 2004 were also recovered. Important dual fuel supply contracts were also signed outside the territory managed by Hera.
On the business market 300 customers, with a total annual consumption of 10.6 m. m^3, were lost in 2005, but others were acquired "outside the net" for a total consumption of 41m m^3.
In the second half of the year loyalty programmes aimed at "corporate" clients and condominiums were launched. In the condominium segment, in particular, 33 customers lost in previous years were recovered, for a total annual consumption of 2.3m m^3, against customers lost in the year for 0.6m m^3.
For the year-end sales campaign a new offer system was set up, which provides customers with a range of offers that vary according to individual requirements, backed up by new reporting material and new contractual documentations for indirect sales. In particular, the "Future dual" dual fuel offer was designed with standardised forms and contracts for electricity and gas.

Electricity sales closed the year 2005 slightly up on 2004.
Furthermore, an electricity consumption forecast instrument was created for the energy exchange and contracts for precise customer metering were signed. This allowed the Group to market the consumption visualisation web service.

In October the new segmentation of the Hera customer base was formally implemented, which led to the rearrangement of organisational structures and to the creation of structures responsible for the full management cycle of pertinent customers. In particular the Business customers will be managed by the Business Customers and Top Customer structure of Hera Comm and the residential customers by the Mass Market customer structure of Hera Comm, which will coordinate the pertinent commercial activities of the Local Operating Companies.

In September Hera Comm gained its first ISO 9001 certification, as independent company. The management of customer contacts was subjected to particularly in-depth analysis and the procedures and systems were found to be in compliance and appropriate.

3.01.04 Trading and Procurement Policy

Business Analysis – reference scenario

2005 saw the global economy continue the expansion phase which began in 2003, even if the pace differed from one part of the world to another. Indeed all the major economic areas recorded GDP growth rates which were more or less constant, while once again it was largely due to the vivacity of economic activity in the United States and in Asia that international recovery continued at a strong pace.

The growth rate in the Euro area continues to sustain decidedly modest levels, especially if compared to the growth rates of the American and Asian economies (1.4% of the Euro area against the 3.6% forecast for the United States, the 9.3% for China and the 4.6% for the Pacific countries). However the third quarter 2005 witnessed an unexpected acceleration in GDP which concerned all the components of domestic demand and, especially, the growth of investments. In spite of this, a certain degree of uncertainty still surrounds future trends in domestic demand and so it is not possible to foresee a virtuous cycle being triggered within the area.

As far as exchange rates are concerned, 2005 witnessed a further strengthening of the dollar, which experienced a 12.5% appreciation, after having risen as high as 1.35 USD per Euro at the beginning of the year before coming back down to 1.18 USD at the end of December 2005. After a few months of substantial stability, with a €/$ exchange rate in the region of 1.20-1.23 USD per Euro in the months of June-July and an exchange rate in the region of 1.23-1.25 USD per Euro in the months of August-September, the dollar rapidly fell below the 1.20 mark, reaching as low at 1.17 dollars mid-November. The progressive strengthening of the dollar is attributable to various factors amongst which a differential in the reference rates between the EU and the US of 175 basic points (4% fixed by the FED against the 2.25% fixed by the ECB), the different growth prospects, the tax benefits on capital inflow from which the American companies benefited up to the end of 2005.

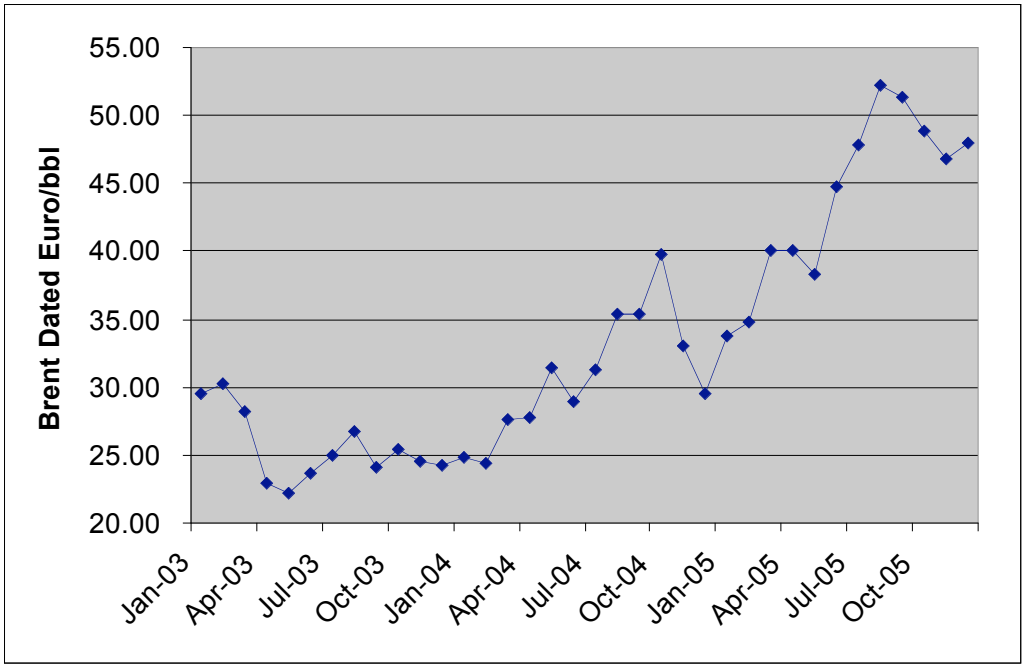
On the inflation front, despite the fact that the price of oil stayed above the 60 dollars/barrel mark, no particular acceleration of inflation was recorded on the end markets. The European Central Bank did however take precautions contrasting any inflationary fears with a modest 25 basic points increase of the reference interest rate. As far as the USA is concerned, this remains the country with the highest risk of inflation from costs: the tendential rate of year-end stands at 3.5%, well above the 2.2% of the Euro area and the 2% of Italy.

Reference Scenario

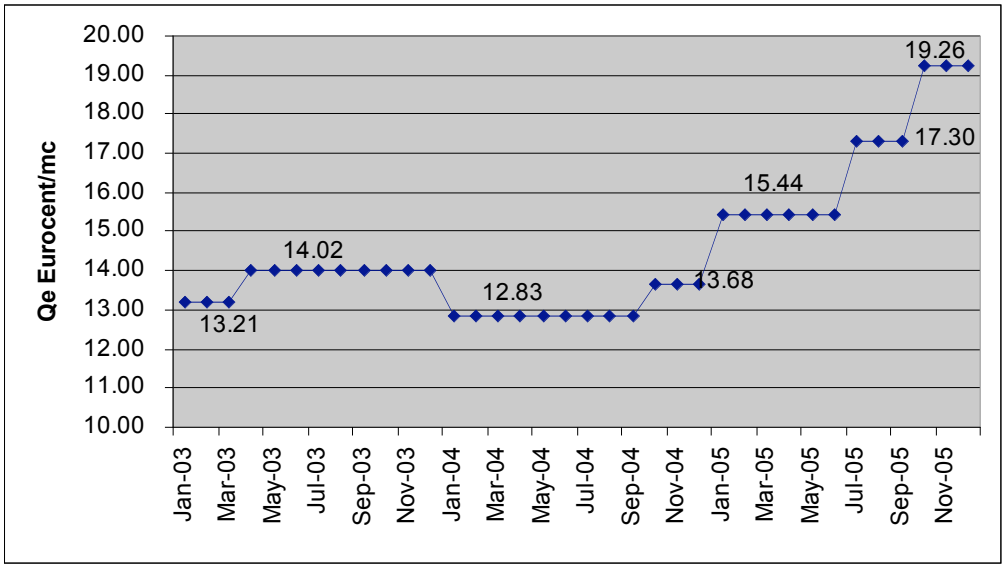
	2005	2004	% variation
$/bbl oil price	54.4	38.2	42.3%
Euro/$ exchange rate	1.24	1.24	-
Euro/bbl oil price	43.7	30.7	42.1%

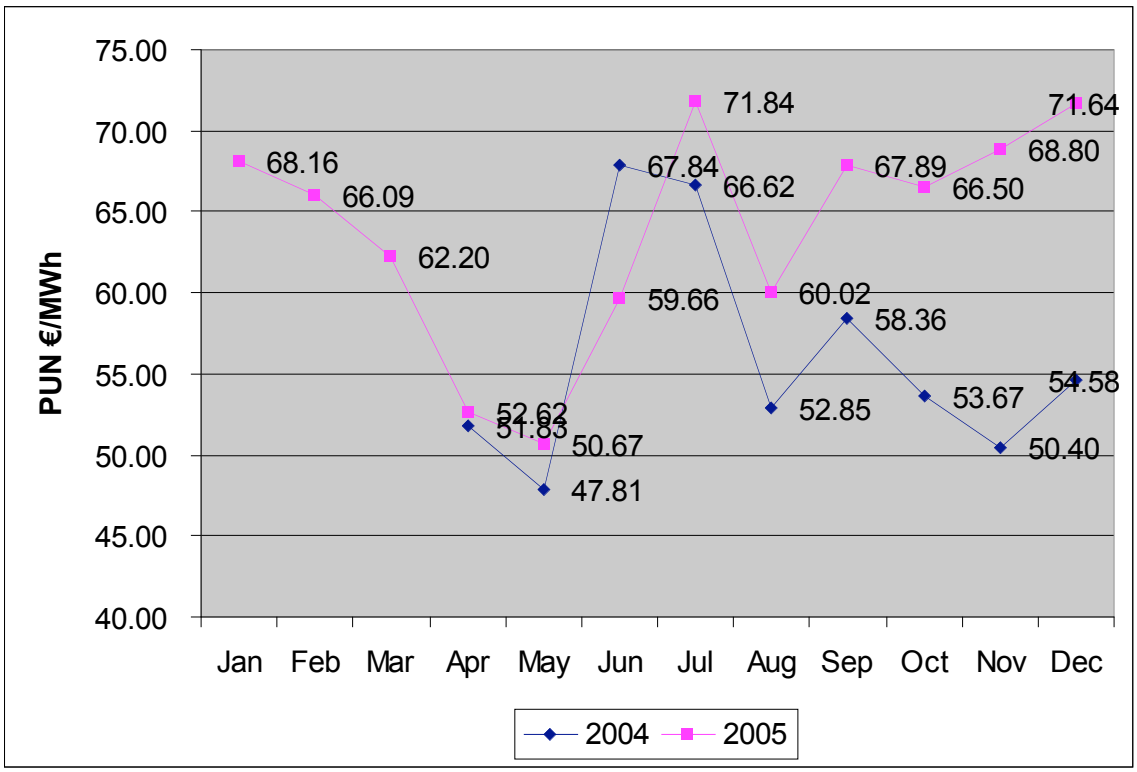
As far as the oil market is concerned, the average Brent price in 2005 was 54.4 dollars a barrel, posting a +42.3% compared to the 2004 average (38.2 dollars a barrel). In 2005 crude oil touched record highs since 1979, reaching a monthly average of almost 64$/barrel in August and almost 63$/barrel in September. Due to the effect of the relative weight of the Euro on the US Dollar calculated on the annual average, the price increase of Brent in Euro was practically the same (+42.1%). In 2005 crude oil price trends took on a structural pattern; experts expect to see a slight drop in prices next year.

The tension in black gold prices is attributable to a series of factors which have profoundly changed the structure of the world oil market, first and foremost the sharp upsurge in consumption (due to China and the other Asian countries, as well as the US) in the face of deficiencies in the additional production capacity and in refining. Secondly, factors of a geopolitical nature have contributed to the belief that the world's crude oil industry no longer has the same capacity to meet the pressures of demand, amongst which the prolonging of the serious situation in Iraq and the problems which have affected producing countries such as Venezuela and Nigeria.



Against this backdrop, as far as gas is concerned, the average value of the QE was equal to 16.858 in 2005, compared to an average value of 13.040 in 2004 and an expected value of 23.770 in 2006. As it is possible to infer from these figures, the full effect of the sharp rise in the price of oil recorded during 2005, has yet to work its way through to gas prices and is destined to have major repercussions through 2006. This is naturally due to the effect of the delays associated with the formulas for updating gas prices.





As far as electricity is concerned, the average exchange sales price (PUN) was equal to 64.00 €/MWh in 2005, which was higher than the previous year.

In 2004, the tariffs established by AEEG equal to an average of 57.34 €/MWh remained in force until March and from April the electricity exchange was launched with an average PUN in 2004 equal to 56.18 €/MWh.

The increase in energy prices in 2005 compared to 2004 was particularly apparent in the second half of the year, the period in which the most notable increases in oil prices were recorded.

GAS DIVISION

As in 2004, the reference scenario for 2005 suffered the effects of a particularly tight market situation due to the limited capacity available for "new operators" on the methane pipelines interconnecting with overseas procurement sources. This situation is destined to continue in the short/medium-term period, at least until the new infrastructures will start operations (upgrading of the TAG and TTPC methane pipelines, the GNL terminals and the GALSI methane pipelines).

In May 2005, the company TTPC (ENI Group), with view to improving ENI's position with regard to the proceedings implemented by the Italian Anti-Trust Authority (ACGM) to investigate whether it had abused its dominant position, implemented a procedure of non-discriminatory allocation of the capacity relating to the first lot of the upgrading of the TTPC methane pipeline (approximately 3.5 BN m^3/year), said capacity to be available as from 1 October 2008.

Participation in this procedure on the part of all the operators, Hera Trading included, essentially proved futile, given that SONOTRACH deemed the preliminary contracts previously signed with EDISON (from 0.7 to 4 BN m^3/p.a.), BRIDAS (0.5 BN m^3/p.a.), COMPAGNIA ITALIANA DEL GAS (0.5 BN m^3/p.a.), WORLDENERGY (0.1 BN m^3/p.a.) during an earlier procedure implemented in 2002 by TTPC in a non-publicised manner and subsequently annulled by TTPC itself, to be valid.

In short, allocation of the capacity relating to the upgrade, effected on the basis of the new non-discriminatory procedure, gave rise to the same outcome as the previously annulled procedure insofar as the only operators able to document the availability of gas proved to be the four which had negotiated the preliminary contracts with SONATRACH during the first procedure.

With the same intention as above, in November 2005, the Company TAG (ENI Group) implemented a similar non-discriminatory procedure for allocation of capacity on a twenty-year basis, with effect from 1 October 2008, for a quantity equal to approximately 3.5 BN m^3/p.a.

Significant Events

With regard to the gas division, the year 2005 clearly highlighted the problems associated with the limited capacity of operative storage and the equally limited capacity of transportation available on the pipeline interconnecting the Italian system with the procurement areas.

As far as storage is concerned, the late cold spell recorded at the end of February/early March 2005, forced the system to make use of the strategic storage to the extent of approximately 800 million m^3.

Hera Trading was also obliged to use strategic storage for 3 days in the month of March and for a volume of 0.9 million m^3, which were however restored in the next 2 days of the same month.

With regard to the limited transportation capacity, the auctions conducted by ENI-CH on Transitgas with "rising" modality, produced transport prices that were 400% higher than the auction base,

which Hera Trading deemed to be unsustainable and hence abstained from executing new contracts for the gas year 2005/2006.

ELECTRICITY

Legislative/Regulatory Framework

2005 was undoubtedly a watershed year for the electricity sector as it witnessed the Electricity Exchange enter into full effect (both offer and demand side).
The full start-up of the Exchange and the abandoning of the old trading contracts increased the complexity of the operators' activity as they had to balance hour by hour rather than by time-band/month, as in 2004, or even by time-band/quarter as in 2003.
The training initiatives and the development/acquisition of the necessary instruments implemented as early as 2004 proved appropriate and allowed Hera Trading to be fully operative right from 1 January 2005.

Significant Events

The full launch of the Electricity Exchange with effect from 2005 allowed more accurate definition of Hera Trading's operating activity which features the activity of "physical" management of the purchase portfolio to cover the sales of Hera Comm, but also the management of a further purchases/sales portfolio targeted at the wholesale market, which is more orientated towards this type of "financial" activity.
In particular, within this second portfolio, the contracts for differences (CDF) with ATEL and Acquirente Unico (AU) were managed.
During the year, with a view to maximising the economic value of the portfolio import capacity, the opportunities arising from the disalignment of prices which occurred in the Italian and French exchanges were exploited with activation of arbitrage transactions.
In December 2005 negotiations were concluded with EGL (Toller) for the contract of supply to Hera Trading of the electricity from the Sparanise power station.

RISK MANAGEMENT

As part of its trading activities Hera Trading is exposed to fluctuating energy prices and exchange risk given the potentially different sale and purchase prices of gas and electricity. The current exposure to other financial risks (counter-party risk, liquidity risk, etc.) is negligible. The objective of Hera Trading is, in fact, to limit volatility risk to the margins foreseen in the budget that are, after all, those dictated by reference market regulations (for example, CIP 6 and transport costs). For this reason several derivative contracts have been stipulated in order to synthetically align the index formulas of the sales prices:

- to the indexing formulas of supply prices when dealing with supply at indexed prices;
- to the fixed prices when these sales are supplied at fixed prices.

Additionally, in terms of electric energy, in order to reduce exposure to the PUN price generated by the ATEL contract, as agreed upon in the course of budget approval, Hera Trading decided to participate in the auctions held by the Acquirente Unico (a joint stock company set up by the Network Operator to assure competitive pricing in a liberalised market) where it successfully bid for 50 MW of oil product, deemed to the most opportune of the products up for auction.

The two differential contracts, even if not perfectly complementary in terms of quantity and price, were structured to be impacted differently by exchange price trends and that is what effectively took place.

3.01.05 Financial Policy and Rating

Once again in 2005 the Group pursued the customary financial policy directed at guaranteeing coverage of corporate requirements and characterised by utmost prudence, economy and balance between long and short term borrowings.
The performance of the financial markets and that of the raw materials used in energy production, which play a key role in the Group's business, made the management of working capital flows particularly delicate. The consistent increase in the costs of raw materials, while lessened by the strengthening of the euro against the dollar, caused a sharp increase in working capital sustained by an increase in short term borrowings. Account must also be taken of the fact that further temporary unbalance was caused by the gradual progress of the project for renewal of the customer system which led to some suspensions/slow-downs in the scheduled billing flow.
In order to further improve the long-term debt position and in view of the substantial investment plan scheduled in the 2005-2008 industrial plan approved in September (approximately Euro1.4 billion), in October 2005 a pool of leading banking institutes Banca IMI, Citigroup and JPMorgan, were commissioned to organise and issue a fixed rate Eurobond with ten year maturity for a maximum amount of Euro 500 million. This project was brought to a very successful conclusion on 16 February 2006.
The Bond was in fact issued for a maximum amount established in the face of a demand of over Euro 2.3 billion, with annual coupon equal to 4.125%.
The success of the financial policy adopted by the Group was rewarded by Standards & Poor's confirmation of the A+ rating on the long term, to which was added Moody's prestigious A1 rating.
Hera has undertaken to maintain

- a solid financial structure
- an adequate level between liquidity and available committed financing, capable of meeting each financial commitment for the next 12 months
- a defensive rather than speculative risk management policy relating to interest rates, currencies and raw materials.

As far as short term debt is concerned, significant savings and an increase in operative efficiency have been achieved.

3.01.06 Research and Development

Group orientation on the matter of research and development is represented by the necessity, on the one hand, to implement initiatives aimed at increasing plant efficiency, reducing physical losses, minimising risks of service management and limiting as much as possible the environmental impact, that is, developing activities that have a direct effect on the business. On the other hand, it also aims to encourage and orientate research on issues of particular interest to Hera, making use of qualified internal resources dedicated to research as well as the external technical-scientific collaboration of institutional bodies (Universities, Research Centres such as ENEA and CNR, other companies and public entities), including through partnerships or simple sponsorships.

Substantial resources have been invested in research with the aim of achieving the following objectives:

- • improving efficiency in management of the products/services offered: projects and studies are aimed at improving the quality and sustainability and increasing the availability of water and energy resources and reducing wastage;
- • preventing and reducing the environmental risks arising from operations;
- • reducing operating costs: by defining specific techniques for materials, services and works, it is possible to spread the use of best practices in management and maintenance of the networks; the common use of the corporate operative model selected by the Group allows for the creation of an internal benchmark which serves to promote tangible improvement of efficiency levels;
- • increasing the industrial margin through:
    - reduction of losses and disservices
    - expansion of volumes of services managed
    - optimisation of the tariff policy.

Major Research Projects carried out in 2005

Environmental Division

• CO_2 Project: launched in 2005, the project involves experimentation of an innovative technology for capturing CO_2 issuing from exhaust gas produced by any combustion process and its use in the process of anaerobic digestion of sewage sludge. The objectives are to:

- reduce CO_2 emissions;
- use the captured CO_2 to reduce the sludge contained in the of the operators of the purification plants;
- produce a greater quantity of methane gas;
- lay the foundations for Hera's future role as leader in innovative technologies for the limiting emissions.

Networks Division (Water and Energy)

• "Polluting Defence" Project: this project concerns the development and application of new instruments for remote monitoring of the quality of drinking and waste waters and gas emissions. The objective is to monitor in real time several important water and air quality parameters, reducing pollution risks and laboratory analysis costs. After the positive experience in on-line monitoring at the water treatment plant of Val di Setta (BO), in 2005 installation of a similar instrument began at the Ravenna plant, for the purpose of monitoring the efficiency of the water treatment processes.

• King Mida Project: "King Mida" is the name given to a series of research activities concerning the sector of energy recovery from sewage sludge, with the intention of effecting medium-long term experimentation of innovative technologies for the low cost disposal of sludge.

• MIG Project: consists of the creation of a fluid dynamics model for management of the water networks, with the aim of optimising the use of current and future aqueduct sources, in terms of:
1. reliability: placing the primary network in a position to guarantee the water volumes necessary to the population even in the event of serious difficulties, such as exceptional drought, or accidental pollution of a water resource;
2. costs: reallocating volumes between the various sources with the aim of optimising the total production cost;
3. quality: so as to guarantee pre-established quality levels, fully exploiting the available resources;
4. environment: limiting the levels taken from the natural water resources (e.g. from water tables).
The model has already been used to simulate strategic scenarios for increasing procurement of water resources. The project was concluded in 2005.

• MIT Project: "MIT" (Technical Hydraulic Model) means the development activity sector which uses the models of hydraulic simulation applied to the networks. This sector is complementary to the MIG sector. The aim of the "MIT" project is to spread the use of the mathematical models in the Local Operating Companies as modern management instrument.

• Ferrara Waters Project: this project involves a series of actions aimed at providing support to the management of the hydraulic network of Ferrara and surrounding countryside through cutting-edge technological solutions, such as mathematical simulation models and foresight models for the rehabilitation of water pipelines.

• Marecchia Project: this project consists in the performance of part of the activities pertaining to a complex study of the alluvial fan of the Marecchia river to aid sustainable management of water resources. Other parties involved in the project, which deal with other correlated study activities, include the Interregional Marecchia-Conca Basin Authority, the Emilia Romagna Region, the Province of Rimini, the Municipality of Rimini, the ATO of the Province of Rimini.

• X-water Project: experimentation of remote reading of waters applied to a pilot section of the distribution network. This project aims to provide indications on the applicability of remote reading to the recording of physical network leakage. By controlling the water balance in a particular section of the network, it is possible to precisely record the volumes of incoming water, that is

introduced to the network and outgoing water, that is, effectively used, and hence allow prompt intervention in the event of breakage and thereof water loss. The project will attempt to assess, through the analysis of more accurately recorded consumption trends, the behavioural patterns of consumers with respect to the resources and any tariff implications linked to said behaviour.
The data gathered has led to some interesting preliminary results in terms of control of water loss. Monitoring of the sample district shall terminate in 2006.

• Meters Project: the project, which was implemented in 2005, aims to analyse samples of the current pool of drinking water meters, in order to identify the best technology available on the market by which to increase the level of service to consumers.

• Fuel Cell Project: construction of plants for distributed production of electricity and heat through combustion cells fuelled by methane or hydrogen. The latter appear particularly suited to guaranteeing the supply of electricity in emergencies. In 2004 three hydrogen Fuel-Cell models were acquired and installed. In 2004 the project obtained funding from the Emilia Romagna Region within the context of the Regional Programme for Industrial Research, Innovation and Technological Transfer.
The initiative forms part of the endeavour to acquire know-how on the issue of alternative and renewable energy sources, in the event that, should the hydrogen market develop, the Group may take on an important role as supplier of raw material or of electricity or heat energy deriving from the transformation of methane into hydrogen.

Other Initiatives

SOV Project : this project began in 2002 and was characterised by intense operating activity in 2005. It concerns the research of volatile organic substances produced in the baking of ceramics and is being carried out in partnership with IPEG SpA, Smaltochimica Srl and Centro Ceramico. For Hera, the interest in the project lies above all in the identification of instruments and methods allowing automatic and continual control of volatile organic substances produced in various processes in the production cycles of Hera, in particular those relating to the treatment of waste.

As the project for "Control of the emission of Volatile Organic Substances (SOV), new systems for continuous monitoring of SOV in gas emissions", constitutes industrial research and pre-competitive development activity, it has been recognised as qualifying for the benefits of Law 46/82 and hence has been funded by the Minister of Productive Activities from the Fund for Technological Innovation (FIT). The research was concluded in 2005.

3.01.07 Human Resources and Organisation

As at 31 December 2005 the employees in the Hera Group totalled 5,904 with the following division by category: Senior Management (93), Managers (245), White-collar (2,458), Blue-collar (3,108). The following movements occurred in the year: new arrivals 90, acquisition of personnel from increased consolidation area 1,027, departures 236. It is noted that the new arrivals essentially related to the change in mix with the insertion of qualified personnel; finally it is noted that the total number of university graduates increased by 85 units (from 461 equal to a percentage of 9.18% of total employees engaged on an open-ended basis, to 546 equal to 9.55%).

Organisation
During 2005, in view of the complexity of the corporate structure and of the sizeable dimensions reached by the Hera Group, the essential organisational structure underwent redefinition. In practical terms:

- the General Management Division, the Local Operating Companies, the Networks, Research & Development, District Heating and Large Plant Engineering and Electricity Grid Coordination Divisions all report to the Managing Director, as do the Purchases and Tenders, Financial Administration and Control, Personnel and Organisation, Quality. Safety and Environment central staff units;

- the Environment, Sales and Marketing and Services Divisions report to the Chairman, as do the Business Development, Legal and Corporate Affairs, External Relations and Investor Relations central staff units;

- the Internal Auditing department reports to the Vice Chairman.

At the same time, in order to supervise the company's social responsibility the organisational position Corporate Social Responsibility, reporting to the Managing Director, was set up.

Furthermore, optimisation of the internal functioning processes continued, with implementation of the SAP-ISU IT system and consequent integration of the customer, activities and billing management processes in the territorial areas of Bologna, Ravenna and Forlì-Cesena, in addition to initiation of implementation of SAP-ISU for Business customers.

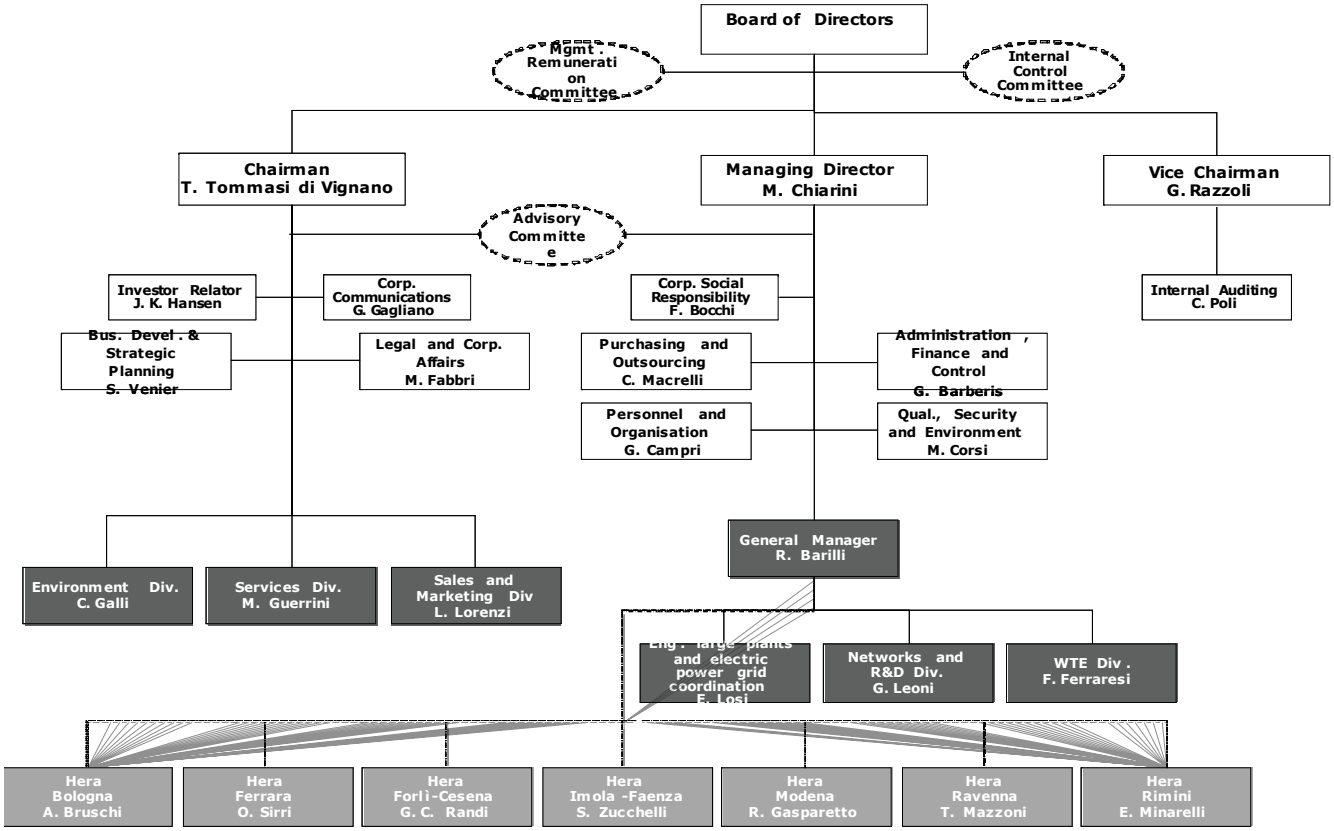
In order to minimise resistance to change caused by system changes, some specific support initiatives were implemented:
- organisation of events to notify and inform the "internal stakeholders" affected by the process changes (directors, department managers, coordinating personnel, trade union organisations, employees, etc.);
- development of IT and process skills, with the provision of over 423 training days and the involvement to date of approximately 1,347 people in 30 ad hoc training programmes.

2005 also saw the launch of the process of integration of the services managed in the territory of Modena and, consequently, the setting up of the Local Company of Hera Modena, which began operations on 1 January 2006, thus confirming the "open entrepreneurial formula" which distinguishes the Hera model.

At year-end 2005 Hera also decided to focus the Electricity Business by setting up a new dedicated Division, and also by planning and constructing large waste-to-energy plants, and by coordinating the Group's electricity grids.

Organisational Macrostructure

The chart below shows the Group's organisational macrostructure, inclusive of the integration of Meta:



Industrial Relations

Trade union activity was largely centred on issues relating to correct allocation, in accordance with Group organisation, of the activities of the former Agea and Acosea companies within subsidiaries companies such as Hera Comm, Famula, Hera Luce and Uniflotte. Important trade union agreements were reached for the purpose of harmonisation of regulatory and economic treatments on the Ferrara and Ravenna territories. At end of September discussion began on a trade union platform containing substantial and important issues. Among these attention is drawn to the following issues, which were also desired and requested by the company: definition of a performance bonus constructed on a single system for both objectives and economic items, definition of the field of application of the various CLA in force in the Group, harmonisation of the economic treatments ensuring from second level negotiations. The trade union negotiations are still underway and it is believed that a conclusion may be reached in the early months of the year.

Training

In addition to accompanying the integration processes underway and to meeting the Group's needs, the primary aim of the training activities implemented during 2005 was also to develop the professional experience present at various levels and to enhance know-how and distinctive skills.
During 2005 103,113 man/hours of training were provided for a total of over 11,800 participations. 4,230 employees (more than 83% of the company roll) were involved in training activities.
On the whole the activity implemented, whether training or professional refresher courses for employees, formed part of several lines of intervention. In addition to intense training activity on the issues of quality, environmental management systems and industrial safety (not only in compliance with provisions of the law), the principle initiatives concerned:

- the launch of the School of Trades aimed at enhancing the specific technical-operative skills of the Hera Group
- update and development of technical-specialist skills
- institutional training to support insertion of resources engaged under the Graduates Project.

The first year-half 2005 also saw completion of a series of training programmes initiated in 2004 (encounters with white and blue collar workers to spread awareness of values and mission, days for senior managers, managers, executives dedicated to the development of collaborators and to communication techniques, specific encounters on the issue of planning and control of managerial activity).
Significant investment continued to be made in support of the implementation of the new company IT systems (approximately 30,000 man/hours).
The overall investment (net of personnel costs for missed production) totals Euro 1,020,840 for the year 2005, up 5.6% on 2004.

The table below quantifies, in terms of man/hours provided, the training scheduled in the 2005 Training Programme:

Training	*Man Hours*
Professional training and specialised courses	45,261
Quality, Safety and Environment	15,010
Managerial training	8,288
Information technology	34,554
Total	**103,113**

3.01.08 Information Systems

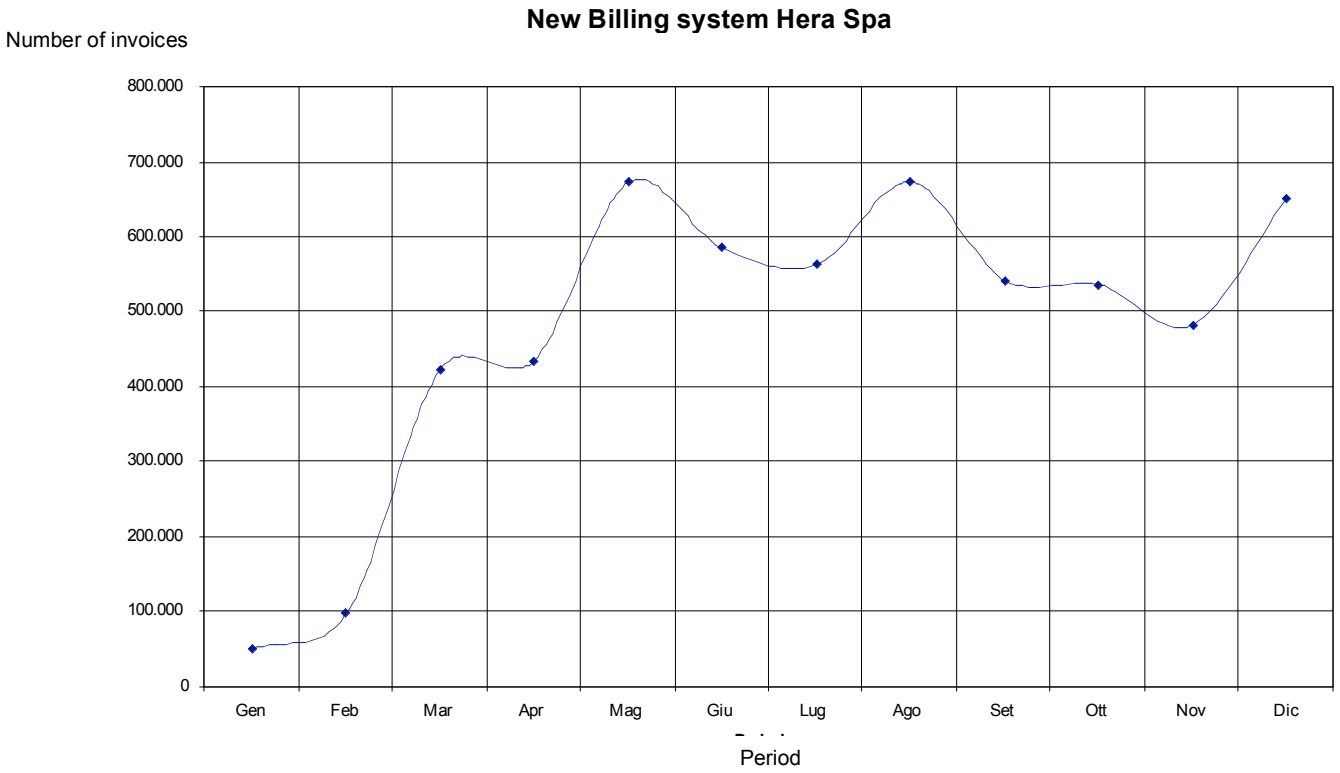
During 2005, the Group continued to optimise internal processes, pursuing the principle of departmental centralisation and rationalisation of all common activities in order to obtain uniform treatment and economies of scale.

The following were the most significant events of the year:

- the full integration of the Ferrara area (former Agea/former Acosea) into the Group
- the beginning of the process of integration of the Modena area (former Meta)
- the revision of the Organisational Macrostructure
- the launch of the new billing system (SAP-ISU) on 70% of the managed territory.

First Phase of SAP-ISU Consolidation

After the introduction of the new billing system, launched in the territories of Rimini (end of 2004) Bologna and Ravenna (February and March 2005) and Forlì/Cesena (June), implementation continued in the territorial area of Imola/Faenza and in the commercial area of Business customers with suspension of billing on the old systems from the month of November.
Trends in invoices issued in 2005, in the territories of Rimini, Bologna, Ravenna, Forlì-Cesena, Imola-Faenza and in the Business customer area, are illustrated in the graph below:



The consequences of suspension of billing in the Imola-Faenza area and Business customer area, for the purposes of implementation of the SAP-ISU system, were reflected in the increase in working capital and in the net financial position as at 31 December 2005 (total impact in the region of Euro 119 million).
However in the first three months of 2006 the billing process in the aforesaid areas has reached full capacity and it is expected that working capital will return to customary levels within the first six months of this year.

The implementation programme has now scheduled application of the new billing system in the Modena area in the first half of 2006 and in Ferrara in 2007.

3.01.09 Quality and Environment

Hera' commitment towards achieving "sustainable quality" progressed strongly in 2005, through a series of actions concerning, among other things, the following:

- stronger emphasis on the sustainability objectives within the 2006-2008 Strategic Plan
- continuation of the integrated Quality Safety Environment certification programme
- setting up of a CRS function (Corporate Social Responsibility)
- creation of a Balanced Scorecard system covering the entire corporate system.

As far as the objective of integrated Group certification is concerned, during 2005, the Quality management system was consolidated and Environment management was implemented in compliance with UNI EN ISO 14001 standards. Hence the final phase of certification of Hera shall occur in the first half of 2006, slightly later than the initial schedule (December 2005).
A further confirmation of Hera's strong commitment to environmental issues was also provided by the approval of the project for EMAS registration, over the 2006-2010 period, of the entire Environment Division of Hera SpA for a total, as at 2005, of 32 sites (corresponding to 53 waste treatment and disposal plants).
The Ecolabel Ecoaudit Committee awarded Hera the international European Emas Award for the aforesaid project.
During 2005, Hera also confirmed its commitment to completing the objective of Group integrated certification with the achievement of the certification of the Safety system, in compliance with the OHSAS 18001 standard, by 2007.
The 2004 Sustainability Report, published during 2005, saw further widening of compliance with the principles defined by the major international reference standards and consolidation of dialogue with the stakeholders, with the involvement of the mayors of the shareholding municipalities, of environmental associations and of employees.
Greater emphasis was given, in the 2004 Sustainability Report, to reporting on progress in the commitments undertaken in the 2003 Report and to defining the commitments for the year 2005.
Tangible evidence of Hera's attention to the two major corporate stakeholders, to customers and to its own employees, was provided in 2005 by the performance of a Customer Satisfaction survey throughout the territory and on all services supplied (which revealed that 88% of customers were satisfied or very satisfied) and by a Corporate Climate survey which involved the full spectrum of Hera employees.
Both surveys, which will be repeated at regular intervals, generated numerous improvement projects involving the majority of corporate functions.
The 2005 Sustainability Report, which will be published in the coming months, shall further continue the improvement process, along the foundations that have been set over the past years.
Hera's commitment to encouraging broader debate and confrontation on the issues of sustainability included the staging of an itinerant photographic exhibition which toured the 8 major towns in the territory throughout the second-half of 2005. In association with this exhibition, the Group held an on-line photographic competition named "Sustainable Glances", open to everyone up to 31 December 2005, with the forwarding of entries and the assessment of the same occurring entirely through the Hera Group website.

3.01.10 Annual Report on Corporate Governance

Introduction

Borsa Italiana S.p.A., has drawn up a Code of Conduct (hereafter the "Code") containing a series of recommendations relating to the procedures and regulations for the management and control of companies listed on regulated markets.

The Code presents a corporate organisational structure in line with the corporate and administrative practices adopted by the majority of companies which have implemented, in recent years, evolved models of corporate governance.

The adoption of the principles contained in the Code has the final objective of reassuring the investors on the existence, in listed companies, of a clear and well-defined organisational structure, with adequate division of responsibility and a correct balance between management and control.

Although the adoption of the principles contained in the Code are not a legal obligation, Hera S.p.A (hereafter the "Company") has considered it appropriate to adhere to the principles of the Code.

The Company adopted the provisions of the Code with a resolution passed by the Board of Directors, with a unanimous vote, on 4 April 2003.

This report illustrates the manner and procedures through which the Company has implemented the provisions of the Code.

Role and Composition of the Board of Directors

The Board of Directors is the central administrative body of the Company. In compliance with the recommendations of the Code, by which the Board of Directors must meet on a regular basis, the Company By-Laws provide that the Board meets periodically, at least on a quarterly basis, and whenever the Chairman considers it necessary or when a request is made by at least one third of its members or by the Board of Statutory Auditors. In addition, in compliance with the recommendations of the Code which provide that the Board must function and operate in such a way as to guarantee the effective and efficient performance of its duties, the Company By-Laws provide that the Board of Directors is vested with the widest powers for the ordinary and extraordinary management of the Company without limitations, with faculty to implement all actions considered necessary or appropriate to the pursuit of corporate objectives, excluding only those that, by law or the By-Laws, are strictly reserved to the Shareholders' Meeting.

In particular, in accordance with the By-Laws resolutions on the following matters are of the exclusive competence of the Board:

(xv) appointment and/or revocation of the Chairman and Vice Chairmen;

(xvi) appointment and/or revocation of the Managing Director and/or of the General Director;

(xvii) constitution and composition of the executive committee, appointment and/or revocation of the members of the Executive Committee;

(xviii) determination of the powers delegated to the Managing Director and/or General Director and/or Executive Committee and amendments thereto;

(xix) approval and amendments to long-term plans or business plans;

(xx) approval and amendment of the group regulations, if adopted;

(xxi) engagement and/or appointment, upon the proposal of the Managing Director, of the managers responsible for each departmental area.

(xxii) proposal to place on the agenda of the extraordinary Shareholders' Meeting amendment to article 7 (public majority shareholding), 8 (limits to shareholding), 14 (quorum for constitution and for resolutions of the Shareholders' Meeting and rights of veto) and 17 (procedures for the nomination of members of the Board of Directors) of the By-laws;

(xxiii) the assumption and disposal of equity investments worth more than Euro 500,000 ;

(xxiv) purchase and/or sales of properties worth more than Euro 500,000;

(xxv) the provision of sureties, liens and/or other collateral worth more than Euro 500,000;

(xxvi) purchase and/or sale of companies and/or business units;

(xxvii) the appointment of directors of subsidiary and/or investee companies;

(xxviii) participation in tenders and/or public procedures that involve contractual obligations exceeding Euro 25,000,000.

The Company By-Laws, amended by Shareholders' Meeting resolution of 23 September 2005, provide that the Board of Directors is comprised of 18 members. The current Board of Directors will remain in office until the approval of the financial statements relating to 2007.

Name and surname	Office	Position
Tomaso Tommasi di Vignano	Chairman	Executive Director
Maurizio Chiarini	Managing Director	Executive Director
Giorgio Razzoli (2)	Vice Chairman(3)	Non-executive independent director
Mara Bernardini (2)	Director	Non-executive independent director
Filippo Brandolini	Director	Non-executive independent director
Luigi Castagna	Director	Non-executive independent director
Pier Luigi Celli	Director	Non-executive independent director
Piero Collina (1)	Director	Non-executive independent director
Pier Giuseppe Dolcini (1)	Director	Non-executive independent director
Giuseppe Fiorani (2)	Director	Non-executive independent director
Vander Maranini	Director	Non-executive independent director
Nicodemo Montanari	Director	Non-executive independent director
Fabio Roversi Monaco (1)	Director	Non-executive independent director
Roberto Sacchetti	Director	Non-executive independent director
Luciano Sita	Director	Non-executive independent director
Ermanno Vichi	Director	Non-executive independent director
Stefano Zolea	Director	Non-executive independent director

(1) Members appointed by the Shareholders' Meeting of 28 April 2005 on the basis of lists presented by minority shareholders in compliance with the provisions of Law 474/1994.
(2) Members appointed directly by the Municipality of Modena pursuant to Article 2449 of the Italian Civil Code with effect from 31 December 2005.
(3) Member appointed by the Vice Chairman of the Board of Directors on 16 January 2006.

Currently there are 15 directors qualifying as non-executive independent members of the Board, in that:
(i) they do not have, or have recently had, directly, indirectly or on behalf of third parties, economic relations with the Company, its subsidiaries, the executive directors, the shareholder or groups of shareholders which control the company, of such consistency as to influence the autonomy of their judgment;
(ii) they are not holders, directly, indirectly, or on behalf of third parties, of shareholdings of such consistency as to permit them to exercise control or considerable influence over the Company, nor are they party to shareholders' agreements for the control of the Company;
(iii) they are not close family members of executive directors of the Company or of subjects indicated in letters (i) and (ii) above.
The following circumstances do invalidate the requisites for independence of a director: the appointment of the director by the shareholder or group of shareholders that control the Company, holding the office of director of a subsidiary of the Company and relative remuneration, holding the office of member of one of consultative committee described hereunder.

The Board of Directors, in the meeting of 28 April 2005, passed a resolution to confer to the Chairman, in addition to the powers entrusted by Annex 9.2 of the Voting Trust and Share Transfer Rules Agreement, which are fully transcribed below:

i) to preside and manage the Shareholders' Meetings;

j) to establish the agenda of the meetings of the Board of Directors taking into account the proposals of the Managing Director;

k) to supervise the execution of the resolutions passed by the corporate boards of the Company, also based on the periodic reports provided by the internal audit department and on which he shall be obliged to report jointly with the Chairman;

l) to represent the Company before third parties and in court with the power to appoint attorneys and lawyers;

m) in the case of urgency, to take, in association with the Managing Director, all decisions pertaining to the Board of Directors, notifying the Board of Directors thereof in the subsequent meeting;

n) in association with the Managing Director, to propose to the Board of Directors designation of Company representatives on the administrative and control boards of the investee companies;

o) to represent the company in relations with the shareholding public authorities;;

p) to propose to the Board the candidates for members of the Committees that the Board may decide to constitute in compliance with the Stock Exchange regulations by which the Company is bound or may intend to constitute;

the following powers:

11. to execute the decisions of the Shareholders' Meeting and of the Board of Directors as far as his authority permits;
12. to supervise the Company's performance for the purposes of achieving corporate goals and to draw up proposals relating to management of the Company to be submitted to the Board of Directors;
13. to be responsible for the organisation of the services and offices under his authority and also for the subordinate employees;
14. to take, in association with the Managing Director, any urgent decision reserved to the Board of Directors, of which the Board shall be notified in the first meeting thereafter;
15. to supervise operations of the Company and of the subsidiaries, providing the Board of Directors with a monthly report;
16. to draw up the Multi-Year Plans and the Business Plan to be submitted to the Board of Directors; to implement corporate and Group strategies, within the context of directives established by the Board, and to exercise the powers delegated thereto, and in particular those listed hereunder, in compliance with said strategies and directives;
17. to propose to the Board all the initiatives that he may deem useful to the interests of the Company, and of the Group, and to draw up proposals on matters reserved to said Board;
18. to represent the Company in the shareholders' meetings of companies, associations, entities and bodies which do not constitute stock companies, of which said Company is member, with faculty to issue special proxies;
19. to effect deposits on bank and postal current accounts of the Company, and to endorse cheques and drafts for crediting on said accounts;
20. to actively or passively represent the Company before Public and Private Entities and Offices,

Chambers of Commerce, Stock Exchanges, the National Commission for Listed Companies and the Stock Exchange, the Ministry for Foreign Trade, and the Italian Exchange Office as well as any other Public Administration or Authority; by way of example:

a. to sign notices, including notice to the General Register of Shares and to CONSOB, and to fulfil the corporate obligations provided by law and regulations;
b. to submit reports, motions and appeals, to apply for licences and authorisations;

27. to represent the Company in all active and passive lawsuits, in all stages of civil and administrative proceedings, before arbitration boards, with the widest powers to:
    a. bring conservative, restraining and executive actions, request summary judgments and seizure of property and oppose the same, enter civil proceedings, file motions and appeals;
    b. request and oppose any evidence, undergo free or formal examination, elect domicile, appoint lawyers, attorneys and arbitrators and perform all else that proves necessary to the positive outcome of the lawsuits at issue;
28. to confer and revoke powers of attorney within the aforesaid powers, for individual acts or categories of acts, to both employees of the Company and to third parties including legal entities;
29. to stipulate and sign contracts and memorandums of association of companies, associations, and consortiums worth no more than €500,000.00 (Euro five hundred thousand) for each transaction;
30. to establish, in the Company's interest, consulting relations with external experts and professional consultants, specifying terms and conditions of payment, all within the limits of €100,000.00 (Euro one hundred thousand) for each transaction;
31. as far as his authority permits, to stipulate, amend and terminate commercial and service agreements of any nature with companies and entities;
32. to participate, as far as his authority permits, in the capacity of representative of the Company, as lead company or as principal company, in the incorporation of joint ventures, T.A.C. (Temporary Associations of Companies), E.G.E.I. (European Group of Economic Interest), consortiums and other entities, issuing and receiving the relative mandates, for the purpose of participating in tenders for the award of works, service and supplies;
33. to take part, as far as his authority permits, in the Company's name, also in T.A.C. (Temporary Associations of Companies), E.G.E.I. (European Group of Economic Interest), consortiums and other entities, in tenders for contracts or concessions, auctions, private invitations to tender, private treaties, calls for bids and other public auctions at national, community and international level, even admitted to State contribution or aid, for the award of works, supplies of plant, including "turnkey", and/or of goods and/or of studies and/or of research and/or of services in general for any national, community and international public or private entity; submit application for participation from the prequalification stage; submit bids and, in the case of award, sign the relative documents, contracts and commitments, including the issue of guarantees and/or the establishment of deposit money, with full and wide powers to negotiate, settle and/or complete all the clauses that he may deem necessary and/or appropriate and/or useful;
34. to take part, as far as his authority permits, in any type of public or private auction or invitation to bid in Italy and abroad;
35. to stipulate, amend and terminate contracts for insurance policies with expense limit relating to the annual premium;

36. to rent or let out property under lease or sublease and stipulate, amend and terminate the relative contracts;
37. to deliberate the cancellation, reduction, restriction of mortgages or liens registered in favour of the Company, as well as subrogation in favour of third parties, where the aforesaid cancellations and waivers are requested further or subordinate to the full discharge of the credit;
38. as far as his authority permits, to stipulate, with all the appropriate clauses, assign and terminate contracts and agreements in any case pertaining to the corporate purpose – including those referring to know-how, trademarks and patents – even in consortium with other companies;
39. to establish, register and renew mortgages and liens for third parties' account and to the benefit of the Company; permit mortgage cancellations and limitations for third parties' account and to the benefit of the Company for return and reduction of obligations; waive mortgages and mortgage subrogation, including those of a legal nature, and effect any other mortgage transaction, always for third parties' account and to the benefit of the Company, and therefore receivable, exonerating the competent property registrars from each and any responsibility;
40. to appoint lawyers and attorneys in any disputes and for any stage of proceedings; conclude settlements, sign arbitration agreements and arbitration clauses, also proceeding to nominate and appoint arbitrators;
41. to appoint attorneys for single acts, within the powers assigned;
42. to decide the Company's subscription to bodies, associations, entities of a scientific and technical nature or pertaining to studies and research within the Company's field of interest, for which fees do not constitute an interest in the equity of said entity and for which participation does not involve an outlay of more than €100,000.00 (Euro one hundred thousand);

During the same meeting the Board of Directors passed a resolution to vest the Managing Director with the following powers:

30. to execute the decisions of the Shareholders' Meeting and of the Board of Directors as far as his authority permits;
31. to take, in association with the Chairman, any urgent decision reserved to the Board of Directors, of which the Board shall be notified in the first meeting thereafter;
32. to implement corporate and Group strategies, within the context of directives established by the Board, and to exercise the powers delegated thereto, and in particular those listed hereunder, in compliance with said strategies and directives;
33. to propose to the Board all the initiatives that he may deem useful to the interests of the Company, and of the Group, and to draw up proposals on matters reserved to said Board;
34. draw up the annual budget to be submitted to the Board of Directors;
35. to be responsible for the organisation of the services and offices under his authority and also for the subordinate employees;
36. to define the functional structures of the Company and its subsidiaries, within the framework of the general organisation lines established by the Board, specify the criteria for personnel recruitment and management in compliance with the annual budget; propose the engagement of directors to the Board of Directors; engage, appoint and dismiss personnel up to and excluding the rank of General Director, in compliance with the provisions contained in the annual budgets; adopt and implement the disciplinary sanctions, dismissal and any other

measure in respect of workers, office workers, assistants and auxiliaries;

37. to stipulate, amend and terminate contracts for the opening of credit, loans of any type and duration; request the drawdown of tranches of loans, up to the amount of €3,000,000.00 (Euro three million) for each contract;
38. to open and close current accounts with banks and credit institutions, withdraw sums from the accounts held in the Company's name, issuing for this purpose the relative cheques or equivalent credit documents, and order transfers utilising effective availability or credit lines in the current account;
39. to effect deposits on bank and postal current accounts of the Company, and to endorse cheques and drafts for crediting on said accounts;
40. to draw bills on customers, endorse also for discount promissory notes, bills and drafts as well as cheques of any kind and effect any consequential transaction;
41. to actively and passively represent the Company before Financial Administration and Commissions of any nature and rank as well as before Cassa Depositi Prestiti, Bank of Italy, Customs Offices, Post and Telegraphic Offices; by way of example:
    a. to sign tax and VAT returns and to fulfil any tax-related obligation,
    b. to submit reports, motions and appeals, to apply for licences and authorisations;
    c. to issue receipts, in particular for payment orders in relation to credits subject to factoring transactions;
    d. to perform any transaction at Cassa Depositi Prestiti, Bank of Italy, Customs Offices, Post and Telegraphic Offices for shipment, deposit, clearance and collection of goods, credit instruments, parcels and packages, registered and insured letters, issuing receipts in discharge;
42. to represent the Company in all lawsuits pertaining to labour law including the power to:
    a. settle individual labour disputes concerning the categories of officers, white-collar workers, assistants and auxiliaries;
    b. request and oppose any evidence, undergo free or formal examination, elect domicile, appoint lawyers, attorneys and arbitrators and perform all else that proves necessary to the positive outcome of the lawsuits at issue;
43. to represent the Company before the offices of Social Security Institutions for the solution of issues relating to employees of the Company, and also before Trade Unions in negotiations for contracts, agreements and labour disputes, with the power to sign the relative documents;
44. to issue guarantees and grant loans up to the value of €500,000.00 (Euro five hundred thousand) for each transaction; said limit shall not apply to transactions related to participation in tenders; issue, accept and endorse credit instruments;
45. to confer and revoke powers of attorney within the aforesaid powers, for individual acts or categories of acts, to both employees of the Company and to third parties including legal entities;
46. to participate, as far as his authority permits, in the capacity of representative of the Company, as lead company or as principal company, in the incorporation of joint ventures, T.A.C. (Temporary Associations of Companies), E.G.E.I. (European Group of Economic Interest), consortiums and other entities, issuing and receiving the relative mandates, for the purpose of participating in tenders for the award of works, service and supplies;
47. to take part, as far as his authority permits, in the Company's name, also in T.A.C. (Temporary Associations of Companies), E.G.E.I. (European Group of Economic Interest), consortiums

and other entities, in tenders for contracts or concessions, auctions, private invitations to tender, private treaties, calls for bids and other public auctions at national, community and international level, even admitted to State contribution or aid, for the award of works, supplies of plant, including "turnkey" and/or of goods and/or of studies and/or of research and/or of services in general for any national, community and international public or private entity; submit application for participation from the prequalification stage; submit bids and, in the case of award, sign the relative documents, contracts and commitments, including the issue of guarantees and/or the establishment of deposit money, with full and wide powers to negotiate, settle and/or complete all the clauses that he may deem necessary and/or appropriate and/or useful;

48. to take part, as far as his authority permits, in any type of public or private auction or invitation to bid in Italy and abroad;
49. as far as his authority permits, to stipulate, amend and terminate commercial and service agreements of any nature with companies and entities;
50. as far as his authority permits, to stipulate, with all the appropriate clauses, assign and terminate contracts and agreements in any case pertaining to the corporate purpose – including those referring to know-how, trademarks and patents – even in consortium with other companies;
51. to establish, in the Company's interest, consulting relations with external experts and professional consultants, specifying terms and conditions of payment, all within the limits of €100,000,00 (Euro one hundred thousand) for each transaction;
52. to conclude settlements, sign arbitration agreements and arbitration clauses, also proceeding to nominate and appoint arbitrators;
53. to arrange for guarantees to be provided by third parties in favour or in the interest of the Company, both in its position as creditor and as debtor, not exceeding the amount of €100.000,00 (Euro one hundred thousand) for each transaction;
54. to provide for the expenses incurred by the Company for investments; stipulate, amend and terminate the relative contracts, in particular for:
    e. works and supplies necessary to the transformation and maintenance of properties and plants;
    f. purchases and disposals of furniture, fittings, machinery and moveable assets in general, including those enrolled in public registers, as well as finance leases and rentals of said assets, with the cost limit referred to the annual rental;
    g. purchases, also under usage licence with cost limit referred to the annual premium, and job orders relating to EDP programmes;
    h. commercial information;
55. to appoint attorneys for single acts, within the powers assigned;
56. the Managing Director is also assigned the powers and responsibilities set forth in Legislative Decree no. 626 of 19 September 1994 and subsequent amendments and integrations in the matter of workers' health and safety during work, all of which with faculty to delegate;
57. in particular, the Managing Director is assigned the role of "Employer" pursuant to and for the purposes of Legislative Decree no. 626 of 19 September 1994 and subsequent amendments and integrations, with the duties provided for therein with faculty to delegate, as far as is permitted by said decree, the performance of every activity useful and/or necessary to ensuring compliance with provisions of the law;

58. lastly, the Managing Director is assigned the powers and responsibilities set forth in Legislative Decree no. 196 of 30 June 2003 concerning the protection of persons and other entities in respect of the treatment of personal data.

Hence neither the Chairman nor the Managing Director are executive directors.

In compliance with the recommendations of the Code, the delegated offices report to the Board of Directors and to the Board of Statutory Auditors, at least on a quarterly basis, on the activities performed in the exercise of the powers assigned thereto and on the most important economic and financial operations implemented by the Company and by the subsidiaries, with particular reference to atypical, unusual operations or those with related parties.

The Board of Directors in compliance with the provisions of Article 23 of the By-Laws and Article 150 of the Legislative Decree 58/98, regularly reports to the Board of Statutory Auditors, at least on a quarterly basis, normally during the meetings of the Board of Directors or even directly with written report sent to the Chairman of the Board of Statutory Auditors, on the activities performed and on the most important economic and financial operations implemented by the Company and by its subsidiaries, as well as on the operations in which the directors have an interest, on their own behalf or on behalf of third parties or which have been influenced by the party that exercises the activity of direction and coordination. The director, pursuant to Article 2391 of the Italian Civil Code, informs the other directors and the board of statutory auditors of every interest that, on his own behalf or on behalf of third parties, he has in a given operation of the company, indicating the nature, terms, origin and value; if the managing director is involved he must abstain from undertaking the operation entrusting it to the board.

In 2005 the Board of Directors met 22 times. In 5 meetings all of the directors and the statutory auditors participated and in the other 18 meetings almost all of the directors and the entire board of statutory auditors participated, with the exception of four meetings in which one statutory auditor was absent.

The General Director of the company is invited to attend the meetings of the Board of Directors and during 2005 attended 20 meetings.

In relation to the current year, as at 27 March 2006, 4 meetings of the Board of Directors have been held which almost all of the directors and the entire board of statutory directors attended; at present another 5 meeting of the Board of Directors have been scheduled.

The Chairman ensures that each Director and Statutory Auditor has all of the information and documentation necessary to discuss the business on the agenda of the Board meetings at least 3 days before the meeting, except in the cases of necessity and urgency.

Lastly, the Chairman and Managing Director ensure that the Board of Directors is also informed on the most important changes in legislation and regulations relating to the company and corporate offices.

Role and Composition of the Executive Committee

The Board of Directors, as provided by Article 23.3 of the By-Laws, in the meeting of 16 January 2006, set up an Executive Committee, appointing the following members:

- Tomaso Tommasi di Vignano - Chairman,
- Giorgio Razzoli - Vice Chairman,
- Maurizio Chiarini - Member.

The Committee, with regard to the annual definition of the Group Industrial Plan and to the proposals for appointment of 1st level Senior Managers, has the task of expressing an opinion prior to presentation to the Board of Directors and also deliberating:

7. as to contracts and conventions in any way pertaining to the corporate purpose worth more Euro 2 million per single contract;
8. in the interest of the Company consulting relations with external experts and professional consultants, specifying terms and conditions of payment, worth more than Euro100,000 and up to Euro 500,000 and more generally on the overall criteria for use;
9. as to the Company's subscription to bodies, associations, entities of a scientific and technical nature or pertaining to studies and research within the Company's field of interest, for which fees do not constitute an interest in the equity of said entity and for which participation involves an outlay of more than Euro 100,000 and up to Euro 500,000.
10. to settle disputes and/or waive credits of an amount exceeding Euro 1,000,000;
11. as to the activation, amendments and termination of contracts for the opening of credit, loans of any type and duration which involve a commitment of more than Euro 1,000,000 and up to Euro 5,000,000; request the drawdown of tranches of loans, for an amount of more than Euro 3,000,000 and up to Euro 5,000,000 per single contract;
12. as to the stipulation, amendment and termination of contracts relating to:
    - works and supplies necessary to the transformation and maintenance of properties and plants worth more than €15,000,000;
    - *purchase and disposal of furniture, fittings, machinery and moveable assets in general, including those enrolled in public registers worth more than € 8,000,000*

As at 27 March 2006 the Executive Committee has held one meeting, at which all the members were present.

Nomination and Remuneration of Directors

Article 17 of the By-Laws attributes to the local authorities holding shares the faculty to nominate, pursuant to Article 2449 of the Italian Civil Code, 14 members of the Board of Directors. In practice this means that:
the Municipality of Bologna has the right to nominate 4 directors; the Province of Bologna, including on behalf of 47 Municipalities, has the right to nominate 1 director; the Municipality of Cesena, including on behalf of another 25 Municipalities, has the right to nominate 1 director; Con.Ami has the right to nominate 1 director; the Municipality of Forlì has the right to nominate 1 director, the Municipality of Ravenna, including on behalf of another 11 other Municipalities, has the right to nominate 1 director, the Municipality of Rimini, including on behalf of another 26 Municipalities, has the right to nominate 1 director, the Municipality of Ferrara, including on behalf of another 9 Municipalities, has the right to nominate 1 director, the Municipality of Modena, including on behalf of another 30 Municipalities, has the right to nominate 3 director.

The other 4 members of Board of Directors not nominated by local authorities will be nominated by the Shareholders' Meeting on the basis of the list vote system provided for by Article 17 of the By-Laws which specifies that the list must be presented by shareholders representing at least 1% of shares with voting rights and must be filed, at the Company's registered office at least 20 days prior to the date set for the Shareholders' Meeting, together with the curriculum vitae of the candidates, their irrevocable acceptance of the appointment and a certificate verifying that there are no grounds for ineligibility and/or forfeiture.
These lists will be made public through notice published in three national newspapers of which two financial, at least 10 days prior to the Shareholders' Meeting. The local authorities entitled to effect direct nominations pursuant to Article 2499 of the Italian Civil Code must abstain from presenting lists and voting.

The local authorities holding shares have entered into a Voting Trust and Share Transfer Rules Agreement which provides clauses on the composition of the Board of Directors.

There are also two consultation pacts that provide for clauses on the composition of the Board of Directors and in particular:

3) pact of consultation signed on 16 September 2003 and most recently modified on 27 July 2005 by 30 minority shareholders of HERA S.p.A.;
4) pact of consultation signed on 6 November 2003 and most recently modified on 14 September 2005 by 5 minority shareholders of HERA S.p.A .

The Shareholders' Meeting of 28 April 2005 awarded the directors a fixed annual remuneration.

The Board of Directors, in the meetings of 30 May 2005 and 6 February 2006, deliberated to award the Chairman and the Managing Director a remuneration comprising a fixed amount, inclusive of the indemnity due thereto, as well as a further variable annual consideration linked to the Company's operating results or to the reaching of specific targets set by the Remuneration Committee (in this case the Remuneration Committee linked the variable annual consideration to the Company's achievement of set indexes for EBITDA, Net Profit and NFP of the Hera Group).

In the meeting of 30 May 2005, the Board of Directors also awarded, only to the directors holding specific roles, a further fixed annual remuneration over and above the consideration due thereto as directors, for serving on other Boards of Directors of Group companies and/or other boards associated with the Company's Board of Directors.
In the meeting of 16 January 2006, the Board of Directors passed a resolution to award the Vice Chairman a fixed annual remuneration inclusive of the consideration due thereto as director and of any other consideration for offices held within Group companies.

Committees

The Committees constituted are representative of the Board of Directors and fulfil an advisory and consultative role.

a) Remuneration Committee

In the meeting of 4 November 2002, the Board of Directors, in compliance with the provisions of the Code, constituted the Remuneration Committee with the role of formulating proposals to the Board of Directors for the remuneration of the Managing Director, the Chairman and the directors holding particular roles, as well as on the basis of indications provided by the Managing Director, for the adoption of general criteria for the remuneration of management, without prejudice to the Managing Director's duty to define policies and levels of management remuneration.

This Committee is composed of Giorgio Razzoli (appointed on 16 January 2006) as Chairman, Pierluigi Celli (appointed on 11 May 2005), Piero Collina (appointed on 11 May 2005) and of Nicodemo Montanari (appointed on 11 May 2005). The Chairman of the Board of Directors and the Managing Director may attend the Committee meetings upon express invitation of the Chairman of the Committee.

In the year 2005 the Committee held 4 meetings during which it defined the guidelines of the Remuneration Policy for the Management of the Group for the year 2005.

b) Internal Control System and Internal Control Committee

An Internal Auditing function has been set up within the Company, and the person in charge reports directly to the Managing Director.

The person responsible for Internal Auditing provides a report of his activity, on a quarterly basis or whenever he considers it necessary, to the Managing Director, to the Chairman of the Board of Directors, to the Internal Control Committee and to the Board of Statutory Auditors.

In terms of hierarchy he is not subordinate to the heads of the operating divisions.
In compliance with the provisions of the Code, the Board of Directors of the Company, in the meeting of 4 November 2002, passed a resolution to set up an Internal Control Committee with advisory and consultation functions. This committee is composed of Giorgio Razzoli (appointed on 16 January 2006), as Chairman, Ermanno Vichi (appointed on 11 May 2005) and Stefano Zolea

(appointed on 11 May 2005). The Chairman of the Board of Statutory Auditors or another Statutory Auditor designated by the Chairman and, upon express invitation of the Chairman of the Committee, the Managing Director and the Chairman of the Board of Directors, may attend the Committee's meetings. The Committee has been assigned the functions indicated at paragraph 10.2 of the Code.

The Internal Control Committee met 5 times in 2005; 4 meetings were attended by all of the members while 1 meeting was attended by the majority of members.
The Chairman of the Board of Statutory Auditors attended all of the meetings.

During the above-mentioned meetings the audit plan was assessed as were the audit activities performed.

c) Committee for the Proposal of Nominations

A Committee for the proposal of nominations to the office of Director has not been set up as pursuant to the By-Laws the nomination of 14 directors is the responsibility of the local authorities as per Article 2449 of the Italian Civil Code and that of the other 4 directors is the responsibility of the remaining shareholders through the list vote system.

Treatment of Confidential Information

The Board of Directors of the Company, in the meeting of 10 March 2003, passed a resolution to approve the code of conduct for the members of the corporate boards and the employees of the Company and subsidiary companies – "Internal Dealing" – which was adopted by the Company as from the date in which trading commenced (26 June 2003).

The aforesaid code, drawn up on the basis of the Regulations and Instructions of Borsa Italiana S.p.A., governs the reporting obligations relating to transactions on financial instruments carried out by Directors, the General Director and the Statutory Auditors of the Company, as well as by any other person who has access, by virtue of the office held in the Company and in its main subsidiaries, to information on facts such as to determine significant variations in the economic and financial prospects of the Company and of the Group and capable, if made public, of significantly influencing the price of the relative financial instruments (so called "significant persons" or "internal dealers").

The provisions of the code of conduct are binding for "significant persons". The persons considered as such are:
(i) the Directors, Standing Auditors and General Director;
(ii) General Management and Divisional Managers;
(iii) persons in the Company and its main subsidiaries (that is, the companies whose revenues exceed 10% of the total consolidated revenues), identified by the Managing Director, each in relation to his area of competence, who, by virtue of the role held in the pertinent company, may have access to information on facts such as to determine significant variations in the economic and

financial prospects of the Company and the Group and capable, if made public, of significantly influencing the price of the relative listed financial instruments issued by the Company.

Communications from significant persons must be sent to the person responsible for the Legal and Corporate Affairs Department. This person will liaise with the person responsible for investor relations for disclosure to the market of the information through the electronic system NIS (Network Information System).

The Code of Conduct is published on the Company's website www.gruppohera.it

Transactions with Related Parties

In relation to the recommendations contained in Articles 5 and 11 of the Code of Conduct and in order to guarantee that any significant transactions with related parties are implemented in compliance with the criteria of substantial and procedural correctness, the Board of Directors on 27 May 2003 adopted the following procedure:

1) The Board identified the related parties as:
a) parties that control, are controlled by, or are subject to common control with the issuer;
b) the parties subscribing, even indirectly, to the shareholders' agreements as set forth in Article 122, sub-section 1 of the Finance Act 58/1998, referring to the exercise of the voting right, if these agreements are vested with a total controlling interest;
c) the parties related to the issuer and those which exercise a significant influence on the issuer;
d) those who are assigned powers and responsibilities pertaining to the exercise of functions of administration, direction and control of the issuer;
e) close family members of the individual persons included in letters a), b), c), and d);
f) the parties controlled by the individual persons included in letters b), c), d) and e) and over which the individual persons included in letters a), b), c), d) and e) exercise a significant influence;
g) the entities that share the majority of the directors with the issuer.

2) The Board of Directors approves in advance the transactions with related parties, including inter-group transactions, except typical or usual transactions or those to be concluded under arm's length conditions as per point 3) below.

3) Typical or usual transactions are those that, due to their subject matter or nature, are not unrelated to the normal business of the Company and those that do not feature critical elements due to their characteristics or risks relating to the nature of the counterpart, or to the time of their fulfilment. Arm's length transactions are those concluded at conditions applied by the Group to any party.

4) The Board of Directors, through the delegated bodies, receives adequate information on the nature of the relation, on the procedures for execution of the transaction, on the conditions, including those of an economic nature, for its implementation, on evaluation procedures followed, on the interests and on the underlying reasons, and on any risks for the Company. Where the

relation is with a Director or with a party related through a Director, the Director in question will do no more than provide clarification and absent himself from the meeting during deliberation.

5) Based on the nature, value and other characteristics of the transaction, the Board of Directors, in order to avoid that the transaction is carried out at inappropriate conditions, may be assisted by one or more experts who express an opinion, as the case may be, on the economic conditions and/or on the legitimacy and/or on technical aspects of the transaction.

6) For the transactions with related parties, including inter-group transactions, that are not submitted to the Board of Directors, in that typical or usual and/or at arm's length conditions, the delegated bodies, without prejudice to compliance with procedures as per Article 150, sub-section 1, of the Finance Act 58/1998, gather and conserve, including by type or groups of transactions, adequate information on the nature of the relation, on the procedures for execution of the transaction, on the conditions, including those of an economic nature, for its implementation, on the evaluation procedures followed, on the interests, and on the underlying reasons and on any risks for the Company.
One or more experts may also be nominated for these transactions, in accordance with the above procedures.

7) The experts selected must be recognised professionals and experts on the subject matter, of whom the independence and the absence of conflicts of interest will be carefully assessed.

The most important transactions with related parties during 2005 are specifically reported in the Directors Report.

Relations with Shareholders

In order to favour a more detailed knowledge of the Company on the part of the shareholders, the Company has set up a special structure dedicated to investors relations. On 11 March 2003, Mr. Jens Klint Hansen was appointed as head of investor relations (Investor Relations may be contacted through the telephone number + 39 051 287737 or the email address ir@gruppohera.it).

The Shareholders' Meeting of 29 April 2003 approved the Shareholders' Meeting Regulations. These regulations indicate the procedures to be followed in order to permit the orderly and proper functioning of meetings, without prejudice to the right of each shareholder to express his opinion on the matters under discussion.

The Shareholders' Meeting Regulations are published on the Company's website www.gruppohera.it

Statutory Auditors

The Board of Statutory Auditors is composed of three standing members. Two alternative members have also been appointed. The Board of Statutory Auditors will remain in office until approval of the financial statements for the year ended 2007.

Composition of the Board of Statutory Auditors

Name and surname	Office
Antonio Venturini	Chairman
Fernando Lolli	Standing Auditor
Sergio Santi (*)	Standing Auditor
Stefano Ceccacci (*)	Alternate Auditor
Roberto Picone	Alternate Auditor

(*) appointed by the Shareholders' Meeting of 28 April 2005 on the basis of the only list presented by the minority shareholders in compliance with the provisions of legislation in force.

The By-Laws provide that the Statutory Auditors must possess the requirements of integrity and professionalism established by legislation in force.

For the purposes of the provisions of legislation in force concerning the requirements of professionalism of the members of the Board of Statutory Auditors of listed companies, subject matter and sectors of activity strictly relating to the activities carried out by the company are intended to mean the subject matters and sectors connected or relating to the activity exercised by the company and set forth in Article 4 of the By-Laws.

The office of statutory auditor is not compatible with that of councillor or alderman in local public authorities, or with that of statutory auditor in more than 3 listed companies with the exclusion of the subsidiaries of the Company pursuant to Articles 2359 of the Italian Civil Code and 93 of the Legislative Decree 58/98. In this latter case, the statutory auditor that subsequently exceeds said limit automatically falls from office as statutory auditor of the company.

The statutory auditors are nominated by the Shareholders' Meeting on the basis of the list vote system provided by Article 26 of the By-Laws which specifies that (i) the Municipalities, the Provinces and the Consortiums constituted pursuant to Article 31 of the Legislative Decree 267/2000 and the consortiums or the joint-stock companies controlled by these may present a single list and (ii) the shareholders other than those indicated in point (i) may present lists provided they represent at least 3% of the shares with voting rights. The lists must be filed at the registered office at least 20 days prior to the date of the Shareholders' Meeting, together with the declaration of the individual candidates certifying the inexistence of grounds for ineligibility or incompatibility provided by law, as well as existence of requirements of integrity and professionalism as required by law for the members of the Board of Statutory Auditors.
These lists will be made public through notification in three national newspapers of which two financial newspapers, at least 10 days prior to the Shareholders' Meeting.

The Shareholders' Meeting of 28 April 2005 appointed the new members of the Board of Statutory Auditors designated by a list presented by Public Shareholders representing over 3% of the shares with voting rights and from a minority list in order to comply with the obligations of the law.

The Board of Statutory Auditors held 14 meetings, of which 11 were attended by all the members and 3 by the majority of members.

The local authorities holding shares have entered into a Voting Trust and Share Transfer Rules Agreement which provides clauses on the composition of the Board of Statutory Auditors.

There are also two consultation pacts that provide for clauses on the composition of the Board of Statutory Auditors and in particular:

3) pact of consultation signed on 16 September 2003 and most recently modified on 27 July 2005 by 30 minority shareholders of HERA S.p.A.;
4) pact of consultation signed on 6 November 2003 and most recently modified on 14 September 2005 by 5 minority shareholders of HERA S.p.A .

Administrative Responsibility of the Company

Legislative Decree 231/2001 introduced into Italian legislation the administrative responsibility of legal entities, companies and associations. In particular, the law introduced the penal responsibility of entities for certain offences committed in the interest or to the advantage of the same by persons fulfilling roles of representation, administration or management of the entity or one of its organisational units with financial and operating independence, as well as persons who exercise, even de facto, management and control thereof and, lastly, persons subject to the direction or supervision of one of the above mentioned parties. The important offences are the offences against Public Administration and corporate offences committed in the interest of the companies.

However, Articles 6 and 7 of Legislative Decree 231/2001 provides for a form of exoneration from the responsibility where (i) the entity proves that it adopted and efficiently implemented, prior to commitment of the act, organisational, management and control models appropriate to preventing the perpetration of the offences considered by said decree; and (ii) the duty of supervising the effectiveness of and compliance with the models, as well as providing for their revision, is entrusted to a board of the entity vested with autonomous powers of initiative and control.
For this purpose, on 16 February 2004, the Board of Directors of Hera SpA approved the organisational, management and control model pursuant to Legislative Decree 231/2001 with the aim of creating a structured and organic system of procedures and control activities directed at preventing the offences referred to in the aforesaid decree, through identification of activities exposed to the risk of offence and the consequent implementation of procedures therein.

Hence the Board of Directors set up the supervision board composed of the Head of Internal Auditing of Hera SpA as the Chairman, the Head of Legal and Corporate Affairs of Hera SpA and an external member to which it entrusted the aforesaid duties including the periodic reporting to the corporate boards of Hera SpA on the implementation of the said model.

The Supervision Board met 6 times in 2005; all the meetings were attended by all the members.

The Supervision Board provided for the revision of the organisational model which was extended to the other Group companies. The Supervision Board also applied and analysed the information flows that permits the Board to supervise the effectiveness of and compliance with the models.
In order to carry out the verifications and controls, the Supervision Board drew up a schedule of interventions to verify compliance with the protocols adopted.

The Company also adopted an Ethical Code which was approved by the Board of Directors on 16 February 2004 and was widely circulated to both employees and stakeholders.

TABLE 1 : STRUCTURE OF THE BOD AND OF THE COMMITTEES

UP TO 28.04.2005

Board of Directors

Office	Members	executive	non-executive	independent	****	Number of other offices **	Internal Control committee ***	****	Remuneration Committee ***	****	Nomination Committee (where present) ◊ ***	****	Executive Committee (where present) ***	****
Chairman	Tomaso Tommasi di Vignano		X	X	100%									
Managing Director	Stefano Aldrovandi	X			100%									
Director	Aleardo Benuzzi		X	X	100%				X	100%				
Director	Enrico Biscaglia		X	X	71%		X	100%						
Director	Filippo Brandolini		X	X	100%						Not present		Not present	
Director	Piero Collina *		X	X	100%				X	100%				
Director	Pier Giuseppe Dolcini *		X	X	86%									
Director	Nicodemo Montanari		X	X	86%									
Director	Fabio Roversi Monaco *		X	X	57%		X	100%						
Director	Roberto Sacchetti		X	X	86%									
Director	Giovanni Tamburini		X	X	71%									
Director	Fulvio Vento		X	X	86%									
Director	Ermanno Vichi		X	X	86%		X	100%						

_ Summary of the reasons fo r absence (where applicable) of the Committee or composition differing from Code recommendations:

_ Summary of the reasons for absence (where applicable) of the Committee or composition differing from Code recommendations:

◊ Summary of the reasons for ab sence (where applicable) of the Committee or composition differing from Code recommendations: **the Committee was not set up insofar as pursuant to the By -Laws 11 directors are to be appointed by the public authorities as per Article 2449 Italian Civil Code and the other 3 through the list vote system**

Number of meetings held during the period under review (up to 28.04.2005)	BOD: 7	Internal Control Committee: 1	Remuneration Committee: 1	Nomination Committee: /	Executive Committee: /

NOTE

* The presence of asterisks indicates whether the director was appointed through lists presented by minority shareholders

** This column indicates the number of offices as director or statutory auditor the party concerned holds in other companies listed on regulated markets, including foreign markets, in financial, banking, insurance companies or large enterprises

*** In this column an "X" indicates the Board member's membership of the Committee

**** This column indicates the percentage of attendance of the directors in the Board meetings and Committee meetings respectively

TABLE 1 : STRUCTURE OF THE BOD AND OF THE COMMITTEES FROM 28.04.2005

Board of Directors							Internal Control Committee _		Remuneration Committee _		Nomination Committee (where present) ◊		Executive Committee from 6.01.2006	
Office	Members	esecutive	non-esecutive	independent	****	Number of other offices **	***	****	***	****	***	****	***	****
Chairman	Tomaso Tommasi di Vignano	X			100%								X	-
Managing Director	Maurizio Chiarini	X			93%								X	-
Director	Giorgio Razzoli (from 31.12.2005)		X	X	-		X	-	X	-			X	-
Director	Mara Bernanrdini (from 31.12.2005)		X	X	-									
Director	Filippo Brandolini		X	X	93%						Not present			
Director	Luigi Castagna		X	X	100%									
Director	Pier Luigi Celli		X	X	73%				X	67%				
Director	Piero Collina *		X	X	87%				X	100%				
Director	Pier Giuseppe Dolcini *		X	X	87%									
Director	Giuseppe Fiorani (from 31.12.2005)		X	X	-									
Director	Vander Maranini		X	X	93%		X	75%						
Director	Nicodemo Montanari		X	X	93%				X	100%				
Director	Fabio Roversi Monaco *		X	X	87%									
Director	Roberto Sacchetti		X	X	100%									
Director	Luciano Sita		X	X	80%									
Director	Ermanno Vichi		X	X	100%		X	100%						
Director	Stefano Zolea		X	X	100%		X	100%						

_ Summary of the reasons for absence (where applicable) of the Committee or composition differing from Code recommendations:
_ Summary of the reasons for absence (where applicable) of the Committee or composition differing from Code recommendations:
◊ Summary of the reasons for absence (where applicable) of the Committee or composition differing from Code recommendations: **the Committee was not set up insofar as pursuant to the By -Laws 14 directors are to be appointed by the public authorities as per Article 2449 Italian Civil Code and the other 4 through the list vote system**

Number of meetings held during the period under review (from 28.04.2005)	BOD: 15	Internal Control Committee: 4	Remuneration Committee: 3	Nomination Committee: /	Executive Committee: -

NOTE
* The presence of asterisks indicates whether the director was appointed through lists presented by minority shareholders
** This column indicates the number of offices as director or statutory auditor the party concerned holds in other companies listed on regulated markets, including foreign markets, in financial, banking, insurance companies or large enterprises
*** In this column an "X" indicates the Board member's membership of the Committee
**** This column indicates the percentage of attendance of the directors in the Board meetings and Committee meetings respectively

TABLE 2 : BOARD OF STATUTORY AUDITORS

Office	Members	Percentage attendance of Board meetings	Number of other offices **
Chairman	Venturini Antonio	100%	-
Standing Auditor	Fernando Lolli	93%	-
Standing Auditor *	Sergio Santi	93%	2
Alternate Auditor *	Stefano Ceccacci	-	-
Alternate Auditor	Roberto Picone	-	-

Number of meetings held in the calendar year: 14

Indicate the quorum required for the presentation of lists on the part of minority shareholders for the election of one or more standing members: Article 26 of the By - Laws specifies that (i) the Municipalities, the Provinces and the Consortiums pursuant to Article 31 of Legislative Decree no. 267/2000 as well as the consortiums and joint -stock companies in any case controlled by said entities may present a single list and (ii) the shareholders other than those indicated at point (i) may present lists provided that the y represent at least 3% of the shares with voting right .

NOTE
* The asterisk indicates whether the statutory auditor has been designated through lists presented by minority shareholders.
**This column indicates the number of offices as director or stat utory auditor the party concerned holds in other companies listed on regulated Italian markets.

TABLE 3: OTHER PROVISIONS OF THE CODE OF CONDUCT

	YES	NO	Summary of the reasons for any deviation from the Code recommendations
System of delegated powers and transactions with related parties			
Has the BOD delegated powers defining:			
a) limits	X		
b) procedures for exercise	X		
c) frequency of reporting?	X		
Has the BOD reserved the right to examine and approve the transactions of particular importance in financial and economic terms (including transactions with related parties)?	X		
Has the BOD defined guidelines for the identification of "important" transactions?		X	The BOD has not defined the guidelines and criteria for the identification of "important" transactions, however the delegated bodies provide prior report to the BOD and spontaneously submit to the approval thereof the transactions of greater importance in economic, strategic and financial terms.
Are the above guidelines described in the report?		X	
Has the BOD defined special procedures for approval of the transactions with related parties?	X		
Are procedures for approval of the transactions with related parties described in the report?	X		
Procedures for the most recent nomination of directors and statutory auditor			
Were the nominations for the office of director filed at least 10 days in advance?	X		
Were the nominations for the office of director accompanied by exhaustive information?	X		
Were the nominations for the office of director accompanied by specification of suitability to qualify as independent?		X	The By-Laws do not make provision for this, however following appointment, the directors have filed appropriate declaration certifying the existence of the requirement of independence.
Were the nominations for the office of statutory auditor filed at least 10 days in advance?	X		
Were the nominations for the office of statutory auditor accompanied by exhaustive information?	X		

	YES	NO	Summary of the reasons for any deviation from the Code recommendations
Shareholders' Meetings			
Has the company approved Shareholders' Meeting Regulations?	X		
Are the Regulations attached to the report (or is it specified where they may be obtained/downloaded?)	X		
Internal Control			
Has the company appointed the persons in charge of internal control?	X		
In terms of hierarchy are the persons in charge non-subordinate to the heads of the operating divisions?	X		
Organisational unit in charge of internal control (pursuant to Article 9.3 of the Code)	X		
Investor relations			
Has the company appointed a person responsible for investor relations?	X		
Organisational unit and references (address/telephone/fax/e-mail) of the person responsible for investor relations	*Jens Klint Hansen (HERA S.p.A. V.le Carlo Berti Pichat 2/4, 40127 Bologna / telephone +39 051 287737 / fax 051 287224 / e-mail ir@gruppohera.it.*		

3.01.11 Performance of Hera SpA in 2005

The main highlights are presented below.

(Euro millions)	2004	2005	Change %
Value of production	1,268.1	1,597	25.9%
EBITDA	178.9	248.6	39.0%
EBIT	48	76.6	59.6%
Net profit	59.4	75.4	26.9%

The interpretation of the results must also take into consideration the current economic set-up of the Group, which sees the distribution of the total result between the Parent Company and the various sales, operational and maintenance companies and specific business units. For this reason, there was a shift in Hera S.p.A.'s profitability towards the dividend component from subsidiaries and towards the results of financial operations and equity investments. The implementation of the service contracts between the different units of the Group also led to an increase in the value of production and the EBITDA.

A summary is presented below of the reclassified balance sheet and financial position as at December 31, 2005, shown on a comparative basis with the balances as at December 31, 2004:

Analysis of the capital employed and the sources of financing

(milioni di euro)	31-dic-04	%	31-dic-05	%	Var ass	Var %
Immobilizzazioni Immateriali	*334,3*	*22,9%*	*359,0*	*16,4%*	*24,7*	*7,4%*
Immobilizzazioni Materiali	*820,8*	*56,3%*	*1.247,3*	*56,8%*	*426,5*	*52,0%*
Immobilizzazioni finanziarie	*371,9*	*25,5%*	*492,4*	*22,4%*	*120,5*	*32,4%*
Totale immobilizzazioni	1.527,0	104,7%	2.098,7	95,6%	571,7	37,4%
Capitale circolante netto	91,8	6,3%	319,7	14,6%	227,9	248,2%
(Fondi)	(160,5)	(11,0%)	(224,0)	(10,2%)	(63,5)	39,6%
Capitale Investito Netto	**1.458,3**	**100,0%**	**2.194,3**	**100,0%**	**736,0**	**50,5%**
Patrimonio Netto	965,1	66,2%	1.256,5	57,3%	291,4	30,2%
Debiti finanziari a lungo	*347,1*	23,8%	*390,7*	17,8%	*43,6*	12,6%
Posizione netta a breve	*146,1*	10,0%	*547,1*	24,9%	*401,0*	274,5%
Posizione Finanziaria Netta	493,2	33,8%	937,8	42,7%	444,6	90,1%
Totale fonti di finanziamento	**1.458,3**	**100,0%**	**2.194,3**	**100,0%**	**736,0**	**50,5%**

Analysis of the capital employed and the sources of financing

(Euro millions)	**31 Dec. 04**	**%**	**31 Dec. 05**	**%**	**Change**	
					Amount	**%**
Intangible assets	*334.3*	*22.9%*	*359.0*	16.4%	*24.7*	*7.4%*
Tangible assets	*820.8*	*56.3%*	*1,247.3*	56.8%	*426.5*	*52.0%*
Financial assets	*371.9*	*25.5%*	492.4	22.4%	120.5	*32.4%*
Total fixed assets	1,527.0	104.7%	2,098.7	95.6%	571.7	*37.4%*
Net working capital	91.8	6.3%	319.7	14.6%	227.9	*248.2%*
(Provisions)	(160.5)	(11.0%)	(224.0)	(10.2%)	(63.5)	*39.6%*
Net capital employed	**1,458.3**	**100.0%**	**2,194.3**	**100.0%**	**736.0**	**50.5%**
Shareholders' equity	965.1	66.2%	1,256.5	57.3%	291.4	*30.2%*
Long-term debt	*347.1*	23.8%	*390.7*	17.8%	*43.6*	*12.6%*
Net short-term position	*146.1*	10.0%	*547.1*	24.9%	*401.0*	*274.5%*
Net financial position	493.2	33.8%	937.8	42.7%	444.6	*90.1%*
Total sources of financing	**1,458.3**	**100.0%**	**2,194.3**	**100.0%**	**736.0**	**50.5%**

The net capital employed increased as at December 31, 2005 by Euro 736.0 million, rising from Euro 1,458.3 million to Euro 2,194.3 million.

Fixed assets as at December 31, 2005 amounted to Euro 2,098.7 million, up by Euro 571.7 million when compared with December 31, 2004, in relation to the integration of the Modena companies and the investments made which are more fully described in the Group's report on operations.

The net working capital rose from Euro 91.8 million to Euro 319.7 million, mainly in relation to the billing problems linked to the start-up of the new customer computerised information system during the period, as mentioned previously.

Provisions increased both as a result of the merger of the Modena companies, the normal provision made to the Provision for Employee Leaving Indemnities (TFR) and the provision of the portions for restoring the networks and plants granted under use to the Group as owned by the asset companies.

The shareholders' equity, which rose from Euro 965.1 million to Euro 1,256.5 million, includes the share capital increase relating to the inclusion within the shareholding structure of the Municipal authorities associated with the Modena integration operation.

In relation to the afore-mentioned share capital increases, the net financial position passed from Euro 493.2 million as at December 31, 2004 to Euro 937.8 million at the end of 2005.

The increase in fixed assets (Euro 571.7 million) is partly covered by the increase in shareholders' equity (Euro 291.4 million) and partly by the rise in the short-term net financial position.

So as to re-balance the financial structure, in February 2006 the Group issued a 10-year bond totalling Euro 500 million.

3.01.12 Holdings of Directors, Statutory Auditors and General Managers (Article 79 of the Consob Regulations)

HOLDINGS OF DIRECTORS, STATUTORY AUDITORS AND GENERAL DIRECTOR (ART. 79 CONSOB REGULATIONS)

NAME	OFFICE HELD IN HERA S.p.A.	COMPANY	NUMBER OF SHARES HELD AS AT DECEMBER 31, 2004	NUMBER OF SHARES ACQUIRED	NUMBER OF SHARES SOLD	NUMBER OF SHARES HELD AS AT 31 DECEMBER 2005
Tomaso Tommasi di Vignano (1)	Chairman	Hera S.p.A.	8.000	2.000	-	10.000
Maurizio Chiarini	Managing Director	Hera S.p.A.	-	-	-	-
Giorgio Razzoli	Vice Chairman	Hera S.p.A.	-	-	-	-
Mara Bernardini	Director	Hera S.p.A.	-	-	-	-
Filippo Brandolini	Director	Hera S.p.A.	2.750	-	-	2.750
Luigi Castagna (1)	Director	Hera S.p.A.	250	1.700	-	1.950
Pier Luigi Celli	Director	Hera S.p.A.	-	-	-	-
Piero Collina	Director	Hera S.p.A.	-	-	-	-
Pier Giuseppe Dolcini	Director	Hera S.p.A.	2.750	-	-	2.750
Giuseppe Fiorani	Director	Hera S.p.A.	-	-	-	-
Vander Maranini	Director	Hera S.p.A.	-	-	-	-
Nicodemo Montanari	Director	Hera S.p.A.	-	-		-
Fabio Alberto Roversi Monaco	Director	Hera S.p.A.	-	36.000	-	36.000
Roberto Sacchetti	Director	Hera S.p.A.	-	-	-	-
Luciano Sita	Director	Hera S.p.A.	-	-	-	-
Vichi Ermanno	Director	Hera S.p.A.	-	-	-	-
Stefano Zolea	Director	Hera S.p.A.	-	-	-	-
Antonio Venturini	Chairman Board of Statutory Auditors	Hera S.p.A.	-	-	-	-
Fernando Lolli	Member Board of Statutory Auditors	Hera S.p.A.	-	-	-	-
Sergio Santi	Member Board of Statutory Auditors	Hera S.p.A.	-	-	-	-
Roberto Barilli	General Manager	Hera S.p.A.	-	25.000	-	25.000
Stefano Aldrovandi (in carica fino al 28.4.2005)	Managing Director	Hera S.p.A.	-	-	-	-
Aleardo Benuzzi (in carica fino al 28.4.2005)	Vice Chairman	Hera S.p.A.	2.750	-	-	2.750
Enrico Biscaglia (in carica fino al 28.4.2005)	Director	Hera S.p.A.	-	-	-	-
Giovanni Tamburini (in carica fino al 28.4.2005)	Director	Hera S.p.A.	-	10.895	-	10.895
Fulvio Vento (in carica fino al 28.4.2005)	Director	Hera S.p.A.	-	-	-	-

(1) held indirectly through spouse

3.01.13 Significant Events after Year-End

The most important events for the activities of the Group in the first months of 2006 are summarised below.

- ***A1 Rating from Moody's***

  On 27 January 2006 Moody's, the leading international rating agency, assigned the Hera Group A1 rating, with stable outlook, for the first time.

  Standard & Poor's also confirmed the Group's A+ rating, passing the outlook from stable to negative in the event of further acquisitions being planned for Hera, which however is not a circumstance envisaged by the Group's Industrial Plan.

  Hence Hera has become the only Italian public utility that can boast the double rating assigned by these two prestigious agencies.

  The rating level achieved reflects the Group's financial solidity and assumes even greater value in connection with the subsequent bond issue on the international markets. The principal grounds for the award of this rating lie in the fact that the company features a strong business profile, with a very balanced portfolio, provides excellent service levels in one of Europe's richest regions and enjoys share solidity and financial liquidity.

- ***First bond issue of the Hera Group***

  On 17 February 2006, with admission to trading on the Luxembourg Stock Exchange, the Group took the last step in the procedure, which began on the 27 January 2006 with the launch of the international roadshow to present the transaction to the market, which led Hera to its first bond issue.

  The issue, which has a 10 year duration and annual coupon detachment at a fixed rate of 4.125%, concluded with a success rate that surpassed even the most optimistic previsions. Demand was in the region of €2.2 billion (4.4. times higher than the offer of €500 million) and allowed Hera to reduce the credit spread to 47 basic points, above the mid-swap rate for the period, compared to the initial indications of 50 base points.

  The placement was implemented by the merchant banks JPMorgan, Citibank and Banca IMI.

- ***Purchase of own shares***

  On 16 January 2006, the Board of Directors of Hera approved an initiative for the repurchase of own shares for a counter-value of up to €45 million. This initiative will be submitted to the approval of the Shareholders' Meeting and shall be valid for 18 months.

  The shares purchased may be used within the scope of acquisitions transactions which involve share trades.

  The purchase will be effected on the market managed by Borsa Italiana S.p.A. at a price per share no lower than the nominal value and no higher than 5% compared to the reference price recorded in the market day preceding each purchase.

  To date Hera does not hold own shares and the maximum number of own shares that may be purchased is equal to 15,000,000 ordinary shares, the equivalent of approximately 1.5% of share capital.

- ***Merger through incorporation of Geat Distribuzione Gas***

  On 16 January 2006, the Board of Directors of Hera approved the project for merger through incorporation in the Hera Group of Geat Distribuzione Gas, the company which operates in the distribution of gas in the Riccione area and, through its subsidiary Gas Riccione, in the sales to end customers.

  The transaction, of which the value has been established as €12.5 million, allows Hera to continue the process of consolidation with its own reference territory, which in 2005 saw integration of Meta and acquisition of three local operators serving the municipalities of Ro Ferrarese, Castello d'Argile and Monghidoro for a total of approximately 147,000 customers.

  The transaction with Geat Distribuzione Gas represents a strategic element which allows the Group to create, together with the equity investment already held in the company SGR Servizi, a core unit in the province of Rimini with significant opportunities for synergy.

  The company Geat has over 20,000 customers and achieves sales to the order of approximately 40 million m^3 of natural gas. The transaction is scheduled to be concluded next summer, while the effects will commence as from 1 January 2006.

- ***Increase of the equity investment held in Hera Luce S.r.l.***

  On 17 January 2006 Hera S.p.A. acquired the share held by Gemmo S.p.A. (equal to 18% of share capital) in Hera Luce S.r.l., the company which manages the public lighting service activities, hence bringing its interest to 87.3%.

- ***Purchase from Enel of the electricity grid of 18 Municipalities of the Province of Modena***

  On 13 March 2006 Hera and Enel signed the preliminary agreement for disposal of the Enel distribution grid of 18 Municipalities of the Province of Modena for a total consideration of approximately Euro 107.5 million. The business unit at issue includes 80,000 customers and over 3,700 km serving the Municipalities of Castelnuovo Rangone, Fanano, Fiumalbo, Guiglia, Lama Mocogno, Marano sul Panaro, Montecreto, Contese, Pavullo nel Frignano, Pievepelago, Polinago, Riolunato, San Cesario sul Panaro, Sestola, Spilamverto, Vignola and Zocca.

- ***Disposal of minority investments in no-core areas***

  The activity of rationalisation of the Group's corporate investments in no-core areas continued and particular mention is given to the following: sale to the Municipalities of Piano di Sorrento and of Meta, of 48% of Penisola Verde S.P.A., a company which supplies environmental services in Campania and sale, to the Municipality of Ferrara, of 20% of Ferrara T.U.A. S.p.A., a company which provides paying parking services.

As far as progress in the projects relating to the new waste-to-energy (WTE) and electricity generating plants is concerned, the following is reported:

- the new WTE plant of Frullo, after having concluded the first year of industrial operation with a total quantity of disposed waste equal to 188.1 Kton (+ 4.7% compared to 2004) and an electricity production equal to 92,09 Gwh (+ 308% compared to 2004), in the first two months of 2006 disposed of a total of 35,000 tonnes of waste and produced over 24,000,000 Kwh, in addition to 12,000,000 of Mcal for district heating;
- the WTE plant of Ferrara (Canalbianco) is under construction and all the orders have been issued; the plant is scheduled to start operations at the end of the first year-half 2007;
- the WTE plant of Forlì was granted final authorisation in September 2005 and all the orders were issued by the end of 2005; the work site is scheduled to open in the forthcoming month of May and plant start-up is scheduled for September 2007;
- the WTE plant of Modena is under construction, all the orders have been issued and plant start-up is scheduled for the end of the second year-half 2007;
- for the WTE plant of Rimini the authorisation process is scheduled to be completed in the forthcoming May; all the orders have been subjected to pre-contract and plant start-up is scheduled for the first year-half 2008;
- the co-generation plant of Imola (80 MW) has been granted final authorisation by the Ministry of the Environment and all the orders have been defined; plant start-up is scheduled for halfway through the second year-half of 2007;
- as far as the Sparanise plant is concerned (800 MW of which Hera holds a 15% interest), the construction works are progressing according to plan and plant start-up is confirmed for the first year-half 2007;
- lastly, as far as the Teverola plant is concerned (400 MW of which Hera holds a 39% interest), the construction activities are nearing completion and plant start-up is confirmed for the end of 2006.

3.01.14 Resolutions on the Results

Dear Shareholders,

The Financial Statements of your Company, as at 31 December 2005, closed with a net profit of Euro 75,413,346.93.

If you are in agreement with the criteria used in drawing up the Financial Statements and the accounting principles adopted, we invite you to approve the following resolutions:

The Shareholders' Meeting

- having acknowledged the Director's Report on operations.
- having acknowledged the Report of the Statutory Auditors;
- having acknowledged the Independent Audit Report;
- having reviewed the financial statements as at 31 December 2005 which closes with a net profit of Euro 75,413,346.93.

resolves

a) to approve the Financial Statements as at 31 December 2005 of Hera SpA and the Director's Report on operations;
b) to allocate the net profit for the year 1 January 2005 – 31 December 2005 equal to Euro 75,413,346.93 as follows:
   - Euro 3,770,667.35 to legal reserve
   - Euro 1,486,789.58 to extraordinary reserve
   - Euro 70,155,890.00 to dividend to the shareholders, corresponding to Euro 0.069 per share, also proposing that payment occurs as from 8 June 2006, with detachment of coupon number 3 on 5 June 2006.

3.02 Attachments to the Consolidated Financial Statements of Hera Group

3.02.01 Income statement

	Note	Dec. 31, 2005 € /000	Dec. 31, 2004 € /000 (Adjusted)
Income statement			
Net sales	4	1.730.723	1.492.572
Change in inventories of finished products and products in work in progress		2.465	9.187
Other operating revenues	5	34.771	27.106
Consumption of raw materials and consumable materials (net of the change of the inventories of raw materials and stocks)	6	-809.571	-622.006
Service costs	7	-440.135	-416.930
Personnel costs	8	-227.639	-215.863
Depreciation, amortisation and provisions		-142.652	-115.256
Other operating expenses	9	-108.038	-92.152
Capitalised costs	9 bis	138.463	110.599
Operating results		**178.387**	**177.257**
Adjustments to technical fixed assets	10	15.518	
Quota of profits/(losses) of associated companies	11	-444	-3.029
Financial income	12	34.359	6.071
Financial charges	12	-74.102	-32.755
Pre-tax result		**153.718**	**147.544**
Income taxes	13	-66.055	-61.083
Discontinued activities			
Profit from discontinued activities			
Net profit/(loss) for the period		**87.663**	**86.461**
Attributable:			
To the shareholders of the Parent Company		80.346	80.994
To the minority shareholders		7.316	5.467
Earning per share		**0.086**	**0.103**

3.02.01 Balance sheet

	Note	Dec. 31, 2005 € /000	Dec. 31, 2004 € /000 (Adjusted)
ASSETS			
Non current assets			
Tangible fixed assets	14	1.914.946	1.298.867
Intangible fixed assets	15	212.847	210.947
Goodwill and consolidation differences	16	273.432	151.610
Equity instruments and securities	17	91.831	78.385
Financial assets	18	54.441	18.903
Deferred tax assets	19	41.474	35.079
Financial instruments - derivatives	20	3.413	0
Other non current assets	21	33.799	43.804
		2.626.183	**1.837.595**
Current assets			
Inventaries	22	35.751	41.513
Trade receivables	23	895.657	597.452
Contract work in progress	24	20.688	14.671
Financial assets	25	13.918	36.827
Other current assets	26	145.527	44.922
Cash and cash equivalents	27	189.107	172.372
		1.300.648	**907.757**
Assets classifed as available for sale			
TOTAL ASSETS		**3.926.831**	**2.745.352**

	Note	Dec. 31, 2005 € /000	Dec. 31, 2004 € /000 (Adjusted)
SHAREHOLDERS' EQUITY AND LIABILITIES			
Share capital and reserves	28		
Share capital		1.016.752	839.903
Reserves		360.020	114.988
Reserve for derivative instruments valued at fair value		-4.185	0
Retained earnings/(Accumulated losses)		0	0
Net profit/(loss) for the period		80.346	80.994
Group shareholders' equity		**1.452.933**	**1.035.885**
Minority interest share		30.603	28.346

Total shareholders' equity		**1.483.536**	**1.064.231**
Non-current liabilities			
Loans - payable beyond one year	29	534.518	489.063
Employee leaving indemnity and other benefits	30	100.902	82.634
Provisions for risk and charges	31	119.923	79.206
Deferred tax liabilities	32	94.614	53.036
Debiti per locazioni finanziarie – scadenti oltre l'esercizio successivo	33	39.859	28.668
Financial instruments - derivatives	20	19.225	
Other non-current liabilities	34	105.344	91.135
		1.014.385	**823.742**
Current liabilities			
Banks and financing - payable within one year	29	645.628	271.832
Lease finance payables - payable within one year	33	9.784	62
Trade payables	35	670.051	432.923
Taxes payable	36	32.545	86.670
Other current liabilities	37	70.902	65.892
Financial instruments - derivatives		0	0
		1.428.910	**857.379**
Liabilities directly associated with assets classified as available for sale			
Total liabilities		**2.443.295**	**1.681.121**
TOTAL SHAREHOLDERS' EQUITY & LIABILITIES		**3.926.831**	**2.745.352**

3.03 Consolidated explanatory notes to the financial statements of the Hera Group

1. INTRODUCTION

HERA S.p.A. (the Company) is a joint-stock company established in Italy and enrolled in the Bologna Companies' Register. The addresses of the registered offices and the locations where the main activities of the Group are carried out are indicated in the introduction to the financial statement dossier. The main activities of the Company and its subsidiaries (the Group) are described in the report on operations.

When comparing the balance sheet balances in the financial statements as at December 31, 2004 and December 31, 2005, it is necessary to take into account that the first do not include the contribution from the Meta Group; the merger by incorporation of the Meta Group into Hera S.p.A. was in fact resolved as at December 31, 2005.

The consolidated balance sheet and income statement schedules and the information included in the explanatory notes are expressed in thousands of Euro, unless otherwise indicated.

2. CONSOLIDATION AREA

The consolidated financial statements of the Hera Group include the financial statements as at December 31, 2005 of the Parent Company, Hera S.p.A., and those of the subsidiary companies. Control is obtained when the Parent Company has the power to determine the financial and operating policies of a company in such a way as to benefit from its activities.

Subsidiary companies whose size is insignificant, where the voting rights are subject to serious and long term restrictions and the subsidiary companies held for the exclusive purpose of their subsequent disposal are excluded from the scope of line-by-line consolidation.

Investments representing non-current assets in associated companies whose size is insignificant are carried at equity. By contrast, dormant companies, in liquidation, or of an irrelevant size are maintained at cost.

The companies held exclusively for the purpose of their disposal are excluded from consolidation and valued at fair value.

There are no companies consolidated under the proportional method.

The list of companies included within the scope of consolidation, including the changes with respect to the previous year, is illustrated at the end of these notes.

3. ACCOUNTING POLICIES AND CONSOLIDATION PRINCIPLES

As from January 1, 2005, the Hera Group adopted the new International Financial Reporting Standards (IFRS) issued by the IASB, the updates to the existing ones (IAS), as well as the documents of the International Financial Reporting Interpretations Committee (IFRIC) deemed applicable to the transactions entered into by the Group as from the current accounting period. These principles are those in force as of the date of these financial statements. The adoption of the IFRS has led to changes in the accounting policies whose impact and the related methods are described in an **APPENDIX** which also contains the statement of reconciliation of the shareholders' equity and net profit for the year as at January 1, 2004 and December 31, 2004.

The financial statements used for the preparation of the consolidated balance sheet and income statement schedules were those which the companies included within the scope of consolidation reclassified and adjusted, for consistency with the accounting policies and principles of the Hera Group, on the basis of specific instructions issued by the Parent Company. Shareholders are informed that a number of associated companies provided financial statements drawn up in accordance with the Italian accounting principles. The effects of the failure to apply the international accounting standards to the Group's balance sheet and income statement are not however significant.

When drawing up the consolidated balance sheet and income statement schedules, the assets and liabilities as well as the income and expenses of the consolidated companies are included on a line-by-line basis. However, the receivables and payables, income and expenses, gains and losses resulting from operations carried out between companies included in the scope of consolidation have been eliminated. The book value of the equity investments is eliminated against the corresponding portion of the subsidiary's shareholders' equity.

The difference between the book value of the equity investments and the corresponding portion of shareholders' equity is recorded in the consolidated shareholders' equity. In the case of acquisitions, the above-mentioned difference is allocated to the assets and liabilities; any remaining difference, if negative, is recorded under the "consolidation reserve" item, or, if it is the result of expected unfavourable economic results, in the account "consolidation provision for future risks and charges"; if it is positive, the difference is recorded as an asset under "consolidation differences". . The total of capital and reserves of subsidiaries pertaining to minority interests is recorded within shareholders' equity in the account "minority interests in capital and reserves". The portion of the consolidated result relating to minority interests is recorded in the account "Net profit (loss) for the year pertaining to minority interests

The dividends from subsidiaries, in which the Parent Company has majority control during shareholders' meetings, are recorded in the year in which they accrue, provided that the draft financial statements of the Parent Company are approved by the Board of Directors of the latter after the approval of the draft financial statements of the subsidiary companies. The consolidation of the subsidiary companies leads to the elimination of the dividends recorded on an accruals basis.

The valuation of the financial statement items has been carried out aspiring to the general criteria of prudence and accruals, with a view to the business as a going-concern. For the purposes of the accounting entries, priority is give to the economic substance of the transactions rather than their legal form.

ACCOUNTING STANDARDS AND POLICIES

Tangible assets - Tangible assets are recorded at acquisition or production cost including accessory costs, or at the value based on expert appraisals of the business assets, net of the related accumulated depreciation and any losses in value. The production cost includes the portion of the direct and indirect costs reasonably attributable to the asset (such as: transport,

customs duty, costs for the preparation of the installation location, final test & inspection costs, notarial fees, land registry expenses). Cost includes any professional fees and, for certain assets, capitalized financial charges up to the moment the asset enters into service. Cost also comprises the costs for reclamation of the site on which the tangible fixed asset exists, if complying with the provisions of IAS 37.

As of the date of changeover to the IFRS – January 1, 2004 – the Group adopted the criteria of fair value as a replacement for cost (fair value as deemed cost) for the tangible fixed assets, applying it selectively to certain categories of assets; the additional value which emerged was credited directly to the reserves. The adoption of the fair value occurred on the basis of an expert appraisal carried out by an independent expert which made it possible, amongst other things, to identify the individual plant and machinery components of a significant amount and with a different useful life, in accordance with the approach for components envisaged by IAS 16.

Ordinary maintenance costs are charged in full to the income statement. Improvement, modernization and transformation costs which increase the value of the assets, are charged to the balance sheet assets concerned.

The book value of tangible fixed assets is subject to assessment so as to identify any losses in value on an annual basis, or when events or changes in circumstances indicate that the book value cannot be recovered (for details, see the section “losses in value – impairment”).

Depreciation starts to be applied when the assets are ready for use. The tangible fixed assets are systematically depreciated in each accounting period using the economic-technical rates considered representative of the residual possible usefulness of the assets. The following tables contain the useful lives taken into account for the depreciation of the assets.

General services	**Min %**	**Max %**
Land	0	0
Buildings	1.50	3.00
Property complex - Via Razzaboni Mo		
- land	0	0
- buildings	1 - 1.25	2 - 2.5
- external building works	1.66	3.33
Light construction	5.00	10.00
General plant	7.50	15.00
Equipment	5.00	10.00
Office furniture and machines	6.00	12.00
EDP machines	10.00	20.00
Vehicles and internal means of transport	10.00	20.00
Automobiles	12.50	25.00
Measurement and laboratory equipment	5.00	10.00
Remote control equipment	10.00	20.00
- remote control apparatus (RTU)	5.00	10.00
- supervision centres	4.16	8.33
- data transmission network (telephone cable)	2.50	5.00
- data transmission network (fibre optics)	3.33	6.67
Public lighting	4.00	8.00
- type 1 centre	2.00	4.00
- type 2 centre	1.25	2.50
- lighting unit (multiple points)	1.25	2.50
- lighting unit (single points/columns)	2.00	4.00
- flux controllers	1.25	2.50
- distribution network	1.43	2.86
- votive lighting	1.66	3.33
Electricity substations	3.50	7.00

Purification service	**Min %**	**Max %**
Land	0.00	0.00
Buildings/Civil works	1.50	3.00
Buildings IDAR construction section	1.50	3.00
General and specific plant	7.50	15.00
Specific IDAR plant	5.00	10.00
Specific ITFI plant	5.00	10.00
Specific plant	5.00	10.00
- Purification plant/Civil works	1.66	3.33
- Purification plant/Installations	3.33	6.67
Lifting plant	6.00	12.00
Laboratory equipment	5.00	10.00
Network	2.50	5.00
Electricity substations	3.50	7.00
Equipment	5.00	10.00
Furniture	6.00	12.00

District heating and gas service	**Min %**	**Max %**
Land	0	0
1st stage pressure reducer stations - Abstraction		
- Buildings	2.50	5.50
- General plant	7.50	15.00
- Specific plant	4.00	10.00
2nd stage pressure reducer stations - district – Specific plant-user stations	5.00	10.00
User transformers – Specific plant	4.00	8.00
Distribution network in steel	2.22	8.00
Distribution network in cast iron or spheroidal cast iron	2.00	8.00
Distribution network in PE or PVC	2.86	8.00
Outlets/Intakes	2.50	8.00
Meters	4.00	10.00
Cathodic protection	4.00	8.00
Electricity substations – Specific plant	3.50	7.00
Cogeneration and district heating:		
- Production – Buildings	2.50	5.50
- Production – General plant	4.50	9.00
- Production – Specific plant	4.50	9.00
Distribution network	2.86	8.00
Meters	2.50	5.00
Heat exchange units	4.50	9.00
- Boilers	1.43	2.86
- Heat exchangers	2.50	5.00
- Expansion tanks	1.66	3.33
Pumping stations		
- Electricity substations	2.00	4.00
- Generators	2.75	4.55
- Pumps	3.33	6.67
- Electricity substations	3.50	7.00
Equipment	5.00	10.00

Water service	**Min %**	**Max %**
Land	0	0
Buildings/Civil works	1.75	3.50
Wells		
- Buildings/Civil works	1.75	3.50
- General and specific plant	1.25	2.50
- Disinfection plant	2.50	5.00
- Pumps	5.00	10.00
- Building works	1.43	2.86
Abstraction - Buildings/Civil works	1.25	2.50
Lifting and fresh water stations		
- Buildings/Civil works	1.75	3.50
- General plant	7.50	15.00
- Specific plant	6.00	12.00
- Fresh water plant	4.00	8.00
- Disinfection plant	2.50	5.00
- Transformers	2.00	4.00
- Pumps	3.34	6.67
- Reservoirs	1.25	2.5
- Filtration plant and filters	2.78	5.56
- Generators and blowers	2.28	4.55
- Building works	1.43	2.86
Reservoirs	2.00	4.00
- Disinfection plant	2.50	5.00
- Building works	1.11	2.22
Pipelines and distribution network	2.50	5.00
Distribution network in steel, cast iron or spheroidal cast iron	1.00	2.00
Distribution network in reinforced cement-PE-PVC	1.43	2.86
Outlets/Intakes and connections	2.22	5.00
Meters	4.00	10.00
Electricity substations – Specific plant	3.50	7.00
Vehicles	10.00	20.00

Electricity production and distribution service	**Min %**	**Max %**
Land	0	0
Buildings	1.50	3.00
MV underground and overhead distribution network	2.00	4.00
LV underground and overhead distribution network	4.00	8.00
HV/MV - LV/MV transformers	3.50	7.00
- station transformers	2.00	4.00
- pole transformers	2.50	5.00
Connections	3.33	8.00
Meters	4.00	10.00
Tables	1.66	3.33
Limiting devices	1.66	3.33
Masonry and single-pole stations	1.66	3.33
Polyfers	1.25	2.50
Receiver stations	1.66	3.33

Waste Management service	**Min %**	**Max %**
Land	0	0
Buildings	1.50	3.00
Secondary building units (warehouse)	1.50	3.00
General plant	7.50	15.00
Specific IIR plant	5.00	10.00
- land	0	0
- buildings	1.00 - 1.25	2.00 - 2.50
- fixed plant with real estate pertinency	1.66 - 2.00	3.33 - 4.00
- external building works	1.66	3.33
- electricity generation plant	2.00	4.00
- general plant	2.50	5.00
- waste-to-energy post-combustion furnace boiler and fume recovery line	2.50	5.00
- waste-to-energy heater with fluid bed boiler line	3.57	7.14
- steam turbine and electricity generation	2.50	5.00
- waste-to-energy line control systems	5.00	10.00
Specific BIOGAS plant, storage + IRE	5.00	10.00
- land	0	0
- buildings	1.00 - 1.25	2.00 - 2.50
- fixed plant with real estate pertinency	1.66 - 2.00	3.33 - 4.00
- external building works	1.66	3.33
- electricity generation plant	2.50	5.00
- CDR packing	2.50	5.00
- selection, chopping, feeding and sorting plant	2.50 - 3.33	5.00 - 6.67
- ventilation plant	3.33	6.67
- general plant – deactivation plant – storage reservoirs	2.50	5.00
- control systems	5.00	10.00
- containers and bins	5.00 - 10.00	10.00 - 20.00
- internal handling equipment	4.16	8.33
Specific waste composting plant	5.00	10.00

- land	0	0
- buildings	1.00 - 1.25	2.00 - 2.50
- fixed plant with real estate pertinency	1.66 - 2.00	3.33 - 4.00
- external building works	1.66	3.33
- general plant and lifting equipment	3.33	6.67
- pre-selection plant	2.50	5.00
- mixing plant	3.33 - 5.00	6.67-10.0
- palleting plant	5.00	10.00
- energy recovery plant	2.50	5.00
- screening and refining plant	3.33 - 4.16	6.67-8.33
- weighing plant	2.25	5.00
- dioxidization / organic treatment systems	3.33	6.67
- second maturing	5.00	10.00
- cumulus turning and internal handling equipment	4.16	8.33
Vehicles and internal means of transport	10.00	20.00
Waste containers and equipment	5.00	10.00
General equipment	5.00	10.00
Snow service equipment	5.00	10.00
Sanitary equipment	5.00	10.00
Light construction	5.00	10.00
Automobiles	12.50	25.00
Controlled landfills		

Land is not depreciated. The landfills are depreciated on the basis of the percentage filled.

Gains and losses deriving from the sale or disposal of assets are determined as the difference between the sales revenues and the net book value of the assets, and are charged to the income statement.

Leasing – Leasing agreements are classified as financial leases when the terms of the agreement are such that they essentially transfer all the risks and benefits of ownership to the lessee. The assets forming the subject matter of financial leasing agreements are recorded among tangible fixed assets and stated as Group assets at their fair value as of the date of acquisition, or, if lower, at the current value of the minimum payments due for the leasing; they are depreciated on the basis of their estimated useful life on a consistent basis with the assets owned. The corresponding liability vis-a-vis the lessor is recorded in the balance sheet. The payments for lease instalments are divided up into the principal portion and the interest portion and the financial charges are booked directly to the income statement for the year. All the other leases are considered to be operating leases and the related costs for the lease instalments are recorded on the basis of the conditions anticipated in the agreement.

Intangible assets – Intangible assets which are identifiable and whose cost can be reliably determined based on the supposition that said assets will generate future economic benefits, are recorded in the accounts. These assets are stated at cost in accordance with the policies indicated for tangible fixed assets and if they have a defined useful life they are amortised systematically over the period of the estimated useful life. The amortisation commences when the asset is available for utilisation or in any case begins to produce economic benefit for the business. If the intangible fixed assets have an undefined useful life, they are not amortised but subjected to an annual impairment test, even in the absence of indicators which disclose losses in value.

Research and development costs for new products and/or processes are essentially booked to the income statement in the period they are incurred, on a prudent basis.

The advertising expenses are charged directly to the income statement.

Industrial patent rights and know-how are representative of assets which are identifiable and capable of generating future economic benefits under the Company's control; these rights are amortised over the related useful lives.

Concessions and licences mainly comprise rights for the concession under management of local public services and are amortised on a straight-line basis over either the economic-technical life of the assets granted or the duration of the concession involved, whichever period is shorter. The residual value of the intangible fixed assets which corresponds with the water concessions contributed by the merged companies and/or the spun-off business segments, is by contrast amortised in consideration of the average residual management duration in light of the agreements currently in force with the area agencies. The residual value of the intangible fixed assets which corresponds with the concessions for the management of the methane gas distribution networks contributed by the merged companies and/or the spun-off business segments is amortised in consideration of the residual transitory management duration anticipated by current legislation (Letta Decree and Marzano Law).

The gains and losses deriving from the disposal of an intangible fixed asset are determined as the difference between the disposal value and the book value of the assets; they are recorded in the income statement at the time of disposal.

Business combinations - IFRS 3 is applicable to the business combinations which have come about as from March 31, 2004. The Company has applied this policy for the acquisitions of the Agea Group and the Meta Group.

IFRS 3 anticipates that the business combinations be recorded in accordance with the acquisition method. Specifically, the acquisition cost is determined by the sum total of the current values, as of the date of exchange, of the activities given, the liabilities incurred or undertaken and the financial instruments issued by the group in exchange for control over the company acquired, in addition to the costs directly attributable to the combination; the only exception is represented by non-current assets which are classified as "held for sale" in compliance with IFRS 5 and stated and valued at current values less the sales costs.

The goodwill deriving from the acquisition is recorded as an asset and initially valued at cost, represented by the surplus of the acquisition cost with respect to the Group share in the current values of the identifiable assets, liabilities and potential liabilities recorded. If, after the re-determination of these values, the Group share in the current values of the identifiable assets, liabilities and potential liabilities exceeds the acquisition cost, the surplus is recorded immediately in the income statement.

Availing itself of the faculty envisaged by the IRFS, the Group has not retroactively applied IFRS 3 to the business combination transactions which took place before the date of changeover to the IAS/IFRS Standards; these transactions have been recorded at the same values determined on the basis of the previous accounting policies.

Goodwill deriving from consolidation represents the additional value of the acquisition cost with respect to the percentage due to the Group of the assets and liabilities, stated at fair value, of the subsidiary, associated or jointly controlled investee companies as of the acquisition date.

Goodwill deriving from the acquisition of an associated company is included in the book value of the investee company.

Losses in value ("Impairment") – As of each balance sheet date, the Group takes into consideration the book value of the tangible and intangible fixed assets (and in relation to the latter those with an undefined useful life, including goodwill) in order to assess whether there is any indication that said assets have suffered a reduction in value. If there is any indication in this sense, the recoverable amount of said assets is estimated so as to determine the total of the writedown. The recoverable amount is either the net sales price or the usage value, whichever is the greater. Where it is not possible to estimate the recoverable value of an asset individually, the Group estimates the recoverable value of the unit generating the financial flows to which said assets belong. Future cash flows are discounted back to a discount rate (net of taxation) which reflects the current valuation of the market and takes into account the risks associated with the specific business activities.

If the recoverable amount of an asset (or of a unit generating financial flows) is estimated as lower than the related book value, the book value of the assets is reduced to the lower recoverable value and the loss in value is booked to the income statement. When there is no longer any reason for a writedown to be maintained, the book value of the asset (or the unit generating financial flows), with the exception of goodwill, is restated at the new value deriving from the estimate of its recoverable value; however, this new value cannot exceed the net book value which the asset would have had if the writedown had not been made for the loss in value. The writeback of the value is charged to the income statement, unless the asset is valued at revalued value, in which case the value writeback is charged to the revaluation reserve.

Equity investments and securities - The equity investments recorded in this item relate to long-term investments.

- **Investments in associated companies –** An associated company is a company over which the Group is able to exercise significant influence, (but not control, or joint control), by means of participation in the decisions on the financial and operating policies of the investee company. Investments in associated companies are carried at equity, except in the cases where they are classified as "held for sale", or when they are not of a significant value; in such an event they are carried at cost. In accordance with the equity method, the investments are stated in the balance sheet at cost, as adjusted for the changes subsequent to acquisition in the net assets of the associated companies, net of any losses

in value of the individual investments. The additional value of the acquisition cost with respect to the percentage due the Group of the current value of the identifiable assets, liabilities and potential liabilities of the associated company as of the acquisition date is recognized as goodwill. The goodwill is included in the book value of the investment and subject to an impairment test.

- **Other equity investments and securities** – The other equity investments and securities belong to the category anticipated by IAS 39 "financial assets available for sale". They comprise instruments representative of shareholders' equity and are stated at fair value. When the market price or the fair value cannot be determined, they are valued at cost adjusted to reflect permanent losses in value, whose effect is booked to the income statement.
  If the reasons for the writedown cease to exist, the investments carried at cost are revalued within the limits of the writedowns made and the effect is booked to the income statement. The risk deriving from any losses exceeding the book value of the investment is recorded in a specific reserve to the extent that the holder is obliged to fulfil legal or implicit obligations vis-a-vis the investee company or in any event cover its losses.
  Financial assets which the Company intends or is able to maintain until maturity, are stated at cost represented by the fair value of the initial payment made in exchange, increased by the transaction costs. Following initial registration, the financial assets are valued on an amortized cost basis using the effective interest rate method.

Other non-current assets – These are stated at their face value, and possibly adjusted for any losses in value.

Contract work in progress – When the result of a contract can be reliably estimated, contract work in progress is valued on the basis of the contractual payments accrued with reasonable certainty, on a percentage of completion basis *(*so-called cost to cost*)*, so as to allocate the revenues and the economic result of the contract to the pertinent individual accounting periods, in proportion to the stage of completion of the work. The positive or negative difference between the value of the contracts and the advance payments received is recorded respectively among the balance sheet assets or liabilities. Contract revenues, in addition to the contractual payments, include the variations, the price review and the recognition of the incentives up to the extent it is probable that they represent effective revenues which can be determined reliably.

When the result of a contract cannot be reliably estimated, the revenues referable to the related contract are recorded solely within the limits of the contract costs incurred which will probably be recovered. The contract costs are recorded as expenses during the accounting period in which they are incurred.

When it is probable that the total contract costs will be greater than the contractual revenues, the expected loss is immediately stated at cost.

Inventories – Inventories are recorded at purchase cost, including directly chargeable related costs, or net estimated realizable value, whichever is the lower. Cost is determined on the basis of

mobile average cost. The net realizable value is calculated on the basis of the current costs of the inventories at year end, less the estimated costs necessary for achieving the sale.

The value of obsolete and slow-moving stock is written down in relation to the possible use or realization, by means of the provision of a specific materials obsolescence allowance.

Inventories of work in progress and finished products are valued at weighted average manufacturing cost for the period, which comprises the raw materials, the consumables and the direct and indirect production costs excluding general expenses.

Trade receivables – Trade receivables are recorded at face value, reduced by an appropriate writedown in order to reflect the estimate of the losses on receivables.

Financial assets – Financial assets are recorded and reversed from the financial statements on the basis of the date of transaction and are initially valued at cost, inclusive of the charges directly associated with the acquisition. As of subsequent balance sheet dates, the financial assets which the Group intends and is able to hold until maturity are recorded at cost, amortized/depreciated on the basis of the effective interest rate method, net of the writedowns made in order to reflect any losses in value. Financial assets other than those held until maturity, are classified as held for trading purposes or available for sale and are valued at fair value at each period end.

Cash and cash equivalents – The item relating to liquid funds and cash equivalents includes cash and bank current accounts and deposits repayable on demand and other short-term financial investments with high liquidity which are readily convertible into cash and are subject to an insignificant risk regarding their change in value.

Loans – Financial liabilities, with the exception of derivatives, are initially stated at cost, corresponding to the fair value of the liability net of the transaction costs which are directly attributable to the issue of said liability. Following the initial statement, financial liabilities are valued on the basis of amortized cost, using the original effective interest rate method.

Employee leaving indemnity and other employee benefits – The liabilities relating to the defined-benefits plans (such as employee leaving indemnities - TFR) are calculated net of any assets serving the plan on the basis of actuarial suppositions and on an accruals basis in line with the employment services necessary for obtaining the benefits; the valuation of the liability is checked by independent actuaries. The gains and losses deriving from carrying out the actuarial calculation are charged to the income statement as a cost or revenue when the net cumulative value of the "actuarial" gains and losses not recorded for each plan at the end of the previous accounting period exceed 10% of the highest value among the obligations referring to defined-benefit plans (so-called corridor method).

Provisions for risks and charges – The provisions for risks and charges comprise the amounts set aside as recorded in the financial statements on the basis of current obligations (as emerging from past events) which the Group believes it probably will have to meet. The provisions are set aside on the basis of the best estimate of the costs required to meet the fulfilment, as of the

balance sheet date, and are discounted back when the effect is significant and the necessary information is available. In such an event, the provisions are determined by discounting back the future cash flows at a pre-taxation discount rate which reflects the current market valuation and takes into account the risk associated with the business activities. When the discounting back is carried out, the increase in the provision due to the passing of time is recorded as a financial charge. If the liability is associated with an intangible asset (such as the recovery of sites), the provision is recorded as a matching entry to the asset to which it refers and the recording of the charge in the income statement takes place by means of the depreciation process of the tangible fixed asset to which the charge refers.

Trade payables – These concern commercial supply transactions.

Other current liabilities – These concern sundry transactions and are stated at face value.

Derivative financial instruments – The Group holds derivative instruments for the purpose of hedging its exposure to the risk of interest rate fluctuations and the risk of changes in methane gas and electricity prices. In relation to said activities, the Group must handle the risks associated with the misalignment between the index-linking formulas relating to the purchase of gas and electricity and the index-linking formulas linked to the sale of said commodities. The instruments used for the handling the price risk, both with regards to the price of the goods and the related Euro/Dollar exchange rate, are substantiated in commodity-swap agreements, finalized at pre-establishing the effects on the sales margins irrespective of the changes in the afore-mentioned market conditions.

On a consistent basis with the chosen strategy, the Group does not enter into derivative transactions for speculative purposes.

The transactions which, in observance of the risk management policies, satisfy the requisites laid down by the accounting standards for hedge accounting treatment are classified as “hedging”, while those which, despite being entered into for hedging purposes, do not satisfy the requisites required by the standards, are classified as “trading”.

For registration purposes, the hedging transactions are classified as *“*fair value hedges*”* if they cover the risk of fluctuation in the market value of the underlying asset or liability; or as *“*cash flow hedges*”* if they cover the risk of changes in financial flows deriving both from an existing asset or liability, or from a future transaction.

As far as derivative instruments classified as *“*fair value hedges” are concerned, which observe the conditions for the accounting treatment as hedging transactions, the gains and losses deriving from the determination of their market value are booked to the income statement. The gains and losses deriving from the adjustment to fair value of the element underlying the hedge, are also booked to the income statement.

In relation to the instruments classified as “cash flow hedges” which observe the conditions for the accounting treatment as hedging transactions, the gains and losses deriving from the determination of their market value are booked to shareholders’ equity.

The changes in the fair value of the derivative instruments which are not classified as hedging, are recorded in the income statements for the period in which they occur.

Grants – Capital grants are stated in the income statement over the period necessary for correlating them to the related costs; they are represented in the balance sheet by recording the grant as deferred revenue. Operating grants, including those received from users for connection purposes, are considered to be revenues for services carried out during the accounting period and are therefore recorded on an accruals basis.

Revenue recognition - Revenues and income are stated net of returned items, discounts and rebates, and net of direct taxes related to the sales of products and services rendered. They are broken down into revenues deriving from operating activities and financial income which accrues between the sale date and the payment date.

In particular:

- the revenues from energy, gas and water sales are recognised and recorded at the moment of the provision of the service and include the services provided, but not yet invoiced (estimated on the basis of historical analyses determined according to previous consumption levels),
- revenues from services rendered are recognised on the basis of services provided and in compliance with the relevant contracts,
- revenues from the sale of goods are recognised at the time the Group transfers the significant risks and benefits associated with ownership of the assets to the purchaser,
- costs are stated in accordance with the accruals principle.

Financial income and charges – Financial income and charges are recognised in accordance with the accruals principle.

Income taxes – Income taxes are calculated on the basis of the best possible estimate, in relation to the information available, of the forecast trend for the period (up to the end of the tax period); account was also taken of the effects deriving from the activation within the sphere of the Group of the national tax consolidation system. Deferred and prepaid taxes are calculated on the tax timing differences and on the differences which are generated by the application of the international accounting standards.

Translation of foreign currency balances – The functional and reporting currency adopted by the HERA Group is the Euro. Foreign currency transactions are initially recorded using the exchange rate in force as of the transaction date. Foreign currency assets and liabilities, with the exception of fixed assets, are recorded using the exchange rate ruling as of the year end date and the related exchange gains and losses are duly charged to the income statement; any net gain which might arise, is set aside in a specific restricted reserve until the date of realization.

Earnings per share – The earnings per share are represented by the net profit for the period attributable to the shareholders holding ordinary shares, taking into account the weighted average of the ordinary shares in circulation during the year. The diluted earnings per share are obtained by means of the adjustment of the weighted average of the shares in circulation, taking into account all the potential ordinary shares with dilution effect.

4. Revenues

The revenues for the year 2005 amounted to Euro 1,767,959 thousand. The breakdown is presented below.

	2005 €/000s	2004 €/000s (adjusted)	Change €/000s
Revenues from sales and services	1,730,723	1,492,572	238,151
Change in inventories of work in progress, semi-finished and finished products	-3,034	3,538	-6,572
Change in contract work in progress	5,499	5,649	-150
Other revenues and income	34,771	27,106	7,665
Total	**1,767,959**	**1,528,865**	**239,094**

The analysis of the sales performance by business sector is presented in the report on operations. The Group mainly operates in Italy.

5. Other operating income

Other operating income amounts to Euro 34,771 thousand and comprises the following

	2005 €/000s	2004 €/000s (adjusted)	Change €/000s
Insurance reimbursements	4,245	2,307	1,938
Sale of materials and stock to third parties	214	34	180
Portion of capital grants	2,518	1,408	1,110
Portion of operating grants and from separated waste collection	6,698	7,786	-1,088
Rents	804	1,147	-343
Use of provisions	4,095	1,116	2,979
Ordinary capital gains	3,274	2,586	688
Costs reimbursed	991	1,770	-779
Other	11,932	8,952	2,980
Total	**34,771**	**27,106**	**7,665**

The item “Insurance reimbursements” disclosed an increase with respect to the previous year due mainly to the enforcement of a guarantee policy by the subsidiary company Frullo Energia Ambiente SrL for Euro 2,500 thousand.

The item “Use of provisions” disclosed an increase of Euro 2,979 thousand when compared with the previous period, including Euro 1,897 thousand due to the greater use of the landfill post-closure provisions and Euro 977 thousand for the re-assessments of provisions of the Parent Company, Hera S.p.A..

6. Costs for raw materials and consumables (net of the change in inventories for raw materials and stock)

The item is analysed as follows.

	2005 €/000s	2004 €/000s (adjusted)	Change €/000s
Methane ready for sale and LPG net of inventory changes	521,618	367,785	153,833
Fuel for heat generation	2,761	1,530	1,231
Electricity ready for sale	171,377	137,973	33,404
Water	23,676	23,416	260
Maintenance materials: handling and spare parts net of change in stock	37,057	21,303	15,754
Electricity	20,217	25,938	-5,721
Fuels and lubricants	10,607	5,846	4,761
Methane for industrial use	3,424	4,191	-767
Water for industrial use	1,169	399	770
Chemical products	8,587	7,464	1,123
Consumables and sundry materials	7,631	23,863	-16,232
Landfill costs	529	2,298	-1,769
Income and charges from derivatives	918	0	918
Total	**809,571**	**622,006**	**187,565**

The analysis of the trend in costs for raw materials and consumables is presented in the report on operations.

In detail, the item “Consumables and sundry materials” relating to 2004 includes the balance of Euro 10,988 thousand relating to lease-back transactions carried out by the subsidiary Uniflotte S.r.L.; no such transactions were carried out in 2005.

The item “Landfill costs” derives from the application of IFRIC 1 to the changes in the estimates of the expected costs relating to post-closure charges.

The item “Income and charges from derivative contracts” amounting to Euro 918 thousand refers to derivative contracts, classified as hedging arrangements in accordance with international accounting standard 39, which are stipulated to covers risks on commodities.

7. Costs for services

The breakdown is as follows.

	2005 €/000s	2004 €/000s (adjusted)	Change €/000s
Industrial utilities: for water, methane, heat and energy services	2,408	5,788	-3,380
Charges for work and maintenance	160,921	146,601	14,320
Energy transport and storage	64,945	59,715	5,230
Insurance costs	10,157	9,009	1,148
IT and CED services	18,497	5,599	12,898
Cleaning and security costs	3,749	4,301	-552
Waste transportation, disposal and collection services	90,220	81,932	8,288
Announcements, advertising and disputes	5,620	6,213	-593
Transport costs	637	1,024	-387
Technical, organization, legal and tax assistance consultancy	23,314	23,203	111
Remuneration of Directors and Statutory Auditors	4,136	4,115	21
Meter reading	3,634	1,637	1,997
Postal and telephone costs	3,528	4,645	-1,117
Recruitment, training and other staff costs	8,623	7,153	1,470
Other	39,746	55,995	-16,249
Total	**440,135**	**416,930**	**23,205**

The changes in the main operating costs with respect to the previous year have been illustrated in the report on operations.

8. Personnel costs

The breakdown of personnel costs in the two accounting periods is as follows.

	2005 €/000s	2004 €/000s (adjusted)	Change €/000s
Wages and salaries	159,108	152,822	6,286
Social security contributions	55,706	53,363	2,343
Employee leaving indemnity provision	7,803	6,449	1,354
Other costs	5,022	3,202	1,821
Total	**227,639**	**215,863**	**11,804**

The average number of employees in the periods in question, analysed by category, is as follows:

	2005	2004	Change
Executives	89	84	5
Managers	207	186	21
White-collar	2,228	1,996	232
Blue-collar	2,688	2,834	-146
Total	**5,212**	**5,100**	**112**

Overall the average pro-capita cost as at December 31, 2005 came to Euro 44 thousand, up by 4.7 % when compared with December 31, 2004 (Euro 42 thousand).

As at December 31, 2005, employees numbered 5,904, taking into account the inclusion of employees from the absorbed companies following the transaction for the merger of Meta S.p.A. into Hera S.p.A.

9. Other operating costs

The breakdown of other operating costs is as follows.

	2005 €/000	2004 €/000s (adjusted)	Change €/000s
Fees paid to local authorities	58,631	46,022	12,609
Rents and leases payable	16,648	19,980	-3,332
Taxation other than income taxes	3,254	4,518	-1264
Fees payable	4,360	1,308	3,052
Membership fees	1,432	1,338	94
Special landfill levy	12,038	9,951	2,087
Losses on the sale of assets	702	1,034	-332
Losses on receivables not covered by the allowance	1,977	256	1,721
Other minor charges	8,996	7,745	1,251
Total	**108,038**	**92,152**	**15,886**

9.bis Capitalized costs

This item is analysed as follows.

	2005 €/000s	2004 €/000s (adjusted)	Change €/000s
Increases for internally-constructed fixed assets	138,463	110,599	27,864
Total	**138,463**	**110,599**	**27,864**

This item is mainly represented by the investments made by the area operating companies for the Parent Company Hera S.p.A. An analysis of the investments is contained in the notes commenting on the balance sheet assets regarding the analysis of tangible and intangible fixed assets.

10. Value writeback on tangible fixed assets

This item amounts to Euro 15,518 thousand and concerns the value writeback of the tangible fixed assets pertaining to the telecommunications sector. This writeback became necessary following an accurate assessment of the forecast cash flows in light of the synergies generated by the integration of the Modena company, by the prospects of extending a number of strategic contracts and by a review of the discounting back rate taking into account the intrinsic risk relating to transactions outstanding with associated companies and public authorities.

11. Portion of profit (loss) pertaining to associated companies

The valuation of the investments in associated companies using the equity method generated the following balances.

	2005 €/000s	2004 €/000s (adjusted)	Change €/000s
Income pertaining to associated companies	1,850	1,267	583
Losses pertaining to associated companies	-2,294	-4,296	2,002
Total	**-444**	**-3,029**	**2,585**

The valuation was carried out by acknowledging on a pro-quota basis the losses and income for the year reported by the respective companies.

12. Financial income and charges

Financial income is analysed in the following table:

	2005 €/000s	2004 €/000s (adjusted)	Change €/000s
Bank interest income	1,746	1,677	69
Interest income on other short-term receivables	99	310	-211
Interest charged to customers	724	600	124
Financial income generated by derivatives on commodities	25,690	0	25,690
Financial income generated by derivatives on rates	3,319	0	3,319
Other financial income	2,781	3,484	-703
Total	**34,359**	**6,071**	**28,288**

The change when compared with 2004 in financial income generated by derivatives on commodities and rates, is attributable to the fact that the application of IAS 39, as permitted, took place as from January 1, 2005.

A breakdown of interest and other financial charges is presented below:

	2005 €/000s	2004 €/000s (adjusted)	Change €/000s
Interest expense on bank current account overdrafts	10,089	5,661	4,428
Interest expense charged by banks for medium/long-term loans	18,974	14,533	4,441
Financial charges generated by derivatives on commodities	24,423	0	24,423
Financial charges generated by derivatives on rates	4,768	0	4,768
Financial charges as a result of IAS 19	1,886	1,733	153
Financial charges generated by the application of "other international accounting standards"	9,128	5,593	3,535
Other	4,834	5,235	-401
Total	**74,102**	**32,755**	**41,347**

In relation to the changes with respect to 2004 in financial charges generated by derivatives on commodities and rates, reference should be made to the above matters stated for income.

The item "financial charges generated by the application of "other international accounting standards"" increased with respect to the previous year by Euro 3,535 thousand; this increase is made up as follows:

- Euro 1,535 thousand relating to the application of IAS 37 and IFRIC 1. Chiefly, the variation is due to the change in the timing of the estimates of the future cash flows for post-closure charges to be incurred.
- Euro 753 thousand relating to the application of IAS 37 on provisions for the recovery of third party assets.

- Euro 1,247 thousand relating to the application of IAS 17; this change is mainly due to the stipulation of new leasing agreements when compared with the previous period within certain Group companies.

13. Income taxes

This item is made up as follows

	2005 €/000s	2004 €/000s (adjusted)	Change €/000s
Current, deferred and prepaid taxes	66,055	61,083	4,972
	66,055	**61,083**	**4,972**

The total percentage of income taxes for the period on the pre-tax result came to 42.97%.

Shareholders are hereby informed that in accordance with and for the purposes of Article 27 of Italian Law No. 62 dated April 18, 2005, which established the procedure for the recovery of government aid declared illegitimate by the Ruling of the European Commission No. 2003/193 dated June 5, 2002, Hera S.p.A has presented tax declarations relating to the tax periods affected by the exemption regime. The Inland Revenue office responsible for the area has completed the assessment activities at the Company relating to the afore-mentioned declarations, issuing a verification proceedings report as at October 17, 2005; the Company therefore presented briefs on 1 December 2005. Furthermore, section 132 of the Finance Bill, Italian Law No 266 dated 23 December 2005 introduced significant amendments to Article 27 of Italian Law No. 62 dated April 18, 2005, foreseeing, among other things, the extension of the timescale for the recovery of the aid and a change of responsibility from the Exchequer to the Home Office.

Shareholders are also informed that, in accordance with the matters established by the agreements between the shareholders at the time of the corporate merger which led to the formation of HERA, as contained in the Stockmarket listing Information Prospectus, “the Local Authorities pledged to compensate HERA for any costs, losses or damages suffered by the same in relation to compulsory legislative rulings which revoke the tax concessions which the Company and the companies taking part in the merger have availed of”. Consequently, HERA SpA did not provide for any additional provision against charges in the accounts.

In relation to the former Meta SpA, please note that the tax periods affected by the moratorium have been subject to automatic definition (“tax amnesty”) as per Article 9 of Italian Law No. 289/2002 and therefore all assessment activities in relation to the same are precluded in accordance with the matters laid down by Article 9.9 of the afore-mentioned Italian Law No. 289/2002. The financial statements do not contain any provision for this purpose since the Directors believe that the risk of having to repay the taxes following a negative final outcome of the entire infraction procedure is possible but not probable. Prudently, it was considered expedient to restrict a portion of the Unrestricted Reserves, amounting to Euro 4,100 thousand, for the possible liability generated by the merger with Meta SpA , on a consistent basis with the resolution adopted

on January 15, 2003 by said company; this amount would cover any charges consequent to the recovery of the government aid declared illegitimate by the European Commission.

14. Tangible assets

Tangible fixed assets are stated net of the related accumulated depreciation and present the following breakdown and changes during the year:

Statement of changes in tangible fixed assets

(Euro thousands)	Land and buildings	Plant and machinery	Other fixed assets	Construction in progress	Total tangible fixed assets
PURCHASE COST					
Balance as at December 31, 2004	**223,950**	**1,086,902**	**204,969**	**250,684**	**1,766,505**
	-	-	-	-	
Increases	6,259	522,890	12,081	47,902	589,133
Disposals	- 12,063	- 2,669	- 18,876	- 2,176	- 35,784
Changes in consolidation area	58,163	471,192	41,164	25,870	596,388
Other changes	16,224	- 219,487	9,109	- 116,087	- 310,240
Balance as at December 31, 2005	**292,534**	**1,858,828**	**248,447**	**206,193**	**2,606,002**
ACCUMULATED DEPRECIATION					
Balance as at December 31, 2004	**32,030**	**324,425**	**111,183**	**0**	**467,638**
Depreciation for the year	6,951	65,867	17,213	0	90,031
Disposals	- 2,690	- 534	- 14,655	0	- 17,880
Changes in consolidation area	8,666	133,226	21,032	0	162,924
Other changes	- 1,335	- 11,529	1,206	0	- 11,658
	0	0	0	0	-
Balance as at December 31, 2005	**43,622**	**511,454**	**135,979**	**0**	**691,055**
Net value					
As at December 31, 2004	**191,920**	**762,477**	**93,786**	**250,684**	**1,298,867**
As at December 31, 2005	**248,911**	**1,347,374**	**112,468**	**206,193**	**1,914,946**

For an analysis of the investments for the period, reference should be made to the matters specified in the Report on operations under section 3.01.02.01 of this financial statement dossier.

15. Intangible assets

Intangible assets comprise:

Statement of changes in intangible fixed assets

Euro thousands	Patent rights and know-how	Concessions, licences, trademarks and similar rights	Other intangible assets	Assets in process of formation and advance payments	Total intangible fixed assets
PURCHASE COST					
Balance as at December 31, 2004	20,962	245,085	23,595	39,254	328,896
Increases	29,590	3,886	4,549	12,651	50,677
Disposals	- 12	- 1,530	- 638	- 302	- 2,483
Changes in consolidation area	5,369	89	91	2,709	8,258
Other changes	23,235	- 5,309	- 8,867	- 38,978	- 29,919
Balance as at December 31, 2005	**79,144**	**242,221**	**18,730**	**15,334**	**355,429**
ACCUMULATED AMORTISATION					
Balance as at December 31, 2004	10,189	97,960	9,800	-	117,949
Amortisation for the year	14,694	12,402	2,340	-	29,436
Disposals	- 10	- 3,165	- 348	-	- 3,522
Changes in consolidation area	3,839	19	- 911	-	2,947
Other changes	- 9	- 1,399	- 2,820	-	- 4,227
Balance as at December 31, 2005	**28,704**	**105,817**	**8,061**	**-**	**142,582**
Net value					
As at December 31, 2005	50,440	136,404	10,669	15,334	212,847
As at December 31, 2004	10,773	147,125	13,795	39,254	210,947

The item “Patent rights and know-how”, amounting to Euro 50,440 thousand as at December 31, 2005, mainly concerns the costs incurred for the acquisition and implementation of the SAP R/3 and SAP/ISU computerized information system amounting to Euro 47,086 thousand. Such costs are amortised over a period of five years.

Concessions, licences, trademarks and similar rights, totalling Euro 136,404 thousand as at December 31, 2005 (down by Euro 10,721 thousand when compared with the previous year) mainly comprise the value of the concessions belonging to the Parent Company relating to the gas, water and purification plants. The decrease is due to the changeover from concession to ownership for the assets relating to the energy and purification services in the municipalities of

Loiano, Marzabotto, Castelmaggiore, Savigno and San Benedetto Val di Sembro, as envisaged by the related contracts on reaching the expiry dates of said concessions.

Assets in process of formation, amounting to Euro 15,334 thousand as at December 31, 2005 essentially represent the costs incurred for IT projects not yet completed.
The significant decrease with respect to the previous year mainly concerns the coming onto stream of the SAP/ISU invoicing project and the “Template” project for the IT launch of the Territorial Operating Companies of the Hera S.p.A. Group.

16. Goodwill

The item "Goodwill and consolidation differences" as at December 31, 2005, totalling Euro 273,432 thousand, is analysed as follows.

- residual goodwill from the merger transaction which in 2002 gave rise to Hera S.p.A., Euro 86,516 thousand;
- goodwill relating to the absorption of Agea S.p.A. which took place in 2004, Euro 41,658 thousand. This goodwill represents the additional value of the purchase cost with respect to the Group portion in the current values of the assets and liabilities recorded. Specifically, as far as the current value is concerned of Hera S.p.A. shares issued following the share capital increase serving the merger by incorporation of Agea, the value of the shares was determined, in observance of the matters anticipated by IFRS 3, as of the date effective control over Agea S.p.A. was gained;
- goodwill relating to the subsidiary company Ecologia Ambiente arising in 2004 following the conferral of the business segment by Ambiente S.p.A. totalling Euro 11,053 thousand;
- goodwill relating to the META S.p.A. merger transaction, Euro 118,064 thousand. This goodwill, recorded as an asset and initially valued at cost, represents the additional value of the purchase cost with respect to the Group portion in the current values of the assets and liabilities recorded. In detail, as far as the current value is concerned of Hera S.p.A. shares issued following the share capital increase serving the merger by incorporation of META S.p.A., the value of the shares was determined as of the 2005 year end date, essentially identified as the date effective control over META S.p.A. was gained;
- the consolidation difference deriving from the consolidation of the subsidiary Medea, Euro 3,069 thousand; of the subsidiary Nuova Geovis, Euro 1,775 thousand; of the subsidiary Ares, Euro 208 thousand; of the subsidiary Hera Gas Tre, Euro 588 thousand; of the subsidiary ASA for Euro 2,788 thousand; and of the subsidiary TS Energia, for 277 thousand;
- the consolidation difference deriving from the increase in the equity investment in the subsidiary company Uniflotte for Euro 660 thousand.

As envisaged by IFRS 3, as from 2004 goodwill is no longer subject to amortisation and an impairment test is carried out on the residual value at period end.

17. Equity investments and securities

	31/12/2005 €/000s	31/12/2004 €/000s (adjusted)	Change €/000s
Equity investments in non-consolidated subsidiary companies:			
Ambiente 3000 S.r.l.	0	35	-35
Argilegas S.r.L.	19	0	19
Calorpiù Italia Scarl	5	0	5
Calorpiù Modena Scarl	6	0	6
Consorzio Energia Servizi	3	3	0
Geat Service in liquidazione	0	327	-327
Hera Clion	200	0	200
Hera Ferrara S.r.l.	0	10	-10
Hera Immobiliare S.r.l.	100	68	32
Hera Modena S.r.L.	10	0	10
Hera Servizi Funerari S.r.L.	10	0	10
Immobiliare Berti Pichat S.r.l.	0	5	-5
Inter.imm S.r.l.	0	37	-37
Rio d'Orzo	202	0	202
Sbi S.r.L.	51	116	-65
Total	**606**	**601**	**5**
Equity investments in associated companies:			
Acantho S.p.a.	6,288	5,736	552
Agea Reti S.r.l.	7,739	7,739	0
Amav Ambiente S.p.A	0	218	-218
Ambiente 3000 S.r.L.	54	0	54
Asa S.p.A.	0	672	-672
Aspes Multiservizi S.p.A	13,995	13,084	911
Attivabologna	1,803	0	1,803
Delta Web	0	94	-94
Dyna Green S.r.L.	193	0	193
Ferrara Tua	0	164	-164
GAS GAS	105	0	105
Locride Ambiente S.p.A	0	393	-393
Meta Rete GAS in liquidazione	204	0	204
Modena Network	417	0	417
Penisola Verde S.p.A	0	79	-79
Refri	1,706	0	1,706
SET S.p.A	23,028	23,250	-222
SGR Servizi S.p.A	5,144	0	5,144
Tecnometano S.r.L.	591	0	591
Tre-A-Web	0	381	-381
Viviservizi S.r.l.	0	178	-178

Yele S.p.A	177	185	-8
Other investments	583	647	-64
Total	**62,027**	**52,820**	**9,207**
Equity investments in other companies:			
Energia Italiana S.p.A.	24,695	23,980	715
Galsi	639	450	189
Ambiente Mare	300	300	0
Calenia	2,835	15	2,820
Other companies	707	217	490
Total	**29,176**	**24,962**	**4,214**
Total equity investments	**91,809**	**78,383**	**13,426**
Securities			
Fixed-income securities	22	1	21
Variable-income securities	0	1	-1
Total securities	**22**	**2**	**20**
TOTAL EQUITY INVESTMENTS AND SECURITIES	**91,831**	**78,385**	**13,446**

Equity investments in non-consolidated subsidiary companies

On November 24, 2005, the Modena-based territorial operating company known as Hera Modena S.r.l. was formed, following the merger by incorporation of Meta spa within Hera spa. As at December 31, 2005, the company was dormant.

On December 31, 2005, investments were acquired in Calorpiù Modena scarl and Calorpiù Italia scarl belonging to Meta S.p.a., following the merger by incorporation of Meta spa within Hera spa.

As from January 1, 2005, the company Hera Ferrara S.r.L. became operative, and as of this date will be consolidated on a line-by-line basis.

The company Hera Clion S.r.L., an investee company of Hera S.p.A., was placed in liquidation as from October 3, 2005.

INTER-IMM S.r.L., in liquidation, was wound up on December 27, 2005.

Geat Service, in liquidation, was wound up on December 21, 2005.

The company Immobiliare Berti Pichat S.r.L. was placed in liquidation on June 6, 2005; it was subsequently wound up in September.

On April 12, 2005, Hera S.p.A. subscribed a share capital increase amounting to Euro 25,500 relating to the equity investment in Ambiente 3000. This company, carried at cost in 2004, was carried at equity in 2005. It is currently dormant.

On July 6, 2005, the subsidiary company Hera Comm acquired the entire equity investment in the share capital of Argilegas S.r.L. from Gastecnica Galliera. On October 14, 2005, the transfer of the whole of Argilegas S.r.L. to Hera Comm took place, with effects as from October 1, 2005. On November 3, 2005, the company was placed in liquidation.

Hera S.p.A. held an investment of 21% in the share capital of the company Rio d'Orzo. As at November 30, 2005, the Group acquired an additional holding of 25.5% in the company from the municipal authority of Castello di Serravalle, taking the Group's total investment to 46.5%. Following the merger of Meta S.p.A. within Hera S.p.A, the Group acquired an additional 46.5%, therefore takings its shareholding to 93%. The company is dormant.

On December 22, 2005, Hera spa formed Hera servizi Funerari S.r.L., a company with just one staff member and share capital of Euro 10,000. The company manages on its own account, or on behalf of third parties, the activities concerning funeral services and any related activities. The company was dormant as at December 31, 2005.

Equity investments in associated companies

On December 27, 2005, following the additional acquisition of 8% of the share capital from Unieco soc. coop a r.l. and 23% from the Municipality of Castelmaggiore, the investment in Asa spa rose to 51%. The acquisitions led to the effective control over the company and the consequent line-by-line consolidation.

On September 22, 2005, the equity investment in the company AMAV Ambiente was sold to the municipal authority of Sant' Anastasia.

On August 22, 2005, the equity investment in Locride Ambiente S.p.A was sold to the company Ecologia Oggi S.r.L..

The equity investments in Ferrara Tua and PenisolaVerde have been reclassified among "other financial assets" since, during January and February 2006, two sales contracts were stipulated with third parties.

On September 30, 2005, Hera spa sold the 30% equity investment in Delta WEB to Acosea Impianti. The residual investment of 5.56% was reclassified under other companies.

The shares held by Hera S.p.A. in Tre A-Web S.p.A. were transferred to Acnatho S.p.A. on April 15, 2005. On December 31, 2005, Tre A-Web S.p.A. was merged by incorporation within Acantho S.p.A.

On October 12, 2005, Hera S.p.A. acquired an additional equity investment from private shareholders in VIVISERVIZI S.r.L., thereby increasing its holding from 48% to 80.76%. Following this transaction, the consolidation method changed from equity to line-by-line.

On June 7, 2005, the subsidiary company Hera Comm acquired a further holding in the company Attivabologna S.r.L. The ownership percentage therefore rose from 91.74% to 96.40%. On September 22, 2005. Attivabogna took steps to sell off the business segment pertaining to the meter service to Hera Energie Bologna, with effect as of October 1, 2005.
On July 19, 2005, Attivabologna S.r.L. was placed in liquidation. As at December 31, 2005, this company was carried at equity.

On November 22, 2005, the subsidiary Hera Trading subscribed the share capital increase of Dyna Green S.r.L. with effect as of October 1, 2005, acquiring an equity investment of 33.33%. This company operates in the field of research & development on behalf of the shareholders for the opportunity of acquiring and importing natural gas from Libya.

On July 14, 2005, the subsidiary company Hera Comm acquired the entire equity investment in the share capital of GASGAS S.r.L., a company involved with the sale of natural gas. On October 14, 2005, the entire company was sold off to Hera Comm, with effect as of October 1, 2005, and on October 3, 2005, the company was placed in liquidation.

On May 17, 2005, a 20% investment in the company SGR Servizi S.p.A was acquired for a total value of Euro 4,162 thousand. The company is involved in natural gas sales activities, as well as meter reading and invoicing activities.

Following the process for the merger of Meta S.p.A. within Hera S.p.A., equity investments were acquired in Meta Rete Gas, a company in liquidation, and Modena Network.

On December 27, 2005, Hera Spa acquired from Unieco the 20% investment in Refri S.r.L, a company which operates in the field of design, construction, and management of plants and structures for the disposal, purification, treatment and recycling of all types of waste.

Following the process for the merger of Meta S.p.A. within Hera S.p.A., the equity investment in Acantho increased by 3.42%; the overall value of the investment therefore equates to 50.58%. The company has however been carried at equity since, during February 2006, the shareholder Infacom showed its interest in acquiring a holding of 3.124% in Acantho. As of the date the financial statements were drawn up, procedures have been underway for the effective transfer of the holding by Hera spa.

On July 14, 2005, Hera acquired 100% of Tecnometano S.r.L's share capital, a company which operates in the sector involved in the installation and management of plants for the transport and

distribution of liquid fuels and methane gas. On September 30, 2005, the transfer of the entire company to Hera S.p.A. took place, with effect as of October 1, 2005; subsequently, as at November 8, 2005 the company was placed in liquidation. As at December 31, 2005, the company was carried at equity.

Equity investments in other companies

As at June 30, 2005, the Parent Company subscribed its portion of the share capital increase in the investee company Energia Italiana S.p.A., for a value of Euro 715 thousand.

During 2005, the Parent Company made various payments towards future share capital increases of the investee company Calenia Energia S.p.A. for a total value of Euro 2,820 thousand.

The subsidiary company Hera Trading subscribed and paid in a share capital increase in the company Galsi for Euro 189,000 on July 26, 2005.

18 Non-current financial assets

As at December 31, 2005, this item which amounts to Euro 54,441 thousand (Euro 18,903 thousand as at December 31, 2004) essentially comprised:

- amounts receivable for loans to associated companies : Oikothen, Euro 1,343 thousand, 4 Italy, Euro 277 thousand and SET, Euro 18,447 thousand;
- guarantee deposits for Euro 33,325 thousand (of which Euro 12,000 thousand corresponding to the value of the guarantee deposit on the business segment rental agreement between the company which owns the networks Acosea Reti S.r.L. and Hera S.p.A., and for Euro 21,325 thousand corresponding to the value of the deposits afforded in favour of the Provincial authorities of Forlì, Cesena and Ravenna guaranteeing the post-closure management of the landfills),
- amounts receivable for mortgage loans to be received for Euro 925 thousand.

The increase with respect to 2004 includes Euro 21,325 thousand for the affording of the guarantee deposits mentioned above, Euro 849 thousand for increases in loans granted by the Parent Company to the companies 4Italy spa (Euro 277 thousand) and Set (Euro 572 thousand) and by Ares to Oikothen (Euro 1,343 thousand) and for Euro 12,000 thousand in relation to the guarantee deposit paid over by Acosea Reti S.r.L. which as at December 31, 2004 had been classified under the item “other non-current assets”.

18. Deferred tax assets

As at December 31, 2005, this item amounted to Euro 41,474 thousand (Euro 35,079 thousand as at December 31, 2004). Amounts receivable for advance taxes are generated by the timing differences between the net profit recorded in the financial statements and the taxable income and by the differences arising further to the application of the IAS/IFRS. The latter mainly concern the application of IAS 38 (Euro 5,742 thousand), IAS 19 (Euro 1,120 thousand) as well as Euro 6,123

thousand following the application of IAS 39 in relation to the Group's financial derivative instruments.
Amounts receivable for prepaid taxes pertaining to the Group companies mainly refer to the writedowns of fixed assets, provisions to the allowance for doubtful receivables and provisions to non-deductible risk reserves.

20. Financial instruments - Derivatives

The derivative financial instruments classified under non-current assets as at December 31, 2005, amounted to Euro 3,413 thousand and include Euro 1,187 thousand for derivatives on rates and Euro 2,226 thousand for derivatives on commodities.

The derivative financial instruments classified under non-current liabilities amounted to Euro 19,225 thousand and included Euro 13,646 thousand for derivatives on rates and Euro 5,579 thousand for derivatives on commodities.

In its entirety, the Hera Group is exposed to risk pertaining to interest rates, energy product prices and the related exchange rate; the exposure to liquidity risk is more or less inexistent.

In particular, as far as rate risks are concerned, the Hera Group is exposed to the risk that a possible rise in the interest rates may generate greater future financial charges against the sources of medium/long-term lending at floating rates. Therefore, with the aim of mitigating this risk, over the last few accounting periods the Group has stipulated a number of derivative instruments on rates against part of its current and future financial liabilities and, more specifically:

- 6 Interest Rate Swap agreements for a notional amount as of the year end date totalling Euro 209.6 million against variable rate mortgage loans for the same amount. The value of these agreements was negative for a total of Euro 3.4 million (Euro 4.8 million as at December 31, 2004);
- 3 Interest Rate Cap options acquired for a notional amount as of the year end date totalling Euro 154.2 million against variable rate mortgage loans for the same amount. The value of these agreements was negative for a total of Euro 0.5 million (Euro 0.2 million as at December 31, 2004);
- 9 Interest Rate Swap agreements against the future fixed rate bond to be issued, effectively issued on February 15, 2006, for a total nominal amount of Euro 500 million, equating to the entire nominal value of the bond. The value of these agreements was negative for a total of Euro 6.5 million. In relation to these agreements, shareholders are informed that as of February 2, 2006 steps were taken to redeem the transaction, generating financial income of Euro 2.3 million.

All the hedging relationships between the afore-mentioned derivative contracts and the related underlying liabilities qualify as Cash Flow Hedges in accordance with the International Accounting Standards; a specific negative equity reserve totalling Euro 7.7 million has been provided for the same.

The Hera Group is also party to other derivative contracts on rates, also in structured form, for a nominal residual total of Euro 72 million, whose value as of the year end date was negative for Euro 2.3 million (compared with Euro 3.5 million as at December 31, 2004).

When developing its core business activities, the Hera Group is also exposed to risks on the prices of energy products and the exchange rate risk due to potentially different price conditions applied to the sales and to the purchases of gas and electricity. The exposure to other financial risks (counterpart risk, liquidity risk, etc.) is not appreciable at present.
In this context, the Group's aim is to mitigate the risk of volatility in the forecast budget margins deriving, amongst other things, also from the regulation of the reference markets (for example: CIP6 and usage fees for transport). Therefore, a number of derivative contracts were stipulated so as to briefly align the index-linking formulas of the sales prices:

- to the index-linking formulas of the supply prices, in the event of supplies at index-linked prices;
- in fixed prices, in the event that said sales are supplied at a fixed price.

The agreements in question are represented by:

- 6 Swap agreements on the price of natural gas for a total notional value at year end of 26,640,000 m^3 against sales anticipated at a variable price. The value of these agreements is negative for a total of Euro 2 million.
- 5 Swap agreements on the price of electricity for a total notional value at year end of 710,203 MWh against sales anticipated at a variable price. The value of these agreements is positive for a total of Euro 0.8 million.

All the hedging relationships between the afore-mentioned derivative contracts and the related underlying sales qualify as Cash Flow Hedges in accordance with the International Accounting Standards; a specific negative equity reserve totalling Euro 1.2 million has been provided for the same.

The Hera Group is also party to other derivative contracts on commodities, for a residual notional total of 30,950,000 m^3 (whose value at year end was negative for Euro 2.1 million) and 20,680,266 MWh. These include the agreements stipulated with the Sole Purchaser on the basis of the action proceedings (Oil product), so as to reduce the exposure to the price risk of the "pun" generated by the ATEL contract. The two agreements, of a differential nature, even if not perfectly complementary in terms of quantities and price, were in fact destined to feel the contrary effect of the stockmarket price trend, as was effectively confirmed subsequently.

21. Other non-current assets

Other non-current assets as at December 31, 2005 amounted to Euro 33,799 thousand (Euro 43,804 thousand as at December 31, 2004) and mainly concern:

a. guarantee deposits, Euro 15,175 thousand;
b. trade receivables, Euro 4,648 thousand;
c. amounts due from shareholders, Euro 1,018 thousand (the called portion totalling Euro 59 thousand and the uncalled portion amounting to Euro 959 thousand);

d. amounts due for substitute tax on mortgage loans and freeing up of the goodwill generated following the creation of Hera spa in November 2002, Euro 12,036 thousand.

The decrease with respect to December 31, 2004, Euro 10,005, is mainly due to the reclassification of Euro 12,000 thousand pertaining to the guarantee deposit of Agea Reti Sr.l., classified in 2005 among “financial assets”.

22. Inventories

Inventories are made up as follows:

	31/12/2005 €/000s	31/12/2004 €/000s (adjusted)	Change €/000s
Raw materials and stock	34,730	35,241	-511
Work in progress and semi-finished products	284	2,675	-2,391
Finished products	682	3,509	-2,827
Advance payments	55	88	-33
Total	**35,751**	**41,513**	**-5,762**

Inventories as at December 31, 2005 are stated net of the obsolescence allowance amounting to Euro 1,407 thousand (Euro 843 thousand as at December 31, 2004). Inventories of raw, ancillary and consumable materials essentially comprise spare parts and equipment mainly intended for maintenance and the running of the operative plants, as well as stock of methane gas amounting to Euro 13,366 thousand.

23. Trade receivables

Trade receivables as at December 31, 2005 amounted to Euro 895,657 thousand (Euro 597,452 thousand as at December 31, 2004) and comprise estimated consumption, for the portion pertaining to the period, relating to bills and invoices which will be issued after December 31, 2005. The balances are stated net of the allowance for doubtful receivables amounting to Euro 23,442 thousand (Euro 15,385 thousand as at December 31, 2004) which is considered to be fair and prudent in relation to the estimated realizable value of said receivables. The recording of the allowance is made on the basis of analytical valuations in relation to specific receivables, supplemented by valuations based on historic analysis for the receivables regarding the general body of the customers (in relation to the aging of the receivables, the type of recovery action undertaken and the status of the creditor). The considerable increase in trade receivables when compared with the previous year if mainly reflected in the extension of the scope of consolidation to the Modena companies

€/000s	Dec. 31, 2004	Provisions	Uses	Change in consolidation area	Merger of Meta Group 31 Dec. 2005	Dec. 31, 2005
Allowance for doubtful receivables	15,385	5,565	-2,772	80	5,184	23,442
Total	**15,385**	**5,565**	**-2,772**	**80**	**5,184**	**23,442**

24. Contract work in progress

Contract work in progress as at December 31, 2005 disclosed a balance of Euro 20,688; as at December 31, 2004, the balance amounted to Euro 14,671.

25. Current financial assets

This balance, amounting to Euro 13,918 thousand as at December 31, 2005, mainly comprises amounts receivable for loans granted to municipal authorities (Euro 2,831 thousand), receivables for mortgage loans to be received (Euro 5,483 thousand), portfolio securities (Euro 5,062 thousand) and equity investments intended for sale (Penisolaverde, Euro 155 thousand and Ferrara Tua, Euro 310 thousand). As at December 31, 2004, the balance amounted to Euro 36,827 thousand and referred to equity investments intended for sale for Euro 19,680 thousand, securities amounting to Euro 14,805 thousand and amounts receivable for mortgage loans to be received totalling Euro 2,343 thousand.

26. Other current assets

Other current assets comprise:

	31/12/2005 €/000s	**31/12/2004** €/000s (adjusted)	**Change** €/000s
Direct/indirect taxation	82,472	5,330	77,142
Ires (corporation tax)/Irap (regional business tax) advances	11,924	848	11,076
Withholdings on interest	6	10	-4
Sundry amounts due from the tax authorities	9,100	1,787	7,313
Grants	4,475	2,485	1,990
Advances paid to suppliers/employees	6,923	12,044	-5,121
Amounts due from social security and welfare institutions	564	417	147
Insurance reimbursements	94	173	-79
Other receivables	29,969	21,828	8,141
Total	**145,527**	**44,922**	**100,605**

The item “direct/indirect taxation” amounting to Euro 82,472 thousand is essentially made up of the Group VAT credit amounting to Euro 3,064 thousand and advance payments for excise on methane gas totalling Euro 60,631 thousand (relating to the subsidiary company Hera Comm) and Euro 11,382 thousand (relating to the subsidiary Metaenergy). The increase recorded with respect to the previous year, amounting to Euro 63,695 thousand, is the result of greater advance payments calculated on the figures for 2004 when compared with the amounts invoiced for 2005 which saw a slowdown in invoicing essentially due to the introduction of the new SAP/ ISU invoicing system.

The item “Ires/Irap advances”, totalling Euro 11,924 thousand mainly comprises advance payments made by Hera spa as part of the procedure relating to the “tax consolidation” system.

The item "Other receivables" amounting to Euro 29,969 thousand includes amounts due from the Asset companies.

27. Cash and cash equivalents

As at December 31, 2005, cash and cash equivalents amounted to Euro 189,107 thousand (Euro 172,372 thousand as at December 31, 2004) and included cash, cash equivalents, cheques (bank and bankers' drafts) existing in the central fund and the decentralized funds amounting to Euro 125 thousand, deposits with banks and lending institutions available for current transactions and post office current accounts for a total of Euro 188,982 thousand (the increase on the previous year came to Euro 16,735 thousand).

28. Share capital and reserves

Share capital

The share capital as at December 312005 amounted to Euro 1,016,752,029 and was fully paid in; it is represented by 1,016,752,029 ordinary shares with a par value of Euro 1 each. The change in the share capital during the year is due to the issue of new shares allocated under exchange conditions to the shareholders of the absorbed company Meta S.p.A.

Reserves

The item "Reserves" totalling Euro 360,020 thousand comprises the share premium reserve for Euro 265,032 thousand, the legal reserve for Euro 10,184 thousand, the revaluation reserves for Euro 2,885 thousand, the extraordinary reserve for Euro 13,074 thousand, the merger surplus reserve for Euro 17,244 thousand, the reserve for share capital payments for Euro 5,400 thousand, the retained earnings reserve, negative for Euro 12,006 thousand and the IAS/IFRS reserve which amounts to Euro 58,207 thousand.

Cash Flow-Hedge Reserve

As at December 31, 2005, this reserve presented a negative balance of Euro 4,185 thousand following the valuation at fair value of the derivative instruments.

The statement which follows shows the changes in shareholders' equity accounts:

	Share capital	Reserves	Reserves for derivative instruments valued at fair value	Net profit for the year	Group shareholders' equity	Minority interests	Total
	€/000s	€/000s	€/000s	€/000s	€/000s	€/000s	€/000s
Balance as at December 31, 2004	**839,903**	**114,988**		**80,994**	**1,035,885**	**28,346**	**1,064,231**
Effect of applying IAS 39		-6,465	-2,474		**-8,939**	-1,381	**-10,320**
Adjusted balance as at January 1, 2005	**839,903**	**108,523**	**-2,474**	**80,994**	**1,026,946**	**26,965**	**1,053,911**
Meta Group merger	176,849	222,829			**399,678**		**399,678**
Change during period in fair value derivatives		2,231	-1,711		**520**	183	**703**
Use of reserves		-762			**-762**		**-762**
Other changes		-3,401			**-3,401**	42	**-3,359**
Allocation of 2004 net profit:					**0**		**0**
- dividends paid				-50,394	**-50,394**	-2,247	**-52,641**
- allocation to reserve		8,974		-8,974	**0**		**0**
- retained earnings		21,626		-21,626	**0**	-1,656	**-1,656**
Net profit for period				**80,346**	**80,346**	**7,316**	**87,662**
Balance as at December 31, 2005	**1,016,752**	**360,020**	**-4,185**	**80,346**	**1,452,933**	**30,603**	**1,483,536**

The statement which follows presents a summary of the differences between the statutory financial statements of the Parent Company and the consolidated financial statements, with reference to the items which have an impact on the net result for the year and on shareholders' equity.

RECONCILIATION BETWEEN THE STATUTORY FINANCIAL STATEMENTS OF THE PARENT COMPANY AND THE CONSOLIDATED FINANCIAL STATEMENTS

	NET RESULT	SHAREHOLDER EQUIT
BALANCES AS PER THE STATUTORY FINANCIAL STATEMENTS OF THE PARENT COMPANY	75,413	1,256,51
Effect on Parent Company of adopting the international accounting standards	**32,752**	**234,12**
IAS 17	1,010	2,24
IAS 19 and other employee benefits	502	(2,034
IAS 37: provision for restoration of third party assets	7,419	35,25
IAS 37: landfill post-closure provisions	(2)	12,47
IAS 38	15,966	16,65
IAS 39	(788)	(6,984
IAS 16	(1,094)	27,03
IAS 39: valuation at fair value of equity investments	0	
IAS 36: impairment test	9,738	
IFRS 3: Agea S.p.A.	0	16,95
IFRS 3 : Meta Group	(18,129)	113,09
Elimination of the effects of transactions between consolidated companies net of tax effects:		
- reversal of writedown on equity investments in subsidiary companies	108	
Effect of the change and the standardization of the accounting policies within the Group, net of tax effects:		
- Dividends recorded	(1,629)	
- Valuation at equity of companies carried at cost in statutory financial statements	1,376	(4,990
Book value of consolidated equity investments		(216,461
Shareholders' equity and net profit for year of consolidated companies	39,780	250,29
Allocation of differences to assets of consolidated companies and related amortisation/depreciation:		
- Goodwill on consolidation		9,36
- Dividends recorded on accruals basis	(48,858)	(48,858
- Other adjustments	(466)	(7,636
TOTAL	80,347	1,452,93
Allocation of portion pertaining to minority interests	7,316	30,60
BALANCES AS PER CONSOLIDATED FINANCIAL STATEMENTS	**87,663**	**1,483,53**

29. Banks and medium/long and short-term loans

As at December 31, 2005, medium/long-term loans amounted to Euro 534,518 thousand (Euro 489,063 thousand as at December 31, 2004) and mainly comprise mortgages and loans raised by the Parent Company.

As at December 31, 2005, short-term loans amounted to Euro 645,628 thousand (Euro 271,832 thousand as at December 31, 2004) and included amounts due to banks for Euro 637,718 thousand, amounts due to other providers of finance for the current portion of loans totalling Euro 5,810 thousand and amounts due to shareholders for loans amounting to Euro 1,202 thousand.

A list of the main mortgage loans outstanding as at December 31, 2005 is presented in the table below.

Lender	Residual balance	Current portion	Portion due within 5 years	Portion due beyond 5 years
CASSA DEPOSITI E PRESTITI	33,923,380.26	3,596,803.58	14,964,681.83	15,361,894.85
BANCA OPI	79,293,239.59	13,468,694.72	49,493,364.42	16,331,180.45
BANCA DELLE MARCHE	1,037,273.76	167,135.50	763,057.67	107,080.59
BNL	516,456.86	258,228.46	258,228.40	-
BANCA POPOLARE DI RAVENNA	332,441.83	79,759.65	252,682.18	-
BANCA DI SICILIA	551428.22	210520.59	340907.63	
CASSA DI RISPARMIO DI RIMINI	490,877.60	490,877.60	-	
CASSA DI RISPARMIO DI CENTO	1,433,162.10	393,224.13	1,039,937.97	-
CARISBO	7,123,160.36	730,734.28	3,550,453.66	2,841,972.42
CASSADI RISPARMIO DI CESENA	9,104,568.96	2,237,040.36	5,214,144.43	1,653,384.17
CREDIOP	1373710.6	780655.69	593054.91	
CASSA DI RISPARMIO DI RAVENNA	2,061,643.20	83,534.40	377,800.16	1,600,308.64
FON SPA	5,638,959.35	514,565.38	2,320,225.99	2,804,167.98
INTERBANCA	8,863,741.73	2,446,791.23	6,416,950.50	-
BANCA INTESA	112,841,714.56	20,790,355.15	72,907,622.56	19,143,736.85
MCC	41,092,699.48	-	1,717,699.48	39,375,000.00
MEDIOCREDITO	60,000,000.00	-	60,000,000.00	-
MONTE DEI PASCHI DI SIENA	26,469,455.33	4,811,413.27	19,313,121.67	2,344,920.39
S.PAOLO	2,415,601.55	251,710.78	1,885,845.47	278,045.30
UNICRED	13,832,180.61	5,337,094.43	7,956,471.91	538,614.27
UNIPOL	65,000,000.00	13,000,000.00	52,000,000.00	-
PROJECT FINANCING	95,648,000.00	10,640,000.00	45,472,000.00	39,536,000.00
Total	**569,043,695.95**	**80,289,139.20**	**346,838,250.84**	**141,916,305.91**

Medium/long-term amounts due to banks also include loans subscribed by the subsidiary FEA Srl (residual debt amounting to Euro 85,008 thousand). These loans are guaranteed by mortgages and special liens in favour of the pool of banks which subscribed the project financing without recourse, guaranteeing the envisaged loans. The repayment of this loan, which has a final maturity date as at December 31, 2017, is contractually established in six-monthly instalments at a “6-month Euribor rate plus a spread”.

30. Provision for employee leaving indemnities and other similar benefits

This item represents the provisions made in favour of staff for the leaving indemnity due in accordance with the law, net of the advances paid out to employees, calculated considering the overall credit which the employees will accrue as of the date they will presumably leave the company (on the basis of hypothesis and using actuarial techniques) and quantifying on an accruals basis the future liability portion discounted back to the balance sheet date.

In accordance with Italian statutory legislation, the employee leaving indemnity is reflected in the financial statements in accordance with a calculation method based on the indemnity accrued by each employee as of the balance sheet date, in the event that all the employees terminate their employment contract as of that date. This method has been considered acceptable so far in accordance with the international accounting standards.
IAS 19 by contrast anticipates the adoption of a method by means of which the sum total of the liability for the benefits acquired must reflect the date of expected resignation and must be discounted back.

Euro thousands	**Dec. 31, 2004**	**Service cost**	**Financial charges**	**Uses and other changes**	**Change in consolidation area**	**Dec. 31, 2005**
Employee leaving indemnity	76,836	7,803	1,886	-8,885	17,986	95,626
Gas discount	3,314	2	78			3,394
Premungas fund	2,484	2	32	-636		1,882
Total	**82,634**	**7,807**	**1,996**	**-9,521**	**17,986**	**100,902**

The change in the scope of consolidation is essentially due to the merger transaction with the Meta S.p.A. Group which took place on December 31, 2005.

The main assumptions used in the actuarial estimate of the employee benefits are as follows:

	2004	**2005**
Discounting back rate, average	4.1%	3.6%
Cost of labour increase rate, average	2.8%	2.8%

31. Provisions for risks and charges

The composition and analysis of the changes in provisions for risks and charges is as follows:

€/000s	Dec. 31, 2004	Provisions	Use and other changes	Change	Dec. 31, 2005
Pensions and similar commitments	36	7	-7	92	128
Staff disputes and legal costs	3,649	2,525	-303	3,993	9,864
Landfill closure and post-closure costs	33,455	6,582	347	12,164	52,548
Restoration of third party assets	24,991	10,828	0	0	35,819
Other provisions:					
Risks and charges	17,075	3,261	-6,699	4,266	17,903
Tariff reductions	0	0	0	3,661	3,661
Total	**79,206**	**23,203**	**-6,662**	**24,176**	**119,923**

The provision for staff disputes and legal costs amounting to Euro 9,864 thousand, reflects the assessments of the outcome of lawsuits and disputes brought by employees.

The provision also includes Euro 1,840 thousand relating to an initial dispute pending with INPS (national social security institute) concerning the alleged payment of contributions on involuntary unemployment, social security benefits (CIG, CIGS, Mobility) and sick-leave for blue-collar workers.

As far as involuntary unemployment is concerned, the Group believes that it is not obliged to pay this contribution by virtue of specific contractual clauses which, limiting the power to withdraw of the employer, in fact ensures the stability of the employment relationship with the employees. Requests for exemption have been presented for each Group company in relation to this contribution. In each case where the Ministry has passed sentence rejecting the request, the reject Decree has been contested.

In relation to the contributions on CIG, CIGS and Mobility, the exclusion is supported not only by specific legal norms but by the fundamental consideration that the social security benefits are effectively unusable since the Hera Group runs essential services which must be constantly ensured. By contrast, INPS believes that the transformation into a joint-stock company and the transfer to private parties of even just a portion of the share capital, support the belief that the contributory obligation is enforceable. The Group's theory was upheld in 2004 by means of the sentence of the Genoa court, but subsequently amended under appeal in November 2005. An appeal is currently pending before the Supreme Court.

In conclusion, the contributions relating to blue-collar workers' sick-leave are considered not to be due since, as a result of an express contractual clause, the Group personally undertakes the entire sick pay liability. This is in accordance with a norm of the corporative period applied without controversy for 60 years. In 2003, a sentence of the Supreme Court however stated the existence

of the contributory obligation to the charge of the employer even if the welfare institute is not obliged to provide sickness benefits, referring to a general solidarity principle. Following this change in case law policy, the Hera Group considered it appropriate to pay the sickness contribution as from January 1, 2005, holding out however in the pending dispute relating to previous years.

Bearing in mind the above, in addition to the favourable judgement expressed by the Council of State upon the request of the Department of Employment and Social Policies concerning the application of the afore-mentioned legislation to Enel S.p.A. (opinion dated February 8, 2006), the Hera Group classified the risk of losing the lawsuit possible, but not probable. The provision present in the financial statements is therefore prudent and refers to the total of just the tax forms - not suspended by a ruling of the ordinary judge– received up until the balance sheet date and the consequent legal costs.

The second dispute outstanding with INPS (deriving from the merged company Meta spa) by contrast relates to the interpretation of Article 41 of Italian Law No. 488/1999 (2000 Finance Bill) concerning the reduction to the contribution rates for family allowance for families (CUAF) and for the MATERNITY contribution in relation to staff disciplined by the electricity sector collective labour agreements (CCNL). The problem was faced with the Insurance Positions Management Office of the Modena INPS branch, which confirmed the correctness of the request originally presented. Consequently, as from 2001, the former Meta spa applied the reduction to the rates at the same time as the request for reimbursement of the additional contributions paid over, which were not due, relating to 2000, (reimbursement which was then made between 2001 and 2002). As from November 2003, INPS served the notices by means of which it requested the payments of the contributions at the full rate, completely amending the interpretative position previously adopted, deeming that the harmonization of the rates owed by the electricity sector was not applicable for the workers enrolled with INPDAP. The Company has appointed the trade association "Federenergia" to look into the question; this association submitted the question before the Department of Employment and at present we are awaiting the latter to express the decisions to be adopted. In the meantime, amounts have prudently been set aside relating to the contributions which might be subject to dispute for the period January, 1 2000 – December 31, 2005, equating in total to Euro 3,097 thousand.

The **landfill closure and post-closure costs provision** represents the amount set aside by the Group to cover the costs which will have to be incurred for the management of the closure and post-closure period pertaining to the landfills currently in use. The future outlays, calculated for each landfill by means of a specific appraisal, have been discounted back in compliance with the provisions of IAS 37. The increases in the provision comprise the financial component inferred from the discounting back procedure, while the uses represent the effective outlays which came about during the year.

The **provision for the restoration of third party assets** includes the provisions made in relation to the legal and contractual restrictions encumbering the Group in its capacity as leaseholder of the distribution networks owned by the asset companies. These provisions have been made on the basis of the normal depreciation rates envisaged for the assets in question; rates established

contractually for the purpose of compensating the lessor companies for the wear and tear of the assets used for the business activities, applied to the value of the assets received under lease.

In observance of the matters laid down by IAS 37, the provision reflects the current value of these outlays which will be determined in future periods (as a rule on expiry of the agreements entered into with the area agencies, as far as the water service is concerned, and on expiry of the transitory period anticipated by current legislation as far as gas distribution is concerned). The increases in the provision comprise the sum total of the provisions for the year, including those discounted back, and the financial charges which reflect the element deriving from the discounting back of the flows on an accruals basis.

The **provision for risks and charges**, under the item "other provisions", amounting to Euro 17,903 thousand, comprises provisions made against sundry risks (all for an essentially modest amount).
With regards to the problem relating to the application of the Authority for Electricity and Gas Resolution No. 248/04, reference should be made to the matters more fully described in the report on operations under section 3.01.02.02. In consideration of the fact that the risk of a negative impact is deemed remote, no provision has been made in this connection.

The **tariff reduction provision**, totalling Euro 3,661 thousand, has been provided to cover the charges deriving from the acknowledgement to retired staff of tariff concessions for electricity consumption.

32. Deferred tax liabilities

As at December 31, 2005, this balance amounted to Euro 94,614 thousand (Euro 53,036 thousand as at December 31, 2004). The provision for deferred taxes comprises the timing differences between the net profit and the taxable income and those which emerged following the application of the IAS/IFRS. These liabilities are collectable when the differences which generated them reverse to the income statement. In particular, the differences generated by the application of the IAS/IFRS mainly relate to:

- IAS 17 (financial leasing) for Euro 3,644 thousand;
- IAS 16 (revaluation at fair value of some categories of assets) for Euro 42,000 thousand;
- IAS 37 (discounting back of landfill post-closure provisions and provision for the recovery of third party assets,) for Euro 32,900 thousand;
- IAS 19 (discounting back of the provision for employee leaving indemnities and other similar benefits) for Euro 3,650 thousand;
- IAS 39 (fair value of derivative instruments) for Euro 1,620 thousand.

33. Financial leasing payables

As at December 31, 2005, this balance amounted to Euro 49,643 thousand (Euro 28,730 thousand as at December 31, 2004).

	Residual balance	Current portion	Non-current portion

Financial leasing payables	49,643	9,784	39,859

This item represents the booking of the payables as a result of IAS 17 under financial lease transactions.

34. Other non-current liabilities

As at December 31, 2005, other non-current liabilities amounted to Euro 105,344 thousand (Euro 91,135 thousand as at December 31, 2004); the breakdown is as follows:

	31/12/2005 €/000s	31/12/2004 €/000s (adjusted)	Changes €/000s
Payables due to social security and welfare institutions	11	17	-6
Guarantee deposits	50,836	43,583	7,253
Payables for contributions towards inlets/outlets, pipelines and other	51,818	45,089	6,729
Advance payments	1,527	1,546	-19
Suppliers	920	645	275
Sundry	232	255	-23
Total	**105,344**	**91,135**	**14,209**

35. Trade payables

Amounts due to suppliers, all of which of a trade nature and inclusive of the provision for invoices to be received, amounted to Euro 670,051 thousand as at December 31, 2005 and Euro 432,923 thousand as at December 31, 2004. The increase is mainly attributable to the change generated by the inclusion in the consolidation area of the Modena companies.

36. Tax liabilities

As at December 31, 2005, tax liabilities totalled Euro 32,545 thousand (Euro 86,670 thousand as at December 31, 2004); they are analysed as follows:

	31/12/2005 €/000s	31/12/2004 €/000s (adjusted)	Change €/000s
Payables due for income taxes (IRES, IRAP) and tax on consumption	17,237	59,045	-41,808
VAT payables	334	13,400	-13,066
Payables due for employee withholdings	5,718	3,860	1,858
Substitute tax	76	80	-4
Sewerage charges	652	1,021	-369
Other tax liabilities	8,528	9,264	-736
Total	**32,545**	**86,670**	**-54,125**

The item “payables due for income taxes and tax on consumption” disclosed a decrease with respect to December 31, 2004 equating to Euro 41,808 thousand, due mainly to lower tax liabilities for direct taxation (IRES – corporation tax and IRAP – regional business tax) and for tax on

consumption and regional surtax, following the slowdown in the invoicing process due to the introduction of the new SAP/ ISU invoicing system. The decrease in VAT payables when compared with December 31, 2004, amounting to Euro 13,066 thousand, was also attributable to the same causes.

37. Other current liabilities

As at December 31, 2005, other payables amounted to Euro 70,902 thousand (Euro 65,892 thousand as at December 31, 2004), the breakdown is as follows:

	31/12/2005 €/000s	**31/12/2004** €/000s (adjusted)	**Change** €/000s
Payables due to social security and welfare institutions:			
INPS – national social insurance institute	2,544	1,810	734
INPDAP - national social insurance institute for civil service employees	5,362	5,444	-82
INAIL – national institute for insurance against industrial injuries	0	3	-3
Other institutes	5,992	5,081	911
Dividends	7	7	0
Payables due to employees	15,967	14,391	1,576
Payables due to Directors and Statutory Auditors	343	253	90
Guarantee deposits	33	31	2
Payables due to users	272	332	-60
Payables due for write-off plans	12,288	7,822	4,466
Other	28,094	30,718	-2,624
Total	**70,902**	**65,892**	**5,010**

IAS 14: Information by business area

2005 balance sheet

	Gas	Electricity	Water cycle	Waste management	Other services	Consolidated financial statements
Net working capital	132.6	61.5	34.0	79.7	14.2	322.0
Net fixed assets	459.1	186.8	689.3	785.1	236.0	2356.3
Provisions	43.4	7.8	50.9	105.4	13.3	220.8
Net invested capital - Hera	**548.3**	**240.5**	**672.4**	**759.4**	**236.9**	**2457.5**
Shareholders' equity						1483.5
Net financial position						974.0

GUARANTEES GIVEN

The main guarantees given to third parties are described below.

- secured guarantees relating to mortgages and special liens on land, plant and machinery recorded by the subsidiary Fea Srl in favour of a pool of banks for project financing without recourse, amounting to Euro 216,909 thousand;
- unsecured guarantees given by the Parent Company in favour of the associated company Acantho S.p.A. for Euro 23,020 thousand (including Euro 15,000 thousand by means of non-binding letter of patronage) against the loan without recourse obtained by said Acantho S.p.A.; letter of patronage for an equivalent value of Euro 8,020 thousand against financial leasing agreements stipulated by Acantho S.p.A.;
- unsecured guarantees given by the Parent Company in favour of the associated company SET S.p.A. for Euro 51,714 thousand against the loan obtained from a pool of banks by SET S.p.A.;
- unsecured guarantees given by the Parent Company in favour of the associated companies Acantho S.p.A. and SET S.p.A., respectively for Euro 86 thousand and Euro 53,171 thousand guaranteeing contractual obligations ;
- unsecured guarantees given by the Parent Company in favour of the area agencies (ATO) of Ravenna and Forlì Cesena for Euro 4,400 thousand guaranteeing the contractual obligations relating to the management of the integrated water service in the related municipalities;
- sureties issued by BNL in favour of leasing companies relating to the subsidiary Ecologia Ambiente for Euro 21,567 thousand;
- a surety issued by the subsidiary Medea SpA in favour of the Municipality of Sassari guaranteeing work for the extension of the gas mains in said municipal area for Euro 4,779 thousand;
- a surety issued by the subsidiary Sotris SpA in favour of the province of Ravenna guaranteeing the environmental impact deriving from activities for the management of the landfills for Euro 15,727 thousand;
- sureties given in favour of third parties for Euro 238,670 thousand against various contracts. The most significant amount concerns the surety issued by Unicredit Banca d'Impresa S.p.A., (amounting to Euro 25,696 thousand), in favour of the municipality of Pesaro as mandate of the public shareholders of ASPES Multiservizi SpA, to guarantee fulfilment of the obligations of Hera S.p.A. following the stipulation of the sale agreement. In particular, on September 19, 2002, Hera S.p.A. signed a contract in which it acquired a shareholding equal to 24% of the share capital in ASPES Multiservizi S.p.A. In 2004 Hera SpA increased its shareholding to 26.86% being committed to acquire, on request of the public shareholders of Aspes Multiservizi SpA, further holdings up to a maximum amount of 65% of the share capital. This obligation will expire on September 18, 2006, the surety has a duration equal to 4 years from the date of the contract that may be unconditionally extended at the request of the municipality of Pesaro for a further 6 months.
- Third party assets in use mainly comprise assets used by the Parent Company for Euro 706,279 thousand by way of concession, for Euro 665 thousand by way of business rental

and for Euro 15,049 thousand by the subsidiary Medea by way of concession for the gas mains from the municipality of Sassari .

TRANSACTIONS WITH RELATED PARTIES

Management of the services

The Hera Group exclusively performs in almost all of the territory of the shareholder Municipalities, the local public services of gas distribution, management of the integrated water cycle and management of the waste cycle (sweeping, collection, transport, recovery and disposal).

In some municipalities the Group carries out "other services" such as urban district heating and heat management, funeral and crematory services, public parks management, electricity distribution (in the Imola area and in the municipality of Modena); by means of specific conventions with the local entities Hera is also requested to carry out the treatment and disposal of waste, excluded from the regional Law 25/1999 but subject to control by the regional Agency that regulates public services. A process is currently underway for the rationalization, whose objective is the concentration of the resources and the investments in the core sectors (electricity, water and waste management).

In relation to only the local services (urban hygiene and water cycle), regulated by article 113 of the Consolidation Act for the regulation of the local authorities, the afore-mentioned regional law assigned the area agency authorities (AATO), envisaged by national legislation, the regulation and control functions previously carried out by the municipalities.

In respect of this regulation the Hera Group signed and continues to sign specific conventions with each ATO that results in the entry into force of the technical and tariff planning.

Energy sector

In relation to the contracts in the Gas Area the management of the service is, as per normal practice, exclusively awarded to the Hera Group.

The duration of the natural gas concessions via local gas ducts, initially fixed for a period between ten and thirty years by the normal concessions agreed with the Municipalities, was reviewed by Italian Decree 164/2000 (Letta decree, reflecting the contents of the EU directive 30/98) and the subsequent law on the reorder of the energy market (known as the "Marzano Law") which establishes the deadline for the concessions in the provincial areas of Bologna, Forlì Cesena and Rimini as 2011 and the deadline for the concessions in the provincial areas of Ferrara, Imola Faenza and Ravenna as 2012.

The conventions relating to the distribution concessions concern the distribution of methane gas or other similar, heating, domestic uses, artisan, industrial and for other general use. Some of these conventions provide for the production and distribution of thermal energy. The tariffs for gas distribution applied to the users are collected by HERA and are fixed in accordance with the regulations in force and the resolution of the Authority for Electricity and Gas.

The contractual deeds discipline the relationship with the customer, the management of the service, the respective accessory obligations of the parties, the maintenance charges for the functioning of the distribution network and the penalties for the irregular provision of the service that generally varies based on the type and gravity of the infringement committed.

In relation to the electricity area, the contracts relate to the distribution of energy including the management of the distribution network, decisions on maintenance work, programming and

identification of the development interventions, the functioning of the plants and the carrying out of maintenance and development.
The most significant convention for the distribution of electricity was agreed with the Municipality of Imola, has a duration of thirty years with expiry on December 31, 2030 and is renewable based on the provisions of Article 2 of the Bersani Decree. An identical concession concerns the management of the networks previously belonging to META SpA, pertaining to HERA following the merger by incorporation of Meta S.p.a. within Hera S.p.A. with backdated effect as at January 1, 2005.

The Authority for Electricity and Gas may suspend or revoke the concession, based on a predetermined procedure against non compliance and violations attributable to the company granted the concession, that harms in a serious manner the provision of the electricity distribution service.
The awarding of the concession does not result in the recognition of exclusive rights.
The company awarded the concession is obliged to apply to the users fixed tariffs in accordance with regulations in force and deliberations adopted by the Authority for Electricity and Gas .

Water sector
HERA manages the integrated water service; the conventions with the area agencies, featuring a variable duration (no less than twenty years), concern the aqueduct service or the sewerage and purification service or the combination of the aqueduct, sewerage and purification services.
The management of the aqueduct service includes the public services of collection, purifying, distribution and sale of drinkable water for civil and industrial use; the sewerage and purification services include the management of the networks and sewage and purification plants.
In some cases, the conventions provide for the planning and construction of new networks and plants to use in the management of the service.
The management of the service is awarded exclusively to HERA for the municipal territory involving the obligation of the Municipality not to grant to third parties usage of the subsoil of its property or state aqueducts without the prior consent of HERA.
The conventions regulate, in addition, other aspects such as the manner of managing the services as well as reciprocal obligations between the parties relating to, principally, the charges for ordinary and extraordinary maintenance work on the networks and plants necessary for the functioning of the services.
The contracts normally establish that the local entities grant to the operator, even without charge, the right to use the networks and plants for the functioning of the integrated water cycle. In the majority of the cases concerning the areas managed by HERA, the local entities have conferred the ownership of networks and plants to special purpose Asset Companies.
At the end of the concession Hera has the obligation to return the assets utilised for the provision of the service to the asset companies, or rather the municipalities. Any works carried out for the innovation or improvement of the networks must be returned, at the end of the concession against payment of the residual value of those assets.
HERA's dealings with the users are disciplined and regulated by specific "Service Charters" that describe in detail the services to be provided by the operator and the rights of the users.

The fee received by HERA for the management of the integrated water service consists of the payment of the tariffs in force determined, from 2004, on the basis of the standardized method introduced by the Galli law and subsequent legislation.

Waste management sector

The conventions stipulated by HERA with the area agencies concern the exclusive management of the waste collection, sweeping and road cleaning services, and the recovery and disposal of waste services.

The duration of the Conventions is fixed by the regional regulations as ten years. The conventions discipline the method for the functioning of the services, the amount payable to Hera for the services performed (equal to the tariff, where implemented, in accordance with Italian Presidential Decree No. 158/1999), the reciprocal obligations of the parties and the cost of the rental concession for the use or occupation by the operator of roads and surrounding area for the performance of the service carried out.

For the use of the waste treatment plants, the HERA Group has agreed specific conventions with the Municipalities where the plants are located.

Management of the networks, plants and equipment

The infrastructures via which the local public services are carried out, or rather the gas networks and the aqueduct and sewerage networks, are in part owned by HERA and in part owned by third parties (Municipalities, Consortium of Municipalities, Asset Companies). The dealings between the service operators and the owners of the operating assets are disciplined by specific conventions; the regulation of the economic elements is, in some cases, covered by rental agreements which fix the fee payable by the Operator to the owners for the use of the networks and plants.

Based on these contracts HERA must carry out, at its own expense, ordinary and extraordinary maintenance as well as the expansion of the networks, as provided for in the investment plans agreed with the Asset Companies.

On the expiry of the contract, HERA will return the business divisions and at the same time pay the difference between the initial value of the assets on stipulation of the rental contract (value equal to that resulting from the net book values recorded in the Asset Companies at the date of the rental) and the value of the aforesaid assets on termination of the contract. This latter value will be calculated by deducting, from the initial value of the assets that constitute the business divisions, the depreciation incurred by the HERA Group on the rented assets up to the date of the return, adding to these values the net investments (or rather the net book value of the investments made by HERA up to the date of the return).

Integrated water cycle

For the period of the contract subsequent to December 31, 2006, the rental will be equal to a sum corresponding to the final value (that indicated in the rental contract of the business division) multiplied by the percentage established in the tariff as a percentage remuneration on the net capital invested, as determined by the application of the normalised method for the determination of the tariffs as per Regional Law No. 25/1999

Gas distribution

The rental contract of the business divisions relating to energy services do not indicate the amount of the rental for the periods after December 31, 2006.

Assets granted under rental contracts by CON.AMI

There is a rental contract in force with the consortium CONAMI of Imola for the use of the networks and assets necessary for the carrying out of the distribution of gas and electricity, waste management, water and district heating services owned by them. This contract contains similar provisions to those contained in the contracts with the Asset Companies.

State property conceded in use to HERA together with the awarding of the services

The state properties utilised by HERA for the carrying out of the activities are granted under use to HERA together with the awarding of the relative public services.

Transactions between HERA and Romagna Acque

The Municipalities of Ravenna, Forlì, Cesena and Rimini, principal shareholders of HERA, are also the principal shareholders of Romagna Acque with whom AMF, AMIR, AREA, SIS, TEAM and UNICA, companies taking part in the integration, have agreed contracts for the procurement of water prior to the merger in HERA SpA. Following the spin-offs and mergers of business units relating to the afore-mentioned Company, HERA took over the above-mentioned procurement contracts.

During 2004, the shareholder Municipalities of Romagna Acque conferred to this company the ownership of the water sources, previously attributed to the relevant asset companies; at the same time Romagna Acque changed its name to “Romagna Acque - Società delle Fonti”. For the areas of Ravenna, Forlì - Cesena and Rimini, thus, Romagna Acque has exclusive ownership of the procurement assets, while the ownership of the networks remains within the asset companies.

Transactions between HERA and Frullo Energia Ambiente S.r.l. (FEA)

FEA operates in the sector for the management of waste treatment plants and is specifically involved in the management of the Frullo waste-to-energy plant (situated in Via del Frullo 5, Granarolo dell’Emilia, Bologna). HERA holds a 51% interest in FEA’s share capital, while the remaining 49 % is held by Actelios S.p.A.

The waste-to-energy plant was conferred on January 1, 2001 by Seabo, now HERA. The renovation and the construction of the new production line was completed in 2004, the year in which the plant was equipped with an electricity generation capacity of 22 MW.

During 2002, HERA and FEA signed the contractual restrictions relating to the conferral of the waste (Put-or-Pay) and the procurement of the thermal energy (Take-or-Pay) up until the date of the start-up of the new plant. As of this date, the contractual restriction concerning the same subject will enter into force, relating to the newly construction plant, featuring a 25-year duration.

Transactions between HERA and HERA COMM S.r.l. Unipersonale

HERA COMM S.r.l. Unipersonale is wholly-owned by HERA and is set up to supply energy (gas, electricity and district heating) to end users, in observance of the corporate separation norms envisaged by the Letta Decree.

HERA Comm arose from Seabo Energia which, following the integration process, was granted the business segment relating to the energy customers, and which, simultaneously, in November 2002 adopted its current name of HERA COMM S.r.l. Unipersonale.

Transaction between HERA and the Territorial Operating Companies

At the beginning of 2003, the five territorial companies were granted the business segments containing the technical equipment, human and financial resources so as to be able to carry out the network management activities (water, gas and electricity) and the waste collection activities throughout the respective areas they are responsible for. These activities are disciplined by service agreements stipulated between Hera and said territorial companies.

A list of the costs, revenues, receivables and payables, which the Parent Company Hera S.p.A. is due or owes to subsidiary and associated companies, in that they are related parties, is shown below. The costs, revenues, receivables and payables relating to just the subsidiary companies have been eliminated from the consolidated financial statements.

Subsidiary and associated companies

SUBSIDIARY COMPANIES	**31_December_2005**
Costs	
Use of third party assets	7,633,577
Raw, ancillary and consumable materials and goods for resale	44,040,704
Services	931,158,937
Interest expense and other charges relating the Group companies	545,655
Other operating costs	133,685
TOTAL COSTS	**983,512,558**
Revenues	
Other income and revenues	7,011,201
Income from long-term receivables from Group companies	109,149
Income from equity investments	1,273,095
Revenues from sales and services	688,422,337
TOTAL REVENUES	**696,815,782**
Receivables due from Group companies	**737,606,919**
Payables due from Group companies	**611,739,279**
ASSOCIATED COMPANIES	
Costs	
Use of third party assets	1,965,824
Raw, ancillary and consumable materials and goods for	4,136,363

resale	
Services	4,919,847
Interest expense and other charges relating the Group companies	891
Other operating costs	4,754,318
TOTAL COSTS	**15,777,243**
Revenues	
Other income and revenues	1,850,329
Income from long-term receivables from Group companies	596,882
Income from equity investments	429,292
Revenues from sales and services	3,996,445
TOTAL REVENUES	**6,872,948**
Receivables due from Group companies	**35,975,657**
Payables due from Group companies	**7,572,535**

Affiliated companies

	Receivables	Payables	Revenues	Costs
Municipality of Bologna	17,532,710.19	-1,657,740.16	-63,120,572.08	7,726,723.09
CON. AMI	528,559.02	-1,818,056.65	-1,696,061.85	7,833,626.82
Romagna Acque spa	34,719.43	-7,572,177.31	-75,446.99	23,212,327.54
Unica reti assets	750,779.41	-2,334,629.97	-87,099.67	8,249,430.93
AMF assets	1,746,461.88	-48,110.56	-225,619.14	13,050.99
AMIA assets	8,295.69	0.00	0.00	10,038.69
AMIR assets	2,186,659.25	-924,818.96	-482,767.70	2,322,428.92
AREA assets	1,138,121.72	-3,828,942.64	-334,994.18	5,320,874.34
TEAM assets	1,138,121.72	-3,828,942.64	-334,994.18	5,320,874.34
SIS spa	3,038,370.76	-1,985,547.81	0.00	2,047,580.62
Municipality of Modena	8,265,809.88	-15,393,396.73	-46,821,918.24	5,421,210.56

FINANCIAL TRANSACTIONS

The Parent Company, Hera S.p.A., operates as a centralized cash management body for some of the Group companies (mainly those which were formed following the spin-offs of business segments).

This relationship evolves via current accounts between the Parent Company and the subsidiaries.

Furthermore, the Parent Company has granted long and short-term loans to the following companies:
Medea S.p.A., Euro 492,000 thousand;
Ares S.p.A., Euro 1,269 thousand;
Frullo Energia Ambiente S.r.l., Euro 4,284 thousand;
Rio d'Orzo S.r.L., Euro 500 thousand;
SET S.p.A., Euro 18,447 thousand;
Recupera S.r.L., Euro 700 thousand;
Delta Web S.p.A., Euro 152 thousand;
4 Four Italy, Euro 276 thousand;
Sotris, Euro 3,860 thousand.

Hera S.p.A. also acts as guarantor in favour of the Group companies which directly undertake financial debts with banks.

Other financial transactions include those deriving from the Group VAT procedure and the tax convention.

COMMERCIAL TRANSACTIONS

The Parent Company provides the subsidiaries and associated companies with administrative, financial, legal and management services for the purpose of optimising the resources available within the Company within a logic of economic advantage. These services are disciplined by specific service agreements.

3.04 List of equity investments

3.04.01 List of consolidated companies

Companies consolidated by the line-by-line method *(in Euro)*

(in Euro) Company name	Registered Offices	Share capital	Ownership %		Total	Total holding
			Direct	Indirect		
Parent company:						
Hera S.p.A.	Bologna	1,016,752,029				
Subsidiaries:						
Agea One S.r.l. in liquidation	Cassana (Fe)	2,300,000	100.00 %		100.00 %	100.00 %
Akron S.p.A.	Imola (BO)	1,152,940	57.50 %		57.50 %	57.50 %
Ares S.p.A. consortile	Bologna	1,125,240	100.00 %		100.00 %	100.00 %
Asa S.p.A.	Castelmaggiore (BO)	1,820,000	51.00 %		51.00 %	51.00 %
Bio Energy S.r.L.	Modena	100,000	100.00 %		100.00 %	100.00 %
Cales S.r.l.	Imola (BO)	250,000	50.01 %		50.01 %	50.01 %
Ecologia Ambiente S.r.L.	Ravenna	20,000,000	100.00 %		100.00 %	100.00 %
Ecosfera S.p.a.	Ferrara	1,000,000	51.00 %		51.00 %	51.00 %
Eris S.c.r.l.	Ravenna	300,000		51.00 %	51.00 %	51.00 %
Famula On-line S.p.A.	Bologna	3,316,427	60.00 %		60.00 %	60.00 %
Frullo Energia Ambiente S.r.l.	Bologna	17,139,100	51.00 %		51.00 %	51.00 %
Gal.A. S.p.A.	Bologna	300,000	60.00 %		60.00 %	60.00 %
Hera Bologna S.r.l.	Bologna	1,250,000	100.00 %		100.00 %	100.00 %
Hera Comm S.r.l.	Imola (BO)	88,591,541	100.00 %		100.00 %	100.00 %
Hera Energie Bologna S.r.l.	Bologna	500,000		67.00%	67.00%	67.00%
Hera Ferrara S.r.l.	Cassana (FE)	810,000	100.00 %		100.00 %	100.00 %
Hera Forlì-Cesena S.r.l.	Cesena (FC)	650,000	100.00 %		100.00 %	100.00 %
HERA GAS TRE Spa	Bologna	120,000	100.00%		100.00%	100.00%
Hera Imola-Faenza S.r.l.	Imola (BO)	750,000	100.00 %		100.00 %	100.00 %
Hera Luce S.r.l.	San Mauro Pascoli (FC)	216,600	69.30 %		69.30 %	69.30 %
Hera Ravenna S.r.l.	Ravenna	850,000	100.00 %		100.00 %	100.00 %
Hera Rimini S.r.l.	Rimini	1,050,000	100.00 %		100.00 %	100.00 %
Herasocrem S.p.A.	Bologna	2,218,368	51.00 %		51.00 %	51.00 %
Hera Trading S.r.l.	Imola (BO)	2,600,000	100.00 %		100.00 %	100.00 %
Ingenia S.r.l.	Imola (BO)	52,000	74.00 %		74.00 %	74.00 %
Medea S.p.A.	Sassari	4,500,000	100.00 %		100.00 %	100.00 %
Metaenergy S.r.L.	Modena	13,795,000	100.00 %		100.00 %	100.00 %
Metaservice S.r.L.	Modena	2,492,000	51.00 %		51.00 %	51.00 %
Nuova Geovis S.p.A.	Sant'Agata Bolognese (BO)	2,205,000	51.00 %		51.00 %	51.00 %
Recupera S.r.l.	Cassana (FE)	1,673,290	75.50 %		75.50 %	75.50 %
Romagna Compost S.r.l.	Cesena (FC)	310,000	60.00 %		60.00 %	60.00 %
Seas Lavori e Servizi s.c.ar.l.	Bologna	51,000	6.00 %	94.00 %	100.00 %	100.00%
Sinergia S.r.l.	Forlì (FC)	579,600		59.00 %	59.00 %	59.00 %
Sotris S.p.A.	Ravenna	2,340,000	70.00 %		70.00 %	70.00 %
TS Distribuzione S.r.l.	Monghidoro (BO)	100,000	100.00%		100.00%	100.00%
TS Energia S.r.l.	Monghidoro (BO)	10,000		100.00%	100.00%	100.00%
Uniflotte S.r.l.	Bologna	2,254,177	99.00 %		99.00 %	99.00 %
Viviservizi S.r.l. Consortile	Bologna	451,500	80.76 %		80.76 %	80.76 %

Companies consolidated on a line-by-line basis include Hera Ferrara S.r.L., carried at cost as at December 31, 2004, since it became operative as at January 1, 2005. The share capital increased from Euro 10,000 to Euro 810,000, subscribed and fully paid-in by Hera S.p.A.

During 2005, Hera S.p.A. took steps to make a series of acquisitions of investments in ARES, from private shareholders, raising its shareholding from 65% (December 31, 2004) to 100% as at December 31, 2005.

As at February 11, 2005, Cales S.r.L. resolved a share capital increase from Euro 11,000 to Euro 250,000, involving an increase of Euro 239,000. The shareholders have paid in 25% of this increase on the basis of the shareholdings held. A change occurred in Hera S.p.A.'s shareholding from 50.09% held as at December 31, 2004 to 50.01% as at December 31, 2005.

With effect as at January 1, 2005, the sale of the Amga Energia business segment to Sinergia was finalized, involving a share capital increase for Sinergia from Euro 414,000 to Euro 579,000. Hera S.p.A.'s investments rose from 51% to 59%. As at December 19, 2005, Hera S.p.A. transferred the entire investments in Sinergia to the subsidiary company Hera Comm S.r.L..

On November 9, 2005, Hera S.p.A. acquired 48% of the equity investment in Uniflotte S.r.L., from the shareholder Capital Service S.r.L., taking its shareholding from 51% to 99%.

Companies consolidated by the net equity method ***(in Euro)***

Company name	Registered offices	Share capital	Ownership %		Total	Total holding
			Direct	Indirect		
Acantho S.p.A.	Imola (BO)	15,875,781	50.58%		50.58%	50.58 %
Adriatica Acque S.r.l.	Rimini (Rn)	89,033		22.32%	22.32%	22.32 %
Agea Reti S.r.l.	Ferrara	19,000,000	39.72 %		39.72 %	39.72 %
Agess s.c.ar.l.	Forlì (FC)	79,750	21.44 %		21.44 %	21.44 %
Ambiente 3000 S.r.l.	Bologna	100,000	51.00 %		51.00 %	51.00 %
Aspes Multiservizi S.p.A.	Pesaro	10,963,627	26.87 %		26.87 %	26.87 %
Attivabologna S.r.l. Cons.in liquid.	Bologna	2,558,600		96.40%	96.40%	96.40%
DYNA Green Srl	Milan	30,000		33.00%	33.00%	33.00%
Estense global service	Ferrara	10,000	23.00 %		23.00 %	23.00 %
Gasgas S.r.l. in liquidation	Ferrara	10,000		100.00%	100.00%	100.00%
Meta Rete Gas in liquidation	Modena	99,000	100.00%		100.00%	100.00%
Modena Network S.p.A.	Modena	2,000,000	30.00%		30.00%	30.00%
Oikothen S.c.r.l.	Siracusa	1,101,730		46.10%	46.10%	46.10%
4Italy Energy & Environment S.p.a	Modena	50,000	50.00 %		50.00 %	50.00 %
Refri S.r.l.	Reggio Emilia	2,800,000	20.00%		20.00%	20.00%
SGR Servizi SpA.	Rimini	5,264,000		20.00%	20.00 %	20.00 %
Service Imola S.r.l.	Borgo Tossignano (BO)	10,000	40.00 %		40.00 %	40.00 %
SET spa	Milan	120,000	39.00 %		39.00 %	39.00 %
Sinergie Ambientali S.r.l.	Bologna	100,000	50.00 %		50.00 %	50.00 %
Tecnometano S.r.l. in liquidation	Comacchio (FE)	10,400	100.00%		100.00%	100.00%
Yele S.p.A.	Vallo della Lucania (SA)	103,400	35.00 %		35.00 %	35.00 %

3.04.02 List of significant equity investments as per Article 120.4 of Italian Legislative Decree No.58/98 and Article 126 of the CONSOB resolution

Hera SpA: Investments held directly as at December 31, 2005

ACANTHO S.p.A. Share Capital Euro 15,875,781 fully paid-in. Held by HERA S.p.A. since 2000		
REGISTERED OFFICES: Via Molino Rosso 8 - 40026 IMOLA (BO)		
Shareholder	Holding in €	Holding
HERA S.p.A.	8,030,200	50.58%

AGEA RETI S.r.l. Share Capital € 19,000,000 fully paid-in. Held by HERA S.p.A. since 31 Dec. 2004		
REGISTERED OFFICES: Piazza Municipale 2 - 44100 FERRARA		
Shareholder	Holding in €	Holding
Hera S.p.A.	7,546,800	39.72%

AGESS S.c.a r.l. Share Capital € 79,750 fully paid-in. Held by HERA S.p.A. since 1 Nov. 2002		
REGISTERED OFFICES: P.zza Falcone e Borsellino 23 - 47100 FORLI'		
Shareholder	Holding in €	Holding
HERA S.p.A.	17,100	21.44%

AKRON S.p.A. Share Capital € 1,152,940 fully paid-in. Held by HERA S.p.A. since 1 Nov. 2002		
REGISTERED OFFICES: Via Molino Rosso 8 - 40026 IMOLA (BO)		
Shareholder	Holding in €	Holding
HERA S.p.A.	662,940	57.50%

AMBIENTE 3000 S.r.l. Share Capital € 100,000 fully paid-in. Held by HERA S.p.A. since June 1, 2003		
REGISTERED OFFICES: Viale Carlo Berti Pichat 2/4 - 40127 Bologna (BO)		
Shareholder	Holding in €	Holding
HERA S.p.A.	51,000	51%

AMBIENTE MARE S.p.A. Share Capital € 2,000,000 fully paid-in. Held by HERA S.p.A. since 1 Nov. 2002		
REGISTERED OFFICES: Via del Marchesato 35 - 48023 MARINA DI RAVENNA (RA)		
Shareholder	Holding in €	Holding
HERA S.p.A.	300,000	15%

ARES S.p.A. Consortile Share Capital € 1,125,240. Held by HERA S.p.A. since 1998		
REGISTERED OFFICES: Viale Carlo Berti Pichat 2/4 - 40127 Bologna (BO)		
Shareholder	Holding in €	Holding
HERA S.p.A.	1,125,240	100%

A.S.A. S.p.A. Share Capital € 1,820,000 fully paid-in. Held by HERA S.p.A.since 1994		
REGISTERED OFFICES: Via Saliceto 43/A - 40013 CASTEL MAGGIORE (BO)		
Shareholder	Holding in €	Holding
HERA S.p.A.	928,200	51%

ASPES MULTISERVIZI S.p.A. Share Capital € 10,963,627 fully paid-in. Held by HERA S.p.A. since 2002		
REGISTERED OFFICES: Via dei Canonici 144 - 61100 PESARO		
Shareholder	Holding in €	Holding
HERA S.p.A.	2,946,382	26.87%

AV2 ECOSISTEMA S.p.A. Share Capital € 120,000 fully paid-in. Held by HERA S.p.A. since 31 Dec. 2005		
REGISTERED OFFICES: Corso Europa 43 - 83031 Ariano Irpino (AV)		
Shareholder	Holding in €	Holding
HERA S.p.A.	24,000	20.00%

BIO ENERGY S.r.l. Unipersonale Share Capital € 100,000 fully paid-in. Held by HERA S.p.A. since 31 Dec. 2005		
REGISTERED OFFICES: Via Razzaboni 80 - 41100 MODENA		
Shareholder	Holding in €	Holding
HERA S.p.A.	100,000	100.00%

CALENIA ENERGIA S.p.A. Share Capital € 100,000 fully paid-in. Held by HERA S.p.A. since 23 Sept. 2004		
REGISTERED OFFICES: Via Appia - Area Industriale ex Pozzi, Sparanise (CE)		
Shareholder	Holding in €	Holding
HERA S.p.A.	15,000	15%

CALES S.r.l. Share Capital resolved and subscribed for € 250,000, and paid-in for € 130,750. Held by HERA S.p.A. since 1 Nov. 2002		

REGISTERED OFFICES: Viale della Costituzione - Centro Direzionale Isola A/3 - 80100 NAPLES		
Shareholder	Holding in €	Holding
HERA S.p.A.	125,033.90	50.01%

CALORPIU' MODENA S.c.a r.l. Share Capital € 10,000 fully paid-in. Held by HERA S.p.A. since 31 Dec. 2005		
REGISTERED OFFICES: Via Razzaboni n. 80 - 41100 MODENA		
Shareholder	Holding in €	Holding
HERA S.p.A.	6,000	60.00%

CALORPIU' ITALIA S.c.a r.l. Share Capital € 10,000 fully paid-in. Held by HERA S.p.A. since 31 Dec. 2005		
REGISTERED OFFICES: Via Razzaboni 80 - 41100 MODENA		
Shareholder	Holding in €	Holding
HERA S.p.A.	5,100	51.00%

ECOLOGIA AMBIENTE S.r.l. Share capital € 20,000,000 fully paid-in. Held by HERA S.p.A. since 10/2004		
REGISTERED OFFICES: Via Baiona 182 - 48100 RAVENNA		
Shareholder	Holding in €	Holding
HERA S.p.A.	20,000,000	100%

ECOSFERA S.p.A. Share capital € 1,000,000 fully paid-in. Held by HERA S.p.A. since 31 Dec. 2004		
REGISTERED OFFICES: Via Stefano Trenti 32 - 44100 FERRARA		
Shareholder	Holding in €	Holding
HERA S.p.A.	510,000	51%

ENERGIA ITALIANA S.p.A. Share capital € 26,050,000 fully paid-in. Held by HERA S.p.A. since 2001		
REGISTERED OFFICES: Via Giovanni Battista Pirelli 20 - 20124 MILAN		
Shareholder	Holding in €	Holding
HERA S.p.A.	2,865,500	11%

ESTENSE GLOBAL SERVICE S.c.a r.l. Share capital € 10,000 fully paid-in. Held by HERA S.p.A. since 31 Dec. 2004		
REGISTERED OFFICES: Via M.N. Plattis 5/c - 44100 Ferrara		
Shareholder	Holding in €	Holding
HERA S.p.A.	2,300	23%

FAMULA ON-LINE S.p.A. Share capital € 3,316,427 fully paid-in. Held by HERA S.p.A. since 2001		
REGISTERED OFFICES: Viale Carlo Berti Pichat 2/4 - 40127 Bologna (BO)		
Shareholder	Holding in €	Holding
HERA S.p.A.	1,989,856	60%

FERRARA T.U.A. - Traffico Urbano Autoparking S.p.A. Share capital € 260,000 fully paid-in. Held by HERA S.p.A. since 31 Dec. 2004		
REGISTERED OFFICES: Viale Manini 15 - 44100 FERRARA		
Shareholder	Holding in €	Holding
HERA S.p.A.	52,000	20%

4 ITALY Energy & Environment S.r.l. Share capital € 50,000 fully paid-in. Held by HERA S.p.A. since 31 Dec. 2004		
REGISTERED OFFICES: Via Razzaboni 80 - 41100 MODENA		
Shareholder	Holding in €	Holding
HERA S.p.A.	25,000	50%

FRULLO ENERGIA AMBIENTE S.r.l. Share capital € 17,139,100 fully paid-in. Held by HERA S.p.A. since 2000		
REGISTERED OFFICES: Viale Carlo Berti Pichat 2/4 - 40127 Bologna (BO)		
Shareholder	Holding in €	Holding
HERA S.p.A.	8,740,941	51%

GAL. A S.p.A. Share capital € 300,000 fully paid-in. Held by HERA S.p.A. since 1997		
REGISTERED OFFICES: Viale Carlo Berti Pichat 2/4 - 40127 Bologna (BO)		
Shareholder	Holding in €	Holding
HERA S.p.A.	180,000	60%

HERA IMOLA-FAENZA S.r.l. Share capital € 750,000 fully paid-in. Held by HERA S.p.A. since 21 Oct. 2002		
REGISTERED OFFICES: Via Casalegno 1 - 40026 IMOLA		
Shareholder	Holding in €	Holding
HERA S.p.A.	750,000	100%

HERA BOLOGNA S.r.l. Share capital € 1,250,000 fully paid-in. Held by HERA S.p.A. since 21 Oct. 2002		
REGISTERED OFFICES: Viale Carlo Berti Pichat 2/4 - 40127 Bologna (BO)		
Shareholder	Holding in €	Holding
HERA S.p.A.	1,250,000	100%

HERA COMM S.r.l. Share capital € 88,591,541 fully paid-in. Held by HERA S.p.A. since 2001		
REGISTERED OFFICES: Via Molino Rosso 8 - 40026 IMOLA (BO)		
Shareholder	Holding in €	Holding
HERA S.p.A.	88,591,541	100%

HERA FERRARA S.r.l. Share capital € 810,000 fully paid-in. Held by HERA S.p.A. since 23 Nov. 2004		
REGISTERED OFFICES: Via Diana 40 - 44044 Cassana (FE)		
Shareholder	Holding in €	Holding
HERA S.p.A.	810,000	100%

HERA FORLI'-CESENA S.r.l. Share capital € 650,000 fully paid-in. Held by HERA S.p.A. since 21 Oct. 2002		
REGISTERED OFFICES: Via Spinelli 60 - 47023 CESENA (FC)		
Shareholder	Holding in €	Holding
HERA S.p.A.	650,000	100%

HERA GAS TRE S.p.A. Unipersonale Share capital € 120,000 fully paid-in. Held by HERA S.p.A. since April 27, 2005		
REGISTERED OFFICES: Viale Carlo Berti Pichat 2/4 - 40127 Bologna (BO)		
Shareholder	Holding in €	Holding
HERA S.p.A.	120,000	100%

HERA IMMOBILIARE S.r.l. Share capital € 100,000 fully paid-in. Held by HERA S.p.A. since June 26, 2003		
REGISTERED OFFICES: Viale Carlo Berti Pichat 2/4 - 40127 Bologna (BO)		
Shareholder	Holding in €	Holding
HERA S.p.A.	100,000	100%

HERA LUCE S.r.l. Share capital € 216,600 fully paid-in. Held by HERA S.p.A. since 2000		
REGISTERED OFFICES: Via Due Martiri 2 - 47030 S. MAURO PASCOLI (FC)		
Shareholder	Holding in €	Holding
HERA S.p.A.	150,103.8	69.3%

HERA MODENA S.r.l. Share capital € 10,000 fully paid-in. Held by HERA S.p.A. since 24 Nov. 2005		
REGISTERED OFFICES: Via Razzaboni 80 - 41100 MODENA		
Shareholder	Holding in €	Holding
HERA S.p.A.	10,000	100%

HERA RAVENNA S.r.l. Share capital € 850,000 fully paid-in. Held by HERA S.p.A. since 21 Oct. 2002		
REGISTERED OFFICES: Via Romea Nord 180/182 - 48100 RAVENNA		
Shareholder	Holding in €	Holding
HERA S.p.A.	850,000	100%

HERA RIMINI S.r.l. Share capital € 1,050,000 fully paid-in. Held by HERA S.p.A. since 21/10/2002		
REGISTERED OFFICES: Strada Consolare per San Marino 80 - 47900 RIMINI		
Shareholder	Holding in €	Holding
HERA S.p.A.	1,050,000	100%

HERA TRADING S.r.l. Share capital € 2,600,000 fully paid-in. Held by HERA S.p.A. since 2001		
REGISTERED OFFICES: Via Molino Rosso 8 40026 IMOLA (BO)		
Shareholder	Holding in €	Holding
HERA S.p.A.	2,600,000	100%

HERASOCREM S.p.A. Share capital resolved € 2,218,368 fully paid-in. Held by HERA S.p.A. since July 10, 2003		
REGISTERED OFFICES: Viale Carlo Berti Pichat 2/4 - 40127 Bologna (BO)		
Shareholder	Holding in €	Holding
HERA S.p.A.	1,131,368	51%

INGENIA S.r.l. Share capital € 52,000 fully paid-in. Held by HERA S.p.A. since 1 Nov. 2002		
REGISTERED OFFICES: Via Molino Rosso 8 - 40026 IMOLA (BO)		
Shareholder	Holding in €	Holding
HERA S.p.A.	38,480	74%

ITALCIC S.r.l. Share Capital € 90,000, paid in for € 69,000. Held by HERA S.p.A. since 31 Dec. 2005		
REGISTERED OFFICES: Via Morandi 54 - 41100 MODENA		
Shareholder	Holding in €	Holding
HERA S.p.A.	30,000	33.33%

MEDEA S.p.A. Share Capital € 4,500,000 fully paid-in. Held by HERA S.p.A. since July 1, 2003		
REGISTERED OFFICES: Via Torres 4 - 07100 SASSARI		
Shareholder	Holding in €	Holding
HERA S.p.A.	4,500,000	100%

METAENERGY S.r.l. Unipersonale Share Capital € 13,795,000 fully paid-in. Held by HERA S.p.A. since 31 Dec. 2005		
REGISTERED OFFICES: Via Razzaboni 80 - 41100 MODENA		
Shareholder	Holding in €	Holding
HERA S.p.A.	13,795,000	100.00%

META SERVICE S.r.l. Share Capital € 2,492,000, paid-in up to extent of € 1,850,975. Held by HERA S.p.A. since 31 Dec. 2005		
REGISTERED OFFICES: Via Razzaboni 80 - 41100 MODENA		
Shareholder	Holding in €	Holding
HERA S.p.A.	1,271,000	51.00%

MODENA NETWORK S.p.A. Share Capital € 2,000,000 fully paid-in. Held by HERA S.p.A. since 31 Dec. 2005		
REGISTERED OFFICES: Via Razzaboni 80 - 41100 MODENA		
Shareholder	Holding in €	Holding
HERA S.p.A.	600,000	30.00%

NUOVA GEOVIS S.p.A. Share capital € 2,205,000 fully paid-in. Held by HERA S.p.A. since 2001		
REGISTERED OFFICES: Via Romita 1 - 40019 Sant'Agata Bolognese (BO)		
Shareholder	Holding in €	Holding
HERA S.p.A.	1,124,550	51%

HERA SERVIZI FUNERARI S.r.l. Share capital € 10,000 fully paid-in. Held by HERA S.p.A. since 22 Dec. 2005		
REGISTERED OFFICES: Viale Carlo Berti Pichat 2/4 - 40127 Bologna (BO)		
Shareholder	Holding in €	Holding
HERA S.p.A.	10,000	100%

PENISOLAVERDE S.p.A. Share Capital € 103,200 fully paid-in. Held by HERA S.p.A. since 1 Nov. 2002		
REGISTERED OFFICES: Corso Italia 236 - 80067 SORRENTO (NA)		
Shareholder	Holding in €	Holding
HERA S.p.A.	49,536	48%

RECUPERA S.r.l. Share Capital resolved for € 1,673,290, subscribed and paid-in for € 413,200. Held by HERA S.p.since 1 Nov. 2002		
REGISTERED OFFICES: Via Cesare Diana 40 - 44044 CASSANA (FE)		

Shareholder	Holding in €	Holding
HERA S.p.A.	311,966	75.50%

REFRI S.r.l. Share Capital € 2,800,000 fully paid-in. Held by HERA S.p.A. since 27 Dec. 2005		
REGISTERED OFFICES: Via Meuccio Ruini 10 - 42100 REGGIO EMILIA (RE)		
Shareholder	Holding in €	Holding
HERA S.p.A.	560,000	20.00%

RIO D'ORZO S.r.l. Share Capital € 59,000 fully paid-in. Held by HERA S.p.A. since 1999		
REGISTERED OFFICES: Viale Carlo Berti Pichat 2/4 - 40127 Bologna (BO)		
Shareholder	Holding in €	Holding
HERA S.p.A.	54,870	93%

ROMAGNA COMPOST S.r.l. Share Capital € 310,000, paid-in for € 93,000. Held by HERA S.p.A. since 1 Nov. 2002		
REGISTERED OFFICES: Via Cesare Spinelli 60 - 47023 CESENA (FC)		
Shareholder	Holding in €	Holding
HERA S.p.A.	186,004	60%

SEAS Lavori e Servizi Soc. Cons. a r.l. Share Capital € 51,000 fully paid-in. Held by HERA, by ARES S.p.A. Cons. and by MEDEA S.p.A. since 1998		
REGISTERED OFFICES: Viale Carlo Berti Pichat 2/4 - 40127 Bologna (BO)		
Shareholder	Holding in €	Holding
HERA S.p.A.	3,060	6%
MEDEA S.p.A.	26,520	52%
ARES S.p.A. Consortile	21,420	42%

SERVICE IMOLA S.r.l. Share Capital € 10,000 fully paid-in. Held by HERA S.p.A. since 1 Nov. 2002		
REGISTERED OFFICES: Via Allende 39 - 40021 BORGO TOSSIGNANO (BO)		
Shareholder	Holding in €	Holding
HERA S.p.A.	4,000	40%

SET S.p.A. Share Capital € 120,000 fully paid-in. Held by HERA S.p.A. since 15 Dec. 2004		
REGISTERED OFFICES: Viale Bianca Maria 15 - 20122 MILAN		
Shareholder	Holding in €	Holding

HERA S.p.A.	46,800	39%

SINERGIE AMBIENTALI S.r.l. Share Capital € 100,000 fully paid-in. Held by HERA S.p.A. since July 1, 2003		
REGISTERED OFFICES: Viale Berti Pichat 2/4 - 40127 BOLOGNA		
Shareholder	Holding in €	Holding
HERA S.p.A.	50,000	50%

SOTRIS S.p.A. Share Capital € 2,340,000 fully paid-in. Held by HERA S.p.A. since 1 Nov. 2002		
REGISTERED OFFICES: S.S. 309 Romea Km. 2.6, 272 - 48100 RAVENNA		
Shareholder	Holding in €	Holding
HERA S.p.A.	1,638,000	70%

TS DISTRIBUZIONE GAS S.r.l. Unipersonale Share Capital € 100,000 fully paid-in. Held by HERA S.p.A.		
REGISTERED OFFICES: Via degli Artigiani 8/1 - Monghidoro (BO)		
Shareholder	Holding in €	Holding
HERA S.p.A.	100,000	100.00%

UNIFLOTTE S.r.l. Share capital € 2,254,177 fully paid-in. Held by HERA S.p.A. since 2001		
REGISTERED OFFICES: Viale Masini 42 - 40126 BOLOGNA		
Shareholder	Holding in €	Holding
HERA S.p.A.	2,231,635	99%

VIVISERVIZI S.r.l. Consortium Share Capital € 451,500 paid-in for € 142,725. Held by HERA S.p.A. since 2002		
REGISTERED OFFICES: Viale Carlo Berti Pichat 2/4 - 40127 Bologna (BO)		
Shareholder	Holding in €	Holding
HERA S.p.A.	364,632	80.76%

YELE S.p.A. Share Capital € 103.400 fully paid-in. Held by HERA S.p.A. since 1 Nov. 2002		
REGISTERED OFFICES: Largo Calcinali 1 - 84078 VALLO DELLA LUCANIA (SA)		
Shareholder	Holding in €	Holding
HERA S.p.A.	36,190	35%

Hera SpA: Investments held indirectly as at December 31, 2005

Shareholdings of HERA COMM S.r.l.:

ADRIATICA ACQUE S.r.l. Share capital € 89,033 fully paid-in. Held by HERA S.p.A. since 31 Dec. 2002		
REGISTERED OFFICES: Via Dario Campana 65 - 47900 RIMINI		
Shareholder	Holding in €	Holding
HERA COMM S.r.l.	19,872	22.32%

ERIS Soc. limited liability cons. Share capital € 300,000 – paid-in for € 75,000 - Held by HERA COMM S.r.l. since 28 Nov. 2004		
REGISTERED OFFICES: Via Romea Nord 180/182 - 48100 Ravenna		
Shareholder	Holding in €	Holding
HERA COMM S.r.l.	153,000	51%

HERA ENERGIE BOLOGNA S.r.l. Share capital resolved and subscribed € 500,000 – paid-in for € 384,500 - Held by HERA COMM S.r.l. since June 30, 2005		
REGISTERED OFFICES: Viale Masini 14 - 40126 Bologna		
Shareholder	Holding in €	Holding
HERA COMM S.r.l.	335,000	67%

SGR Servizi S.p.A. Share capital € 5,264,000 fully paid-in - Held by HERA COMM S.r.l. since May 17, 2005		
REGISTERED OFFICES: Via Chiabrera 34/b - 47900 Rimini		
Shareholder	Holding in €	Holding
HERA COMM S.r.l.	1,052,800	20%

SINERGIA S.r.l. Share capital € 579.600 fully paid-in Held by HERA S.p.A. since 1 Nov. 2002		
REGISTERED OFFICES: Via Righi 1 - 47100 FORLI' (FC)		
Shareholder	Holding in €	Holding
HERA COMM S.r.l.	341,964	59.00%

TS ENERGIA S.r.l. Unipersonale Share capital € 10,000 fully paid-in Held by HERA COMM S.r.l.		
REGISTERED OFFICES: Via degli Artigiani 8/1 - Monghidoro (BO)		
Shareholder	Holding in €	Holding

HERA COMM S.r.l.	10,000	100.00%

Shareholdings of Hera Trading S.r.l.:

DYNA GREEN S.r.l. Share capital € 30,000 fully paid-in. Held by Hera Trading S.r.l. since 22 Nov. 2005		
REGISTERED OFFICES: Viale Bianca Maria 24 - 20100 MILANO		
Shareholder	Holding in €	Holding
Hera Trading S.r.l.	10,000	33%

Shareholdings of METAENERGY S.r.l. Unipersonale:

SO.SEL S.p.A. Share capital € 240,240 fully paid-in. Held by METAENERGY S.r.l. since 16 Dec. 2004		
REGISTERED OFFICES: Via Bellinzona 37/F - 41100 MODENA		
Shareholder	Holding in €	Holding
METAENERGY S.r.l.	48,048.00	20.00%

Shareholdings of ARES S.p.A. Consortium:

OIKOTHEN S.c.a r.l. Share capital € 1,101,730 fully paid-in. Held by ARES S.p.A. Consortium since 2001		
REGISTERED OFFICES: Via Augusta 17 - 96100 SIRACUSA		
Shareholder	Holding in €	Holding
ARES S.p.A. Consortile	507,892	46.10%

Hera SpA: Direct and indirect equity investments in liquidation as at December 31, 2005

AGEA ONE S.r.l. Share capital € 2,300,000 fully paid-in. Held by HERA S.p.A. since 31 Dec. 2004		
REGISTERED OFFICES: Via Cesare Diana 40 - 44044 CASSANA (FE)		
In liquidation since April 19, 2005		
Shareholder	Holding in €	Holding
Hera S.p.A.	**2,300,000**	**100%**

ENERGICA S.p.A. Share capital € 200,000 fully paid-in. Held by HERA S.p.A. since April 24, 2003		
REGISTERED OFFICES: Via Convertite 12 - 48018 Faenza (RA)		
In liquidation since May 19, 2005		
Shareholder	Holding in €	Holding
HERA S.p.A.	**100,000**	**50%**

HERA clion S.r.l. Share capital € 200,000 fully paid-in. Held by Hera since 30 Sept. 2003		
REGISTERED OFFICES: Via del Rione Sirignano 7 - 80121 Napoli		
In liquidation since 3 Oct. 2005		
Shareholder	Holding in €	Holding
HERA S.p.A.	**200,000**	**100%**

IDEAMETROPOLI Centro Global Service S.r.l. - Share capital € 21,045 fully paid-in - Held by HERA S.p.A. since 1988		
REGISTERED OFFICES: Viale Carlo Berti Pichat 2/5 - 40127 Bologna (BO)		
In liquidation since May 1, 2003		
Shareholder	Holding in €	Holding
HERA S.p.A.	**21,045**	**100.000%**

META RETE GAS S.r.l. Unipersonale Share capital € 99,000 fully paid-in. Held by HERA S.p.A. since 31 Dec. 2005		
REGISTERED OFFICES: Via Razzaboni 80 - 41100 MODENA		
In liquidation since June 24, 2005		
Shareholder	Holding in €	Holding
HERA S.p.A.	**99,000**	**100%**

SBI S.r.l. Share capital € 100,000 fully paid-in. Held by HERA S.p.A. since2002		
REGISTERED OFFICES: Viale Carlo Berti Pichat 2/4 - 40127 Bologna (BO)		
In liquidation since 24 Jan. 2005		

Shareholder	Holding in €	Holding
HERA S.p.A.	**51,000**	**51%**
Brochier S.r.l.	49,000	49%

S.E.I.A. S.p.A. Share capital € 175,230 fully paid-in. Held by HERA S.p.A. since 31 Dec. 2004		
REGISTERED OFFICES: Corso Giovecca 81 - 44100 FERRARA		
In liquidation since April 20, 2000		
Shareholder	Holding in €	Holding
HERA S.p.A.	**60,941.10**	**34.78%**

TECNOMETANO S.r.l. Unipersonale Share capital € 10,400 fully paid-in. Held by HERA S.p.A. since July 14, 2005		
REGISTERED OFFICES: Via Cavour 46 - 44022 Comacchio (FE)		
In liquidation since 8 Nov. 2005		
Shareholder	Holding in €	Holding
HERA S.p.A.	**10,400**	**100%**

Shareholdings of HERA Comm S.r.l.:

ATTIVABOLOGNA S.r.l. Consortile Share capital € 2,558,600 paid-in for € 808,725. Held by HERA COMM since 29 Sept. 2003		
REGISTERED OFFICES: Viale Carlo Berti Pichat 2/4 - 40127 Bologna (BO)		
In liquidation since July 19, 2005		
Shareholder	Holding in €	Holding
HERA COMM S.r.l.	2,466,464	96.40%

ARGILEGAS S.r.l. Unipersonale Share capital € 30,000 fully paid-in. Held by HERA COMM since July 6, 2005		
REGISTERED OFFICES: Via Nazario Sauro 2 - 40121 Bologna (BO)		
In liquidation since 3 Nov. 2005		
Shareholder	Holding in €	Holding
HERA COMM S.r.l.	30,000	100.00%

Gasgas S.r.l. Unipersonale Share capital € 10,000 fully paid-in. Held by HERA COMM since July 14, 2005		
REGISTERED OFFICES: Via Cavour 46 - 44022 Comacchio (FE)		
In liquidation since 3 Nov. 2005		
Shareholder	Holding in €	Holding
HERA COMM S.r.l.	10,000	100%

3.05 Highlights of the subsidiary and associated companies

Subsidiaries	Amounts due to shareholders	Fixed assets	Current assets	Share capital	Reserves	Profit+ Loss -	Provisions	Employee leaving indemnity	Payables	Value of production	Production costs	Financial income and charges	Value adjustments to financial assets	Income and charges	Taxation for the year	Net profit
Agea ore S.r.l. IAS	0	0	8,999	2,300	1,325	352	457	0	4,565	29,860	-28,503	156	0	0	-1,161	352
Akron S.p.A. IAS	0	16,336	19,191	1,153	4,095	1,355	1,075	311	27,537	27,748	-25,100	-273	0	0	-1,020	1,355
Ares S.p.A. Consortile IAS	0	1,817	537	1,125	-206	-167	0	0	1,601	8	-137	0	-38	0	0	-167
ASA S.P.A	0	9,978	1,721	1,820	548	318	6,867	117	2,029	4,950	-4,362	6	0	-8	-256	318
Bio Energy S.r.l.	0	5	1,043	100	500	-442	0	0	889	805	-1,463	-2	0	0	218	-442
Cales S.r.l. IAS	89	19	255	250	-2	-80	0	3	198	111	-201	0	0	10	0	-80
Ecologia Ambiente S.r.l. IAS	0	66,846	12,935	20,000	29,749	4,389	1,051	717	23,875	27,243	-20,014	-616	0	0	-2,225	4,389
Ecosfera S.p.A. IAS	0	1,624	1,369	1,000	399	246	8	43	1,314	3,172	-2,876	-19	0	0	-31	246
Eris S.c.r.l. IAS	113	30	3,222	300	-5	69	4	0	2,997	3,203	-3,089	5	0	0	-50	69
Famula Online S.p.A. IAS	0	15,862	17,062	3,316	6,898	330	45	956	21,379	31,812	-31,255	12	0	0	-239	330
Frullo Energia Ambiente S.r.l. IAS	0	124,298	35,112	17,139	-1,446	9,368	763	950	132,636	40,600	-20,513	-4,781	0	0	-5,938	9,368
Gal.A. S.p.A. IAS	0	11,244	7,074	300	60	52	1,005	0	16,852	2,676	-2,182	-404	0	-12	-25	52
Hera Bologna S.r.l. IAS	0	59,903	96,483	1,250	1,771	19,462	1,405	20,053	112,446	308,207	-272,505	-444	0	0	-15,796	19,462
Hera Comm S.r.l. IAS	0	31,762	633,276	88,592	391	-13,006	105	1,296	587,660	835,639	-855,118	1,207	-793	0	6,060	-13,006
Hera Energie Bologna Srl	116	166	1,279	500	0	-9	0	0	1,069	770	-784	2	0	0	4	-9
Hera Ferrara S.r.l. IAS	0	7,006	40,543	810	-5	4,643	219	10,122	31,760	100,697	-91,820	-198	0	0	-4,036	4,643
Hera Forlì-Cesena S.r.l. IAS	0	30,478	73,964	650	874	579	1,370	5,570	95,400	128,673	-126,308	-91	0	0	-1,696	579
HERA GAS TRE Spa	0	0	119	120	-2	0	0	0	1	0	-1	1	0	0	0	0
Hera Imola-Faenza S.r.l. IAS	0	18,295	90,961	750	171	5,983	287	6,135	95,310	107,916	-96,993	-142	0	0	-4,798	5,983
Hera Luce S.r.l. IAS	0	4,392	14,554	217	379	2,348	260	387	15,355	30,425	-26,502	23	0	0	-1,598	2,348
Hera Ravenna S.r.l. IAS	0	7,320	62,019	850	997	7,912	657	7,440	51,484	134,886	-120,384	-191	0	0	-6,397	7,912
Hera Rimini S.r.l. IAS	0	6,457	72,909	1,050	1,422	539	943	7,847	67,565	132,474	-129,496	-267	0	3	-2,173	539
Hera trading S.r.l. IAS	0	3,081	178,577	2,600	-382	-99	758	143	178,638	297,527	-298,954	1,280	0	0	47	-99
Heasocrem S.p.A. IAS	0	550	2,121	2,218	95	85	63	92	117	713	-600	33	0	2	-62	85
Ingenia S.r.l. IAS	0	53	615	52	68	20	22	6	500	1,092	-1,051	1	0	0	-22	20
Medea S.p.A. IAS	0	13,987	6,606	4,500	-1,223	-973	1,157	80	17,051	1,649	-2,832	-214	0	0	425	-973
Metaenergy S.r.l.	0	15,283	125,069	13,795	-185	381	189	1,545	124,626	266,281	-266,106	651	0	-1	-443	381
Metasevice S.r.l.	641	1,495	4,886	2,492	484	86	209	477	3,275	7,015	-6,787	13	0	-8	-147	86
Nuova Geovis S.p.A. IAS	0	15,536	7,133	2,205	969	347	5,903	367	12,869	10,403	-9,390	-352	0	0	-314	347
Recupera S.r.l. IAS	0	4,612	1,853	413	300	188	148	27	5,388	6,898	-6,535	-42	0	0	-133	188
Romagna Compost S.r.l. IAS	217	64	509	310	178	63	0	0	239	618	-514	1	0	-1	-41	63
Seas Lavori e Servizi s.c.a r.l. IAS	0	0	3,959	51	-2	-12	0	0	3,921	7,376	-7,379	0	0	0	-8	-12
Sinergia S.r.l. IAS	0	4,763	4,126	580	2,804	654	166	86	4,599	8,177	-7,124	9	0	0	-408	654
Sotis S.p.A. IAS	0	9,192	9,931	2,340	3,285	1,505	6,097	52	5,845	7,731	-5,086	-199	0	4	-941	1,505
Ts Distribuzione Gas S.r.l	0	1,187	76	100	1,010	-20	0	32	128	78	-98	0	0	0	0	-20
TS Energia S.r.l.	0	2	562	10	15	15	0	0	526	951	-926	2	0	0	-12	15
Uniflotte S.r.l. IAS	0	13,716	13,294	2,254	1,006	1,046	1,321	2,284	19,081	21,897	-19,301	-498	0	0	-1,051	1,046
Viviservizi S.r.l. Consortile	309	0	1,664	452	-82	-2	0	0	1,605	2,192	-2,199	5	0	0	0	-2

Summary of the highlights from the approved financial statements of the subsidiary and associated companies (ARTICLE 2429, last section of the Italian Civil Code)

Amounts in€/000s

Associated companies	Amounts due to shareholders	Fixed assets	Current assets	Share capital	Reserves	Profit+ Loss -	Provisions	Employee leaving indemnity	Payables	Value of production	Production costs	Financial income and charges	Value adjustments to financial assets	Income and charges	Taxation for the year	Net profit
* Acantho S.p.a	0	21,847	26,023	14,663	3	-3,587	149	262	37,353	16,523	-19,241	-766	0	-78	-25	-3,587
Adriatica Acqua S.r.l	0	87	482	89	0	-75	0	15	461	349	-399	22	0	0	-4	-75
Agea reti S.r.L. IAS	0	26,829	40	19,000	484	1	0	0	7,385	1,950	-1,472	-441	0	0	-36	1
Agess S.c.a.r.l. IAS	0	62	182	80	-36	11	0	26	163	423	-419	-1	0	14	-7	11
Ambiente 3000 S.r.l. IAS	0	199	909	100	19	-13	0	0	630	563	-604	7	0	0	-21	-13
* Aspes Multiservizi S.p.a	0	20,853	33,878	10,964	568	1,566	2,778	6,422	32,019	54,380	-49,689	223	-711	-37	-2,600	1,566
* Attivabologna Sl (in Liquidation)	1,750	79	3,896	2,559	-241	-168	0	61	3,475	1,648	-1,812	12	0	-9	-7	-168
DYNA Green Srl	0	3	201	30	194	-22	0	0	3	0	-22	0	0	0	0	-22
Estense global service Cons.a r.l. IAS	0	220	2,843	10	0	0	0	0	3,071	6,318	-6,317	3	0	0	-3	0
Gasgas Srl	0	1	270	10	78	17	16	0	145	911	-893	0	0	0	-332	17
Meta Rete Gas	0	0	383	99	214	-109	0	0	179	1	-47	7	0	109	54	-109
Modena Network S.p.a	0	6,748	9,408	2,000	0	-183	0	0	15,104	12,284	-12,458	-9	0	0	0	-183
Oikothen S.c.r.l. IAS	0	3,169	607	1,102	-47	-60	0	0	2,782	0	-77	0	0	-5	-21	-60
4Italy Energy & Environment S.p.a.	0	4,401	611	50	11	-4	1	0	4,912	290	-325	-16	0	49	1	-4
* Refri S.r.l.	0	2,921	1,037	2,800	275	-871	0	7	1,745	974	-1,044	6	-845	41	-2	-871
Service imola S.r.l. IAS	0	4	218	10	6	29	0	4	174	413	-342	-3	0	0	-31	29
SET S.p.A. IAS	0	187,745	23,432	120	39,889	-568	175	12	171,591	3,594	-1,024	3,215	0	0	-77	-568
SGR Servizi Spa IAS	0	3,092	51,952	5,264	738	4,968	649	500	43,271	103,219	-95,487	439	0	-9	-3,194	4,968
Sinergie Ambientali S.r.l. IAS	0	0	67	100	-29	-5	0	0	12	0	-7	2	0	0	0	-5
Yele S.p.A. IAS	0	448	3,235	103	444	-43	0	140	3,082	4,722	-4,696	-7	0	-4	-66	-43
Tecnometano Sl	0	0	594	10	617	-36	0	0	15	110	-146	0	0	3	0	-36

* The companies marked with an asterisk show the balances from the last set of approved financial statements (December 31, 2004)

3.06 Consolidated cash flow statement

	31/12/2005 €/000s		31/12/2004 €/000s		
Operating activities					
Cash flow					
Net profit pertaining to Group and minority shareholders	87,663				
Depreciation and writedowns of tangible fixed assets	91,094				
Amortisation and writedowns of intangible assets	29,436				
Goodwill	-121,822				
Total cash flow	**86,371**		**118,504**		
Changes in prepaid and deferred taxation	35,183		4,583		
Employee leaving indemnities and other benefits:					
Provisions/ (uses)	18,268		13,621		
Provisions for risks and charges:					
Provisions/ (uses)	40,717		21,406		
Other non-current liabilities:					
Provisions/ (uses)	14,209		48,914		
Working capital					
Change in trade receivables	-298,205				
Change in inventories	-255				
Change in other current assets	-100,605				
Change in trade payables	237,128				
Change in tax liabilities	-54,125				
Change in other current liabilities	5,010				
Change in working capital	**-211,051**		**-10,219**		
Liquidity generated by operations		**-16,303**		**196,809**	a)
Investment activities					
Disposal/(investment) in tangible fixed assets, net of net investments/disposals	- 707,174				
Disposal/(investment) in intangible assets, net of net investments/disposals	- 31,335				
Investments in equity investments net of disposals	-13,446				
Change in non-current receivables	-35,538				
Other non-current assets	10,005				
Liquidity generated/(absorbed) by investment activities		**- 777,488**		**- 366,893**	b)
Financing activities					
Medium/long-term loans	45,455				
Change in shareholders' equity accounts	384,283				
Changes in securities					
Change in current portions of medium/long-term loans	373,796				
Dividends paid	- 52,641				
Change in financial leasing payables	20,913				
Change in financial instruments - derivatives	15,811				
Liquidity generated/(absorbed) by financing activities		**787,617**		**276,630**	c)
		- 6,174	**(a+b+c)**	**106,546**	**(a+b+c**

Change in net financial position		
Opening short-term financial position	209,199	102,653
Closing short-term financial position	203,025	209,199
	-6,174	**106,546**

3.07 Report of the Board of Statutory Auditors

The translation into the english language of the report of the Board of Statutory Auditors will be available as soon as possible

3.08 Independent Auditors' Report

The translation into the english language of the Deloitte's Opinion will be available as soon as possible

3.09 APPENDIX: CHANGEOVER TO THE INTERNATIONAL ACCOUNTING STANDARDS (IFRS)

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Introduction

The Hera Group adopted the international accounting standards, the International Financial Reporting Standards, as from the 2005 accounting period, with date of changeover to the IFRS as of January 1, 2004. The last set of consolidated financial statements drawn up in accordance with Italian accounting principles refer to the accounting period ended December 31, 2004.

As required by IFRS 1 and by Article 81 of the Issuers' Regulation No. 11971/1999 adopted by the Consob by means of Resolution No. 14990 dated April 14, 2005, this Appendix contains the statement of reconciliation between the balances reported previously in accordance with the Italian accounting principles and those reclassified in pursuance of the IFRS, accompanied by the related notes commenting on the adjustments.

These statements have been drawn up solely for the purposes of the changeover project for the drawing up of the first set of complete consolidated financial statements pursuant to the IFRS approved by the European Commission, and do not include the comparative figures and the necessary explanatory notes which would have been required for the complete view of the equity-financial standing and consolidated economic result of the Hera Group in compliance with the IFRS standards.

Shareholders are also informed that they have been prepared in accordance with the International Financial Reporting Standards (IFRS) currently in force, inclusive of the IFRS recently adopted by the International Accounting Standards Board (IASB), the International Accounting Standards (IAS) and the interpretations of the International Financial Reporting Interpretations Committee (IFRIC) and of the Standing Interpretations Committee (SIC). These standards are those which it is assumed will be in force as at December 31, 2005. However, these standards may not coincide with those in force as at December 31, 2005 as a result of both the new stances of the European Commission regarding their approval, and the issue of new standards or interpretations by the competent authorities and, therefore, the figures presented could undergo changes for the purposes of their use as comparative data of the first set of complete consolidated financial statements drawn up in compliance with the IFRS.

The most significant accounting standards and policies used for the preparation of the reconciliation statements are those described in the explanatory notes accompanying the consolidated statements as at June 30, 2005.

For the adoption of the international accounting standards, the Group has applied the matters laid down by IFRS 1 – Initial adoption of the International Financial Reporting Standards, availing itself of the following exemptions:

- Business combinations: the Group has not applied IFRS 3 retrospectively to the business combination transactions which took place before the date of changeover to the IFRS;
- Valuation of real estate property, plant and machinery at revalued cost as the replacement of the cost for certain categories of assets chosen selectively;

- Employee benefits: the Group has decided to record all the cumulative actuarial gains and losses existing as of January 1, 2004, despite having chosen to use the corridor method for the subsequent actuarial gains and losses;
- Classification and valuation of the financial instruments: IFRS 1 makes it possible to apply IAS 39 as from the financial statements for the periods starting as at January 1, 2005. The Group has therefore decided to avail of these exemptions, applying IAS 39 for the valuation and statement of the derivative instruments.

Furthermore, in compliance with the matters established by CONSOB Communication DEM 5025723 dated April 15, 2005, this statement of reconciliation and the related notes have been audited by Deloitte & Touche SpA and the related auditors' report will be made available shortly after the approval of this interim report by Hera S.p.A.'s Board of Directors.

IAS/IFRS consolidated balance sheet as at January 1, 2004 and December 31, 2004
IAS/IFRS consolidated income statement as at December 31, 2004

The balance sheets as at January 1, 2004 and December 31, 2004 and the income statement for 2004 are presented below, indicating:

- the balances in accordance with the Italian accounting principles reclassified in accordance with the IAS/IFRS formats;
- the adjustment for adaptation to the IAS/IFRS standards.

The balances are expressed in millions of Euro.

BALANCE SHEET AS AT JANUARY 1, 2004

	Note	Italian accounting standards IAS reclassified	IAS/IFRS adjustments	IAS/IFRS
ASSETS				
Non-current assets				
Tangible fixed assets	1	954	41	995
Intang. Assets and consolidation diff.	2	262	(17)	245
Goodwill	3	92	-	92
Equity investments and securities		111	-	111
Financial assets		6	-	6
Deferred tax asset	4	15	15	30
Other non-current assets		19	-	19
		1,459	**39**	**1,498**
Current assets				
Inventories		29	-	29
Trade receivables		553	-	553
Contract work in progress		12	-	12
Financial assets		10	-	10
Other current assets		52	-	52
Cash and cash equivalents		93	-	93
		748	-	**748**
TOTAL ASSETS		**2,207**	**39**	**2,246**

	Note	Italian accounting standards IAS reclassified	IAS/IFRS adjustments	IAS/IFRS
SHAREHOLDERS' EQUITY & Liabilities				
Share capital and reserves				
Share Capital		793	-	793
Reserves		28	42	70
Net profit (loss) for the period		49	-	49
Group shareholders' equity				
Minority interest share		24	2	26
Total shareholders' equity		**895**	**44**	**939**
Medium/long term liabilities				
Loans - payable beyond one year		342	-	342
Employee leaving indemnity and other benefits	5	68	1	69
Provisions for risk and charges	6	105	(47)	58
Deferred tax liabilities	7	2	41	43
Lease finance payables - payable beyond one year		10	-	10
Other non-current liabilities		42	-	42
Current liabilities				
Banks and financing - payable within one year		199	-	199
Payables for contract work in progress			-	
Trade payables		384	-	384
Taxes payable		67	-	67
Other current liabilities		91	-	91
Financial instruments - derivatives		-	-	-
Total liabilities		**1,312**	**(5)**	**1,307**
TOTAL SHAREHOLDERS' EQUITY & LIABILITIES		**2,207**	**39**	**2,246**

BALANCE SHEET AS AT DECEMBER 31, 2004

	Note	Italian accounting standards IAS reclassified	IAS/IFRS adjustments	IAS/IFRS
ASSETS				
Non-current assets				
Tangible fixed assets	1	1,259	40	1,299
Intangible assets and consolidation difference	2	235	(20)	215
Goodwill	3	118	29	147
Equity investments and securities		78	-	78
Financial assets		19	-	19
Deferred tax asset	4	20	15	35
Other non-current assets		44	-	44
		1,773	**64**	**1,837**
Current assets				
Inventories		42	-	42
Trade receivables		597	-	597
Contract work in progress		15	-	15
Financial assets		37	-	37
Other current assets		45	-	45
Cash and cash equivalents		172	-	172
		908	**-**	**908**
TOTAL ASSETS		**2,681**	**64**	**2,745**

	Note	Italian accounting standards IAS reclassified	IAS/IFRS adjustments	IAS/IFRS
SHAREHOLDERS' EQUITY & LIABILITIES				
Share capital and reserves				
Share Capital		840	-	840
Reserves		56	59	115
Net profit (loss) for the period		57	24	81
Group shareholders' equity		953	83	1,036
Minority interest share		26	2	28
Total shareholders' equity		**979**	**85**	**1,064**
Medium/long term liabilities				
Banks and financing - payable beyond one year		489		489
Employee leaving indemnity and other benefits	5	85	(2)	83
Provisions for risk and charges	6	146	(67)	79
Deferred tax liabilities	7	5	48	53
Payables for finance leases		29	-	29
Other non-current liabilities		92	(1)	91
Current liabilities				
Banks and financing - payable within one year		272	-	272
Trade payables		433	-	433
Taxes payable		87	-	87
Other current liabilities		66	-	66
Total liabilities		**1,702**	**(21)**	**1,681**
TOTAL SHAREHOLDERS' EQUITY & LIABILITIES		**2,681**	**64**	**2,745**

INCOME STATEMENT AS AT DECEMBER 31, 2004

	Note	IAS reclassified Italian accounting principles	IAS/IFRS Adjustments	IAS/IFRS
Operating assets				
Revenues		1,493	-	1,493
Change in inventories of finished products and work in progress		9	-	9
Other operating income		27	-	27
Use of raw materials and consumables (net of changes in inventories of raw materials and stock)	8	(620)	(2)	(622)
Services	9	(411)	(6)	(417)
Personnel costs	10	(220)	4	(216)
Amortisation, depreciation and provisions	11	(156)	41	(115)
Other operating costs		(92)	-	(92)
Capitalized costs		111	-	111
EBIT		**141**	**36**	**177**
Portion of profit (loss) pertaining to associated companies		(3)	-	(3)
Financial income		6	-	6
Financial charges	12	(27)	(6)	(33)
Pre-tax profit		**117**	**30**	**148**
Taxes for the period	13	(55)	(6)	(61)
Net profit for the year		**62**	**24**	**86**
Attributable to:				
Shareholders of Parent Company		(56.8)	(24.2)	(81)
Minority shareholders		(5.2)	(0.2)	(5.4)

COMMENTARY ON THE MAIN IAS ADJUSTMENTS MADE TO THE BALANCE SHEET ITEMS AS AT JANUARY 1, AND DECEMBER 31, 2004

The main adjustments are presented below, together with the related notes.

Balance sheet items – Assets

1) **Tangible fixed assets** (+ Euro 40.5 million as at January 1, 2004 and + Euro 39.8 million as at December 31, 2004); the adjustments refer to the following:

- The Group has adopted the criteria of fair value as a replacement for cost *(*fair value as deemed cost*)* for the tangible fixed assets, selectively applying it to certain categories of assets; the additional value emerging has been credited directly to reserves. The adoption of the fair value took place on the basis of an estimate made by an independent expert which made it possible to identify the individual elements of plant and machinery which have a significant value and a different useful life, in accordance with the approach by components as anticipated by IAS 16.
  The overall net effect deriving from the application of these standards involves an increase in tangible fixed assets equating to around Euro 50.8 million as at January 1, 2004 and Euro 50.6 million as at December 31, 2004.

- the IFRS require that the charges for restoring waste storage sites, to be incurred on conclusion of the activities, are estimated and recorded at their current value among the tangible fixed assets and subject to depreciation. Correspondingly, these charges must be stated under the provisions for risks and charges, annually adjusting the current value for the financial element. Steps were therefore taken to re-determine the book values since the Italian accounting principles do not envisage either the discounting back of the provisions or the capitalization of the charge anticipated. The effect of this adjustment on the item tangible fixed assets as at January 1, 2004 and December 31, 2004 came, respectively, to approximately Euro 6.1 million and Euro 4.7 million;

- the IFRS require the performance of an *impairment test* which involves a review of the book value of the fixed assets in order to determine if there is any indication that these assets have undergone reductions in value. If such indications exist, the recoverable amount of these assets is estimated so as to calculate the amount of the writedown. When it is not possible to estimate the recoverable value of the assets individually, the Group makes an estimate of the recoverable value of the unit generating the financial flows to which the asset belongs. Following the performance of this test, the Group made an adjustment to the value of the tangible fixed assets for the TLC sector equating, as at January 1, 2004, to Euro 16.4 million and Euro 15.5 million as at December 31, 2004. The rate employed for discounting back the flows generated by the TLC sector was 6.2%.

2) **Intangible fixed assets and consolidation differences** (- Euro 16.9 million as at January 1, 2004 and Euro 19.2 million as at December 31, 2004); the adjustments refer to:

- start-up and expansion costs. In accordance with the Italian accounting principles, the costs for extraordinary corporate transactions and the formation and share capital increase costs can be charged to the balance sheet assets, while the IFRS envisage their booking to the income statement. The application of the standard has led to the reversal of start-up and expansion costs totalling Euro 12.6 million as at January 1, 2004 and Euro 14.2 million as at December 31, 2004.

- research, development and advertising costs and other deferred charges. In accordance with the Italian accounting principles, deferred charges under specific circumstances can be capitalized. The application of the standard led to the reversal of research, development and advertising costs and other deferred charges totalling around Euro 4.3 million as at January 1, 2004 and around Euro 7.5 million as at December 31, 2004;

- consolidation differences. According to the IAS/IFRS standards, these items are not longer amortised systematically but subject to valuation for the purposes of identifying any losses in value. The application of the standard led to the reinstatement of the item for around Euro 2.5 million.

3) **Goodwill –** According to the IAS/IFRS standards, these items are not longer amortised systematically but subject to valuation for the purposes of identifying any losses in value.

The application of the standard led to the reinstatement of the item "goodwill" for a total of around Euro 10.2 million, corresponding to the portion of amortisation for 2004.

Business combinations - IFRS 3 is applicable to the business combinations whose purchase contract date took place after March 31, 2004. The Company has applied this standard for the acquisition of AGEA SpA.

IFRS 3 envisages that the business aggregations be recorded in accordance with the acquisition method. The acquisition method is determined by the sum total of the current values, as of the exchange date, of the assets provided, the liabilities incurred or undertaken, and the financial instruments issued by the Group in exchange for control over the company acquired, plus the costs directly attributable to the combination with the exception of the non-current assets which are classified as held for sale in accordance with IFRS 5, which are recorded and valued at current values less sales costs. Specifically, with regards to the current value of Hera shares issued following the share capital increase serving the merger by incorporation of Agea s.p.a., this was determined as at July 27, 2004 and identified, in essence, as the date as from which the Group took effective control over Agea s.p.a.

The goodwill deriving from the acquisition is recorded as an asset and initially valued at cost, represented by the additional value of the acquisition cost when compared with the Group portion of the current values of the identifiable assets, liabilities and potential

liabilities recorded. If, after the re-calculation of these values, the Group portion of the current values of the identifiable assets, liabilities and potential liabilities exceeds the acquisition cost, the surplus is recorded via the income statement.

Availing itself of the faculty envisaged by IRFS 1, the Group has not retroactively applied IFRS 3 to the business combination transactions which took place prior to the date of changeover to the IAS/IFRS standards; they have therefore been recorded at the same values determined on the basis of the previous accounting principles.

The application of IFRS 3 to the merger with Agea S.p.A. led to the registration of additional goodwill by around Euro 18.7 million.

4) **Deferred tax assets** (+ Euro 14.9 million as at January 1, 2004 and + Euro 14.7 million as at December 31, 2004); these reflect the matching balance sheet asset balance of the tax effects on adjustments to the shareholders' equity.

5) **Employee benefits –** In accordance with the Italian accounting principles, the benefits subsequent to the employment relationship are recorded on an accruals basis during the employment period, in compliance with legislation and applicable labour agreements. According to the IFRS, the benefits subsequent to the employment relationship (e.g. pensions, life assurance and healthcare, etc) are defined on the basis of plans, even if not yet formalized, which in relation to their features are classified as "defined contribution" plans and "defined benefit" plans. In the defined contribution plans, the company's obligation is limited to the payments of the contributions to the State or to a trust or a legally separate entity. The defined benefit plans are social security, insurance and welfare plans which anticipate the obligation, implied or otherwise, for the company to grant the unformalized benefits in favour of former employees. Considering the uncertainties relating to the moment that it will be disbursed, the employee leaving indemnity (TFR) is classified as a defined benefit plan. The related charges, determined on the basis of actuarial hypothesis, are provided for on an accruals basis in relation to the employment period necessary for obtaining the benefits. The amendment of the principle led to a reduction in the employee leaving indemnity provision of around Euro 5.2 million as at January 1, 2004 and around Euro 7.7 million as at December 31, 2004, as well as the recording of a "gas discount" and "Premungas Fund" provision totalling Euro 5.9 million as at January 1, 2004 and Euro 5.8 million as at December 31, 2004. The rate adopted in the discounting back procedure came on average to 4.7%.

6) **Discounting back of provisions for risks and charges** – in accordance with the matters envisaged by IAS 37, if the liability refers to outlays deferred over time, the liability itself is subject to discounting back to a rate, gross of taxation, capable of reflecting the current market values of the actual value of money and the specific risks associated with the liability. The provision increases in each accounting period in order to reflect the passage of time determining the recording of financial charges on an accruals basis. Within the HERA Group, this standard has been applied to the provision for the restoration of third party

assets and the landfill closure and post-closure provision. The application of the standard led to the reversal of said provision for a total of Euro 47 million as at January 1, 2004 and a total of Euro 67 million as at December 31, 2004.

7) **Deferred tax liabilities** (+ Euro 41.3 million as at January, 1 2004 and + Euro 48.3 million as at December 31, 2004); these reflect the matching balance sheet liability balance of the tax effects on adjustments to the shareholders' equity.

COMMENTARY ON THE MAIN IAS ADJUSTMENTS MADE TO THE INCOME STATEMENT ITEMS AS AT DECEMBER 31, 2004

8) **Costs for purchases of raw materials –** the adjustment amounting to approximately Euro 2.2 million represents the surplus of the use of the landfill post-closure provisions with respect to the matters anticipated by the appraisals which, on the basis of the application of IAS 3, have been discounted back. The analysis of these "over-uses" has not however changed the estimate of the future costs discounted back.

9) **Costs for services (**+ Euro 5.9 million) – the adjustment mainly concerns the recording in the income statement of the costs capitalized under the item "intangible fixed assets" during 2004 in relation to which the application of the IFRS anticipates direct booking to the income statement.

10) **Personnel costs** (- Euro 4.2 million) – the adjustments concern the different accounting approach (financial-actuarial) of the benefits due to the employees (leaving indemnities, supplementary in-house welfare and gas discount).

11) Amortisation, depreciation and provisions.

The main adjustments are summarized in the following table:

Euro millions	
Amortisation of goodwill	(10.2)
Amortisation of intangible fixed assets	(9.2)
Depreciation of tangible fixed assets (IAS 16, IAS 37)	1.1
Total	18.3

The afore-mentioned adjustments reflect:

- a decrease, for Euro 10.2 million, attributable to the reversal of the amortisation of goodwill;

- a decrease, for Euro 9.2 million, attributable to the reversal of the amortisation of intangible fixed assets no longer envisaged by the IAS/IFRS;
- an increase, for Euro 1,1 million, due to the effect of the definition for certain categories of tangible fixed assets of the fair value as a replacement for cost and of the consequent definition (and recalculation) of the significant components for the asset categories concerned, as a result of the reversal of the depreciation on the assets written down as per IAS 36 and as a result of the amortisation of reclamation costs for the site on which the tangible fixed assets exist since it complies with the provisions of IAS 37.

The adjustments to the item "provisions" totalling + Euro 22.3 million concerns the reversal of the provisions to the landfill post-closure provisions amounting to Euro 7.4 million and to the provision for the restoration of third party assets totalling Euro 22.6 million, as well as the recording of the provision to the discounted back provision for the restoration of third party assets amounting to Euro 7.7 million.

12) Financial charges (+ Euro 6 million) – the adjustment mainly comprises:

- Euro 2.4 million as a result of the discounting back of the landfill post-closure provisions;
- Euro 1.7 million as a result of the discounting back of the employee benefits;
- Euro 1.9 million as a result of the discounting back of the provision for the recovery of third party assets.

13) Taxation (+ Euro 6 million) – this amount reflects the tax effects of the income statement adjustments.

14) Statement of reconciliation of the shareholders' equity.

By way of supplementing the statements of reconciliation of the balance sheet and income statement shown above, the statement of reconciliation of the shareholders' equity as at January 1, 2004 and December 31, 2004 and the net profit for 2004 is presented as follows.

	Note	Shareholders' equity as at January 1, 2004	Shareholders' equity as at December 31, 2004	Income statement 2004
Italian accounting principles		**894.5**	**979.0**	**62.0**
Adjustments:				
Tangible fixed assets	1	40.5	39.8	(1.1)
Intangible fixed assets and consolidation differences	2	(16.9)	(19.2)	3.2
Goodwill	3	-	10.2	10.2
IFRS 3	3	-	18.7	
Employee leaving indemnities and similar benefits	5	(0.7)	1.9	2.5
Provisions for risks and charges	6	47.8	66.6	15.8
Other current liabilities			0.6	-
Tax effects of the adjustments	4 – 7	(26.4)	(33.5)	(6.0)
Effect of IAS adjustments		**44.3**	**85.1**	**24.6**
IAS/IFRS accounting standards		**938.8**	**1,064.1**	**86.6**

Reclassification of the balance sheet and income statement items

The main reclassifications made to the balance sheet as at January 1, 2004 and December 31, 2004, and to the 2004 income statement are described below, as already included in the column "IAS reclassified Italian accounting principles".

Balance sheet

Intangible fixed assets

In the balance sheet, leasehold improvement costs for a net value of Euro 5.8 million as at January 1, 2004 and Euro 26.9 million as at December 31, 2004, have been reclassified from intangible fixed assets to tangible fixed assets. In accordance with the IFRS, leasehold improvements not economically separable must be classified respecting the nature of the assets to which they refer.

Long-term receivables

The improvement incurred on assets included in the business rental agreement totalling Euro 38.8 million as at January 1, 2004 and Euro 68.8 million as at December 31, 2004 have been reclassified from long-term receivables to tangible fixed assets, together with the related provision

for the restoration of third party assets amounting to Euro 1.6 million as at January 1, 2004 and Euro 3.8 million as at December 31, 2004.

Accrued income and prepayments and accrued liabilities and deferred income

Other assets and/or other liabilities are recorded in the related items.

Income statement

Extraordinary income and charges

The international accounting standards expressly establish the restriction on separately indicating the item extraordinary income/expense in the income statement. Therefore, as from the consolidated income statement for 2004, these items have been reclassified under current items.

Effects deriving from the application of IAS 32 and IAS 39 as at January 1, 2005

As described in the previous section, international accounting standards IAS 32 and IAS 39 adopted by the European Commission have been applied as from January 1, 2005; the application of these standards has led to the recording of liabilities for a total of Euro 13.3 million, assets for a total of Euro 0.7 million, a reduction in intangible fixed assets of Euro 1.5 million, amounts receivable for prepaid taxes of Euro 5.2 million, a deferred taxation provision for Euro 0.4 million and a corresponding decrease in the shareholders' equity of around Euro 9.4 million.

The reconciliation of the shareholders' equity as at January 1, 2005 deriving from the application of IAS 32 and 39 is as follows:

Euro millions	
IFRS shareholders' equity as at January 1, 2005	1,064.1
Valuation at fair value of the derivative financial instruments	(9.4)
Adjusted shareholders' equity as at January 1, 2005	1,054.7

Hera S.p.A.
Holding Energia Risorse Ambiente
Sede: Viale C. Berti Pichat 2/4 - 40127 Bologna
T. + 39 051.28.71.12 F. + 39 051.28.14.036

www.gruppohera.it

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