Financial Information Internal Control System Policy

11th May 2018

Financial and Business Development Mamagement

Canal de Isabel II

Change History

Date	Revision No.	Reason for modification	Signatures
April 2015	00	Initial version	Financial and Business Development Management
May 2018	01	Change in paragraph 5, and other editorial improvement changes	Financial and Business Development Manager

Contents

1 Introduction

Companies increasingly take on greater commitments due to the protection of the interests of their shareholders, customers, employees, creditors, suppliers and society in general.

These requirements include, among others, establishing concrete measures to strengthen confidence in financial information of all kinds provided outside the company.

In this context, Canal de Isabel II, Sociedad Anónima (hereinafter "Canal" or "the Group"), decided to launch a project to adapt its Internal Financial Reporting Control System (hereinafter IFRCS) to international best practices, with the following objectives:

- Improve the efficiency and security of financial support processes, to minimise possible errors.
- Anticipate new regulatory requirements in terms of internal control and corporate governance, adapting to international best practices.
- Position the company as one of the benchmarks in its sector in terms of internal control and corporate governance.

2 Purpose

The purpose of this document is to define the Internal Control Policy for Canal's Financial Information.

In recent years, both the frequency and the volume of financial information provided externally by the companies have increased.

In this new environment, the transparency and reliability of the process of generating financial information, which in many cases must be prepared at short notice, has become a basic necessity.

Canal maintains a keen interest in ensuring the quality of its internal control over the reliability of financial information and has the clear objective of identifying and controlling the critical risks associated with the authorisation, restriction, integrity and accuracy of financial information, including fraud, and anticipating the necessary corrective measures.

3 Scope

This policy is applicable to the system for internal control of Canal's financial information at all its offices and, where applicable, its investee companies and departments, covering all risks relating to the financial information that affects or may affect the Group, whether these originate in its environment or in its activities. In this regard, the IFRCS particularly covers risks that threaten the financial reporting objectives. (existence and occurrence; integrity; valuation; presentation, breakdown and comparability; and rights and obligations) but also takes into account the effects of other types of risks covered by Canal's comprehensive risk system (operational, technological, financial, legal, reputational, environmental, etc.) insofar as they affect financial statements.

4 General Aspects of the IFRCS

In recent years the concepts of Risk Management and Internal Control have been developed and standardised (through widely accepted global frameworks such as that established by the report by COSO (*Committee of Sponsoring Organizations of the Treadway Commission*)), something which should be clarified, since the IFRCS is an essential part of these concepts.

- Risk Management is the process designed to identify potential events that may affect the Organisation and manage any risks to keep them below accepted thresholds, providing a reasonable level of security on the achievement of objectives.

- Internal Control is the process carried out by the Board of Directors, management and other personnel of the Organisation for the purpose of providing reasonable assurance of the achievement of effectiveness and efficiency of operations, reliability of financial information, compliance with applicable regulations and to safeguard assets. Internal Control is an integral part of Risk Management.

4 Aspectos generales del SCIIF

- Taking as a reference the regulations in force at any given time drawn up by Spain's National Stock Market Commission (CNMV), the IFRCS is part of Internal Control and is configured as the set of processes carried out by the Board of Directors, the Audit Committee, Senior Management and the entity's staff involved in it to provide reasonable assurance as to the reliability of financial information published to the markets. To this end, the Canal's IFRCS must ensure:

- **Existence and occurrence:** the transactions, facts and other events included in the financial information actually exist and have been recorded at the appropriate time.

- **Integrity:** the information reflects the totality of the transactions, facts and other events to which the entity is an affected party.

- **Valuation:** the transactions, facts and other events are recorded and valued in accordance with applicable regulations.

4 Aspectos generales del SCIIF

- **Presentation, breakdown and comparability:** the transactions, facts and other events are classified, presented and disclosed in the financial information in accordance with applicable regulations.

- **Rights and obligations:** the financial information reflects, at the relevant date, the rights and obligations through the corresponding assets and liabilities, in accordance with the applicable regulations.

The objectives of the IFRCS are also considered because of their impact on the five basic objectives above, the safeguarding of assets and fraud prevention and detection.

The principles and good practices set out in the CNMV Circular are based on the internationally recognised COSO reports but limited to the IFRCS.

In this context, Canal's IFRCS is inspired by the COSO III reference framework.

4 Aspectos generales del SCIIF

This integrated control framework consists of five interrelated components, derived from management style and integrated into the management process:

- Control environment.
- Risk assessment.
- Control activities.
- Information and communication.
- Monitoring.

The following sections of this policy describe the main characteristics of each component.

One of the key features of the model's design is that it aims to ensure the quality of financial information in all months of the year, not just for periods corresponding to annual or half-yearly closures. This feature is reinforced by the use of a specific application for the internal control model that allows the status of controls to be monitored at all times.

Another important feature is that it extends the culture of internal control across corporate and business organisations, which contribute significantly to the generation of financial information, by assigning personal responsibility for the execution and documentation of controls.

All relevant documentation relating to the internal control model, both of the certification process and of the internal control itself, resides in the aforementioned computer system.

The personnel responsible for carrying out the controls input into the computer system the evidence that proves that these have been carried out, and evaluate the results obtained, classifying them as satisfactory or unsatisfactory.

This allows the internal control situation to be monitored in real time, allowing action to be taken quickly on the deficiencies detected.

The meaning attributed by this policy to the concepts and terms presented in its sections is included in the Glossary of Terms attached as Appendix I.

5 Control Environment

Roles and responsibilities

- **Board of Directors:** as the most senior body representing, administering, directing, managing and controlling the company, except for those activities attributed to the General Shareholders' Meeting, it is responsible for the existence and maintenance of an adequate and effective IFRCS.
- **Audit Committee:** supervises the effectiveness of the Company's internal control, Internal Audit, where appropriate, and risk management systems.
- **Financial and Business Development Management:** as part of the Management Committee, and by delegation, performs the following functions in relation to the internal control of financial reporting:
  - Design, implementation and operation.
  - Selection of accounting policies applicable to financial reporting.
  - Identification and annual assessment of risks associated with the achievement of financial reporting objectives.

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5 Control Environment

- Determination of the scope of the IFRCS (significant accounts and key processes by business unit) and identification of controls that should be documented, implemented and distributed, ensuring their proper design and operation.

- **Internal Audit Function:** Under its mandate to monitor the effectiveness of the internal control and risk management systems and referring to the IFRCS, it has, among others, the following responsibilities:

  - Develop and execute, under the Annual Audit Plan, the assessment of the effectiveness of the IFRCS, oriented to the risks to the financial information identified and assessed by the Finance and Business Development Management.

  - Inform the Audit Committee of possible weaknesses detected during the audits carried out, as well as the timetable assigned to the proposed recommendations for their correction.

Organisation and assignment of responsibilities

- The Board of Directors is responsible for reviewing the necessary organisational

5 Control Environment

structure of the company in order to ensure that it fully meets the objectives set.

- The Board is also responsible for appointing and removal of the Chief Executive Officer.

- The Audit Committee supports the Board of Directors in its monitoring duties by periodically reviewing the process for preparing the economic and financial information, the company's internal controls and the independence of the external auditor.

- The appointment of the Management Committee ensures that duties are adequately segregated and ensures that the scopes of the different managements are coordinated in order to achieve the Company's objectives.

- The Resources Division is responsible for analysing and communicating changes in the Organisation. The company's detailed organisation chart is published on the corporate Intranet and is available to all employees.

5 Control Environment

In order to implement and maintain its IFRCS, Canal has prepared a Manual of Responsibilities which includes the functions and main activities of management and maintenance of the System at all levels of the Organisation.

Code of Conduct and Ethical Guidelines

With the aim of guiding and promoting ethical professional practices and adopting new regulations on integrity and transparency, senior management has drawn up a Code of Conduct that is applicable to and binding on all Canal personnel, that sets out its values and principles.

These ethical and integrity practices implemented in Canal will serve as a reference, where appropriate, for the rest of the group's companies.

- This **Code of Conduct** was approved by the Board of Directors at its meeting held on 8th January 2015.

- The Code of Conduct sets out the general ethical principles for the entire Organisation, embodied in values to be followed by the Organisation and which include:

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5 Control Environment

A. Values

- Compulsory for all company personnel.
- Commitment to a culture of ethics and compliance.
- Code of Conduct.
- Acceptance of and compliance with the Code of Conduct.

B. Integrity and professional responsibility are among the general **criteria governing Canal's conduct**.

It establishes a series of rules, which to a greater or lesser extent are related to the reliability of financial information and compliance with applicable regulations, in particular:

- Obligation to know and comply with the rules, as well as with internal procedures and processes.
- Make decisions traceable.
- Ensure that all information, including financial information, is rigorous and reliable.

5 Control Environment

- Additionally, Canal has an Internal Code of Conduct in matters relating to the stock markets, which was also approved by the Board of Directors at its meeting held on 8th January 2015.

Among other things, this Code covers the following aspects in relation to financial information:

- Rules of conduct in relation to the personal operations of obligated persons.
- Rules of conduct in relation to inside information.
- Rules of conduct in relation to relevant information.
- Rules of conduct in relation to the handling of stock market listings.

These Rules apply, inter alia, to those persons who may have regular and recurring access to inside information.

From this analysis and description of the control environment that covers these Rules, any policies and procedures resulting from it will be drawn up.

5 Control Environment

- As one of the necessary safeguards, an Ethics and Compliance Committee was created. It has the following functions, among others: To inform the Organisation of the approved Code of Conduct.

- Develop materials for delivery of face-to-face training seminars.

- Design and develop online training courses.

- Raise awareness among senior management.

- Implement the Ethical Guidelines and the corresponding Response Protocol.

Training Programmes

The Annual Training Plan drawn up for the entire company includes training actions relating to knowledge of the International Financial Reporting Standards (IFRS), such as updates in new regulations, as well as those regarding trends in the principles relating to Internal Control of Financial Information, Internal Audit and Risk Management.

6 Financial Information Risk Assessment

Canal's IFRCS risk assessment uses a top-down risk-oriented approach, using both materiality and qualitative risk factors to classify the balance sheet and profit and loss accounts of the Group's different reporting units.

This exercise, which will be carried out at least once a year, makes it possible to demarcate the scope of the IFRCS in terms of the key processes and sub-processes of each reporting unit, which must be documented, implemented and their operation ensured. The following information should be available for each process within the scope of IFRCS:

- Significant accounts and breakdowns of information associated with the process.
- Relevant financial information objectives (existence and occurrence, integrity, etc.).
- Specific financial reporting risks.
- Key sub-processes to mitigate identified risks.

The objectives for internal control of financial reporting within the scope defined in this procedure, compliance with which would reasonably ensure the reliability of financial reporting, are as follows:

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6 Financial Information Risk Assessment

- Existence and occurrence
- Integrity
- Valuation
- Presentation, breakdown and comparability
- Rights and obligations

The risks associated with the achievement of the control objectives, in accordance with the scope of application defined in this procedure, are identified in the financial information preparation processes and evaluated in terms of relative importance, which is determined by the probability of the risk of incurring an error with material impact on the Canal's financial statements. The following indicators are assessed in the risk assessment:

- Risk Heat Map
- Externalisation
- Transaction volume
- Critical accounting judgements and estimates
- Automation
- Segregation of duties
- Fraud

The results of the risk assessment on the financial information will be the basis for the design and implementation of the IFRS control activities described below, as well as for the preparation of the annual plan for their evaluation.

7 Control Activities

Adequate IFRCS documentation is an integral part of the control system, because it provides an understanding of the Organisation's control processes and activities, informs the staff involved of their responsibilities, and describes the context in which controls operate and facilitates the monitoring and evaluation of their design.

Therefore, the Finance and Business Development Management will document the key processes identified in the definition of the scope of the IFRCS, resulting from the previous risk assessment component. Therefore, the documentation should be reviewed and updated if necessary, each time the risks to the financial information are assessed, and at least once a year.

Canal has opted for an IFRCS documentation model with the following elements:

- Description of the activities in the process that allow it to obtain a general understanding of it.
- Detailed description of key controls.
- Risk matrix and key controls.

7 Control Activities

Control activities shall include, in all cases:

- The processes related to the different types of transactions that may materially affect the financial statements including the accounting close and the specific review of relevant judgements, estimates, valuations and projections.

- The process of identifying the consolidation perimeter.

- General controls on information systems (among others, access security, change control, change operation, operational continuity and segregation of duties).

- Monitoring processes for management of activities relevant to financial information outsourced to third parties.

8 Information and Communication

The data supporting the financial information must be collected in a complete, accurate and timely manner for all transactions, facts and other events affecting the Company.

Information and communication systems must identify, collect, process and distribute information on transactions, facts and other events in a period of time that allows the personnel involved to perform the duties assigned to them, including those of carrying out the controls for which they are responsible.

The Deputy Manager for Economic Administration, who reports directly to the Financial and Business Development Management, is responsible for defining and updating accounting policies, as well as resolving queries or conflicts arising from their interpretation. This manager maintains fluid communication with those responsible for the Organisation's operations and, in particular, with those responsible for accounting functions.

8 Information and Communication

The Deputy Manager for Economic Administration is also responsible for publishing the Group's accounting practices manual. The purpose of this manual is to establish the principles, bases, conventions, rules and specific practices for the accounting of certain specific financial transactions within the framework of the activity carried out by the Group and to disseminate them appropriately. The manual of accounting practices is updated annually. During the updating process, the Deputy Manager for Economic Administration incorporates into the manual any new or relevant regulatory changes in accounting matters that have occurred during the fiscal year.

During the year, the manager analyses whether new regulations affect the Group's accounting practices, as well as the date on which each standard comes into force. Any regulations identified as affecting the Group's accounting policies are included in the manual at the end of the financial year.

8 Information and Communication

The mechanism for capturing and preparing the information supported by Canal Group's main financial statements is mainly based on the use of the SAP Business Planning and Consolidation (BPC) tool. It is accessible in all geographical areas in which the Group currently operates.

A large part of the information supported by the breakdowns and notes to the accounts is input to in the consolidation tool. The rest is captured by means of spreadsheets in homogeneous formats, which are prepared for annual closings.

The capture and preparation of detailed information on the IFRCS is centralised in the Finance and Business Development Management. This management, through its different deputy managers, holds interviews with the different managers of the areas involved in order to compile the information to support and justify the description of the IFRCS.

9 Monitoring and Self-assessment

The IFRCS monitoring model is based on assessments that are ongoing ("self-assessment") and stand-alone.

Ongoing assessments ("self-assessment")

Throughout the year the corresponding control design and effectiveness tests are run using Internal Control and SAP GRC Risk Management. These are both general system tests, and tests for those described in each of the selected processes. The Internal Audit Department will itself include, once the corresponding Plan has been approved by the Audit Committee, auditing the IFRCS.

Stand-alone assessments

The Audit Committee has the following oversight responsibilities under the IFRCS:

- Monitor the effectiveness of the company's internal control, internal audit where appropriate, and risk management systems, as well discussing with the auditors of the accounts or audit firms the significant weaknesses of the internal control system detected during the audit.

9 Monitoring and Self-assessment

- To supervise the process of preparation and presentation of regulated financial information.

Based on the results of the risk assessment, the Internal Audit Function annually prepares the assessment plan for Canal's IFRCS.

The scope of the IFRCS assessment in each period is submitted to the Audit Committee for approval, as the body responsible for the oversight of the IFRCS.

The internal control system monitoring process must be ongoing so that there is reasonable assurance that the information contained in the interim closures is reliable. To ensure this, the internal control and risk management systems shall be reviewed periodically so that the main risks are properly identified, managed and disclosed.

Information provided to the market and to stakeholders about the IFRCS shall be of an annual nature and relate to the financial year to which the financial report relates.

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Appendix I

Glossary of Terms

To improve the usefulness and uniformity of the information to investors and analysts of listed companies, the following are binding definitions of terms used in the different sections of this document:

Accounting closing procedure: The process of grouping and final consolidation of information from the different units through which the entity operates and of recording adjustments calculated at the corporate level.

Accounting policy department or area: The internal group in the entity responsible for defining accounting policies that are subsequently applied throughout the organisation, to ensure compliance with the financial reporting standards applicable to the entity, and to resolve any queries or conflicts arising from its interpretation.

Code of conduct: This sets out the principles and values that should govern the actions of the Organisation's staff and their responsibilities in the face of fraud, malpractice or illegalities, with the aim of achieving generally accepted business ethics.

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Compensating controls: those that serve to achieve the objective of another control that did not function properly and help to reduce the risk to an acceptable level.

Complaints channel: Channel for direct access to the Audit Committee. Its existence and how to access it are made known everyone in the Organisation. It is outside the usual operational hierarchy, and issues alerts about irregularities, preferably of a financial and accounting nature.

Control/control activities: policies and procedures that help to ensure that the guidelines established by management are being implemented. Control activities, whether automatic within an information system or by manual processes, may cover several control objectives and are applied at different functional and organisational levels.

Control environment: Controls that arise from the management of an organisation and transcend all its levels. It includes the functions, attitudes, awareness and activities of the governing bodies and management of internal control, as well as the importance of internal control in the entity.

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Corporate Risk Management: The process designed to identify potential events that may affect the Organisation and manage any risks to keep them below thresholds accepted by management, to provide a reasonable level of security on the achievement of its objectives.

Detective controls: intended to detect errors or irregularities which could affect the financial information.

Disciplinary regime: A set of formal rules that set out the consequences that a member of the entity will suffer as a result of a verified breach of the code of conduct.

Entity-wide controls: These generally affect the whole organisation and have an impact on controls at the process, transaction or application level. The entity-wide controls vary in precision and nature and may have a direct or indirect effect on the likelihood that an error will be prevented or detected in time.

Error: This includes, for the purposes of this document, any accidental act by which

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information is omitted or presented incorrectly, in such a way that the financial information is not presented in accordance with the standards of its preparation applicable to the entity.

Financial information: The content of the annual or half-yearly accounts, which include the balance sheet, profit and loss account, statement of changes in equity, cash flow statement and notes. It also includes data of an accounting nature contained in management reports and quarterly interim declarations.

Fraud: An intentional act committed by one or more individuals in the management of the company, employees or third parties, which includes the use of deception to obtain an illegal or unfair advantage.

IFRCS deficiency: this is an internal control weakness caused by:

- A weakness in the design of the affected system, either because the controls needed to ensure the reliability of financial information are lacking, or because the existing controls

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are not properly designed, in such a way that, although the control operates effectively, the risk would not be covered.

- A weakness in the functioning of the affected system because the existing controls, although properly designed, do not operate effectively.

Information and communication: Information systems identify, collect, process and distribute information about transactions and events. Communication systems serve to distribute to the organisation the criteria, guidelines, instructions and in general the information that the members of the organisation must have in order to know about their functions and the ways and time in which they must be carried out.

Internal audit: an independent and objective assurance and consulting function designed to add value to and improve the Organisation's operations. It helps the Organisation achieve its objectives by providing a systematic and disciplined approach to assessing and improving the effectiveness of risk management, control and governance processes.

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Internal control: A process carried out by the Board of Directors, Management and other employees of the Organisation. It is designed to provide reasonable assurance as to the achievement of objectives in the following categories:

- Effectiveness and efficiency of operations.
- Reliability of financial information.
- Compliance with regulations applicable to the entity.
- Safeguarding of assets.

Internal control system in the process of preparation and issuing of financial information (IFRC): A set of processes carried out by the board of directors, the Audit Committee, the management and the entity's personnel involved to provide reasonable assurance as to the reliability of the financial information they disseminate to the market.

Key controls: Those that adequately and promptly mitigate any fraud or errors with material impact on financial information issued. They include general controls across the organisation and control activities selected for their effectiveness

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in mitigating risk of material misstatement of financial information.

Listed companies: entities that issue shares for trading on official securities markets.

Management: the person(s) with executive responsibility for performing the company's activities, reporting to Senior Management.

Manual of accounting policies: A document specific to each entity and disseminated to all its units, which contains and explains the rules for preparing financial information and how they should be applied to the entity's specific operations. The recording standards in the accounting manual are based on the standards applicable to the entity (generally IFRS or PGC), that have been adapted for internal use, which is required, and give the specific options adopted by the entity, if any, and cover all types of transactions executed by the entity.

Material Weakness: A deficiency or combination of deficiencies in the IFRCS such that there is a reasonable possibility that a material misstatement of the financial statements will not be prevented or detected on a timely basis (see definition of Materiality).

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Materiality: The extent of an error or omission in financial information that can change or influence a person's reasonable judgement.

Preventive controls: intended to prevent errors or irregularities which could affect the financial information.

Process controls: controls of an organisation's business processes which are more specific than its general controls.

Reasonable security: Risk management, however well designed and operational it may be, cannot provide assurance of the achievement of the entity's objectives, due to the inherent limitations of such management.

Risk: The possibility of an event occurring which adversely affects the reliability of financial information.

Risk assessment: The process for identifying and assessing risks affecting the reliability of financial information and for establishing policies to address them.

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Senior Management: directors who report directly to the Board or to the chief executive of the company and, in all cases, the internal auditor.

Significant deficiency: A deficiency or combination of deficiencies in the IFRCS, which is less severe than a material weakness, yet important enough to merit attention by those responsible for oversight of preparing and issuing the company's financial reporting.

Significant risk: One whose potential impact may be material and requires special attention.

Supervision of the IFRCS: A set of activities to verify that the internal control policies and procedures implemented to ensure the reliability of financial information have been properly designed and are operating effectively, so that they can provide reasonable assurance that the system is effective in preventing, detecting and correcting any material misstatement or fraud in the financial information.

Unified code: Unified code of good governance for listed companies published by the CNMV in May 2006.

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Glossary of Acronyms

CNMV: Comisión Nacional del Mercado de Valores (Spanish National Stock Market Commission).

COSO: Committee of Sponsoring Organizations of the Treadway Commission. (Working group spon-sored by five organisations that includes professionals in internal audit, external audit, accounting, fi-nance and academia. Formed in 1985 to create an internal control framework.
This first document, published in 1992, was followed by work in different areas of risk management, adaptation to small businesses, supervision, etc.).

GTCI: Grupo de Trabajo de Control Interno sobre la información financiera (working group on Internal control over financial information, sponsored by the CNMV).

IAGC: Informe Anual de Gobierno Corporativo (Annual Corporate Governance Report).

ICAC: Instituto de Contabilidad y Auditoría de Cuen-tas (Spanish Institute of Accounting and Auditing).

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IFRS: International Financial Reporting Standards.

ISA: International Standards on Auditing.

LMV: Ley del Mercado de Valores (Spanish Securities Market Law).

NTA: Normas Técnicas de Auditoría (Technical Auditing Standards) published by ICAC.

PGC: Plan General de Contabilidad (Spanish General Accountancy Plan).

SOX: Sarbanes-Oxley law, passed in 2002.

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