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REPORT PREPARED BY THE AUDIT AND CONTROL COMMITTEE OF LAR ESPAÑA REAL ESTATE SOCIMI, S.A. ON ITS FUNCTIONING IN 2016

I. INTRODUCTION

In accordance with the provisions of article 14.7 of the Board of Directors Regulations of Lar España Real Estate SOCIMI, S.A. ("**Lar España**" or the "**Company**") regarding regulation of the Audit and Control Committee, and in order for the Board of Directors to undertake the annual evaluation of this Committee as provided in article 529 *nonies* of the consolidated text of the Spanish Companies Act approved by Royal Legislative Decree 1/2010 of 2 July 2010 (the "**Spanish Companies Act**"), the aforesaid Committee will prepare an annual report on its functioning, highlighting the principal issues arising, if any, in respect of its inherent functions. In compliance with the aforesaid rules, the Audit and Control Committee prepares this report that, when deemed to be appropriate, may also include proposals to improve the Company's governance rules.

This report will be attached to the Company's annual corporate governance report and will be available to shareholders and investors by way of the Company's website (www.larespana.com) from the call of the ordinary General Meeting of shareholders.

For the purpose of complying with recommendation 6 of the Code of Good Governance for Listed Companies, the information regarding auditor's independence, functioning of the Audit and Control Committee and related transactions is included in the present report.

II. COMPOSITION

Articles 42 of the Articles of Association and 14 of the Board of Directors Regulations, at the date of this report, provide that the Audit and Control Committee will be comprised of a minimum of three and a maximum of five directors, appointed by the Board of Directors from among the non-executive directors. The majority of the Audit and Control Committee will be independent and will be appointed —specially the Chairperson— on the basis of knowledge and experience in accounting or auditing, or both. The Board of Directors will also appoint one of the members of that Committee to act as the Chairperson thereof. In accordance with article 14.1 of the Board of Directors Regulations, the Chairperson of the Audit and Control Committee will remain in office for a maximum term of three years, at the end of which the Chairperson may not be re-elected as such until one year has passed after leaving office, without prejudice to the Chairman's continuing or being re-elected as a member of the Committee.

During 2016 there was no change in the composition of the Audit and Control Committee. It was as follows:

- **Mr. José Luis del Valle Doblado** (Chairman) is an independent non-executive director of Lar España. He was appointed as a director of Lar España by Grupo Lar Inversiones Inmobiliarias, S.A., the then sole shareholder of the Company, on 5 February 2014. The Board of Directors of the Company appointed him as a member of the Audit and Control Committee on 6 February 2014. Mr. del Valle has extensive experience in the banking and energy sector. From 1988 to 2002 he

held various positions with Banco Santander, one of the most relevant financial entities in Spain. In 1999 he was appointed General Manager and Financial Manager of the bank (1999-2002). Subsequently he was Development and Strategy Manager of Iberdrola, one of the main Spanish energy companies (2002-2008), Managing Director of Scottish Power (2007-2008), Strategy and Research Manager of Iberdrola (2008-2010) and Advisor to the Chairman of the aerogenerator manufacturer Gamesa (2011-2012). Currently, Mr. del Valle is non-executive Chairman of the Board of GES - Global Energy Services, a provider of construction services, operation and management for the renewable energy industry, a Director of the insurance group Ocaso; and director of the Instituto de Consejeros-Administradores. He also sits in the Board of Directors of Abengoa, S.A., a provider of innovative technological solutions for the sustainable development.

Mr. José Luis is a Mining Engineer from Universidad Politécnica (Madrid, Spain), number one of his class, Master of Science and Nuclear Engineer from the Massachusetts Institute of Technology (Boston, USA). Furthermore, Mr. del Valle holds an MBA with high honours from Harvard Business School (Boston, USA).

- **Mr. Pedro Luis Uriarte Santamarina** (Member) is an independent non-executive director of Lar España. He was appointed as a director of Lar España by Grupo Lar Inversiones Inmobiliarias, S.A., the then sole shareholder of the Company, on 5 February 2014. The Board of Directors of the Company appointed him as a member of the Audit and Control Committee on 6 February 2014. From 1975 to 2001 he held various positions with BBVA, one of the main Spanish Banks, as Vice Chairman of BBV and BBVA. He was appointed Managing Director of BBV in 1994. He held the position as Vice Chairman of the Board of Telefónica, leader in the Spanish telecommunications market. He was appointed Minister of Economy and Finance of the Basque Government in 1980. In 2007, Mr. Uriarte founded and headed Innobasque, the Basque Innovation Agency. Currently, he is Chief Executive Officer of the strategy consulting firm Economía, Empresa y Estrategia, and is member of several boards and consulting bodies of other boards of directors. Moreover, Mr. Uriarte is Vicepresidente of the Civil Council of Bilbao and has been a member of the executive meeting of UNICEF Spain.

Mr. Pedro Luis graduated from Universidad de Deusto (Bilbao, Spain) with a degree in business and administration, and is a member of the board and executive committee of Deusto Business School, and has been honoured with numerous awards such as the "*Gran Cruz al Mérito Civil*" (Spanish government) in 2002, "*Directivo del año*" (Spanish Confederation of Managers & Executives - CEDE) in 2011 and was awarded with the Sabino Arana award in 2016.

- **Mr. Miguel Pereda Espeso** (Member) is a proprietary non-executive director of Lar España. He was appointed as a director of Lar España by Grupo Lar Inversiones Inmobiliarias, S.A., the then sole shareholder of the Company, on 5 February 2014. The Board of Directors of the Company appointed him as a member of the Audit and Control Committee on 6 February 2014. Mr. Pereda has more than 25 years of experience in the real estate sector, and is a director and shareholder of Grupo Lar Inversiones Inmobiliarias, S.A., since 2007, and previously, for a period of 6 years, was Chief Executive Officer of Lar Grosvenor.



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In 2015, Mr. Pereda was appointed Eminent Member (Fellow) of the Royal Institution of Chartered Surveyors in London (RICS).

Mr. Miguel has a degree in business administration from Universidad Complutense (Madrid, Spain), an MBA from the Instituto de Empresa (IE), participated in the Breakthrough program for Senior Executives of the IMD, has a Masters in tax from ICADE and participated in the Real Estate Management Program of Harvard University.

In accordance with the provisions of article 14.1 of the Board of Directors Regulations, the secretary of the Audit and Control Committee is Mr. Juan Gómez-Acebo Sáenz de Heredia, as he is also the secretary of the Board of Directors.

As a result, the composition of the Committee during 2016 has been consistent with the provisions of the Board of Directors Regulations and article 529 *quaterdecies.1* of the Spanish Companies Act, in accordance with its current version, whereby this Committee is comprised exclusively of non-executive directors appointed by the Board of Directors and with a majority of independent directors.

III. MEETINGS

The Audit and Control Committee ordinarily meets on a quarterly basis, in order to review the periodic financial information to be submitted to the stock market authorities as well as the information the Board of Directors must approve and include within its annual public documentation. It also may meet at the request of any of its members and when called by its Chairman. The Chairman must call the meeting whenever the Board or its Chairman requests the issuance of a report or preparation and adoption of proposals and, in any event, whenever it is appropriate to the proper exercise of its authority.

The Audit and Control Committee met ten times during 2016.

As a result, the Audit and Control Committee met with the frequency required for proper performance of its duties. All of its members attended the meetings that were held. Mr. Pedro Luis Uriarte attended two meetings represented by Mr. José Luis del Valle pursuant to a special delegation granted for these purposes.

All the meetings of the Audit and Control Committee were held at the Company's registered office. When a member was not in Madrid and thus could not physically attend the meeting, he or she attended the meeting by conference call.

IV. ACTIVITIES DURING 2016

This Committee, in fulfilment of the duties it assumes under article 14 of the Board Regulations, focused its meetings during 2016 on the following principal activities:

- **Review of periodic financial reporting**

As in the last financial period, the Committee supervised the process of preparation and the integrity of the quarterly and semi-annual financial information, both individual and consolidated, that the Board of Directors must provide to the market and send to the National Securities Market Commission ("CNMV") by virtue of its periodic reporting obligations as a listed company.



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Accordingly, the Committee, prior to its submission, reviewed compliance with the regulatory requirements, appropriate definition of the scope of consolidation and proper application of accounting principles in the periodic financial reporting, all within the terms legally established for that purpose.

- **Review of annual accounts**

The Audit and Control Committee, with the purpose of preventing the individual and consolidated annual accounts prepared by the Board of Directors from being presented with reservations and qualifications in the audit report, performed the following activities prior to the preparation of the accounts:

- Review the accounts of the Company.
- Monitor and verify compliance with legal requirements and the proper application of generally accepted accounting principles.
- Review the periodic financial information that the Board of Directors must provide to the markets and their supervising bodies.

The Audit and Control Committee reported favourably to the Board of Directors prior to the preparation of the annual accounts.

Accordingly, it is noted that the audit reports of the individual and consolidated annual accounts of Lar España corresponding to the financial year ended 31 December 2015 had no reservations or qualifications. Likewise, no reservations or qualifications are expected regarding the audit reports regarding the individual and consolidated accounts of Lar España corresponding to the financial year ended 31 December 2016.

- **External audit**

The Audit and Control Committee supervised the relationships with the external auditors and its fees for the financial year 2016, as well as the compliance with the current auditing services contract, ensuring that the opinion on the annual accounts and principal content of the audit report were drafted clearly and precisely.

Also, the Audit Committee verified, already in 2017, that the work engaged from the statutory auditor is in compliance with the independence requirements established in Royal Legislative Decree 1/2011 of 1 July 2011 approving the recast text of the Audit Act.

The Audit Act and section 4, function f), of article 529 *quaterdecies* of the Spanish Companies Act require that the Audit Committee annually, prior to the audit report, issue a report stating an opinion regarding the independence of the auditors. Based on this requirement and the confirmation of independence received from the auditors through the letter date 20 February 2017 attached to this report as **Annex I**, the Audit and Control Committee concluded that there are no objective reasons for questioning the independence of the statutory auditor for 2016.

In particular, this Committee reasonably concludes that:

- (i) While performing its duties during the fiscal year 2016, the auditor has complied with the applicable rules regarding independence established in the auditing regulations.



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- (ii) No circumstances have been identified in order to question the compliance with the rules governing the auditing activities performed by the external auditor with regards to its independence and the Company.
- (iii) The fees paid by the Company to the auditor do not represent a significant percentage of the revenue of the auditor for the purposes of complying with the rules established in the Audit Act.
- (iv) The fees paid to the auditor have been reasonably justified, estimating that they will not exceed reasonable market prices applicable to these types of services.
- (v) Currently, the obligation regarding the rotation of the signing auditor partner is not applicable.
- (vi) There are no circumstances or aspects that could reasonably be considered as a breach of the auditing rules regarding independence of the auditor or with the delivery of additional services different from the audit services.

- **Internal Audit**

The Audit and Control Committee has performed during 2015 the functions related to internal auditing of the Company that have been attributed to it in the Board Regulations, basically the following: (i) seeing to the independence and effectiveness of the internal audit function; (ii) propose the selection, appointment, re-election and termination of the person responsible for the internal auditing department; (iii) propose the budget of the department; (iv) approve the orientation and the working plans, ensuring that its activity is mainly focused on the relevant risks of the Company; (v) receive periodical information regarding its activities; and (vi) verify that senior management takes into consideration the conclusions and recommendations of its reports.

In this regard, the internal audit of the Company has periodically informed the Audit and Control Committee about its activities. In particular, the Committee acknowledged that, during 2015, no material risks had been identified, there were sufficient controls in general terms and the manager was performing a risks' control that was very positive for the Company's internal control procedures.

Likewise, the Committee reviewed and approved a new risk map for the Company that was submitted by the internal audit department, as well as a handbook of accounting policies. The Committee also agreed on the convenience of appointing a person responsible before the SEPBLAC.

- **Compliance with corporate governance regulations**

The Audit and Control Committee has sought to ensure compliance with the Internal Code of Conduct in the Securities Markets, the Board of Directors' Regulation and, in general, all the corporate governance rules of the Company during the financial year 2016, without noticing any relevant breach.

Furthermore, the Committee reported favourably to the Board of Directors in relation to the amendment proposal of the Company's Internal Code of Conduct in the Securities Markets and appointed Ms. Susana Guerrero Trevijano, Legal Director of the Company, as new Legal Compliance Officer of the Company.



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This Committee reviewed and accepted the Annual Corporate Governance Report for the financial year 2015 that, in accordance with article 538 of the Spanish Companies Act, must be included in a separate section of the Management Report that goes together with the Annual Accounts.

Additionally, following the process of preparing an action plan regarding corporate governance that began in 2015 with the support of an internationally well-known consultancy firm (EY), in 2016 the Company has approved a Crime Prevention Handbook whose supervision will correspond to the Audit and Control Committee.

emphasising that the aforesaid plan must take account of and incorporate international corporate governance standards. Specifically, a Code of Conduct and a Complaints Channel have been approved during this financial year.

- **Supervision of the management company's fees**

The Audit and Control Committee has supervised and approved the calculation of, and different payment alternatives for, the fees received by Grupo Lar Inversiones Inmobiliarias, S.A., in its capacity as the management company for Lar España, in the performance of its functions during the current financial year. In this process, the Company retained consultancy services of an internationally well-known investment bank.

In addition, the Committee reviewed and approved criteria for making a provision of such fees, which have also been approved by the Company's auditors.

- **Other**

Finally, the Audit and Control Committee reviewed the selection process for an insurance broker in relation to civil liability, material harms and rental losses liabilities. The Committee also ratified its conformity with the appointment of such process' winner (Willis). Likewise, the Committee approved the interim dividend payment of the Company's subsidiaries during the year 2016.

V. PROPOSALS RELATED TO THE COMPANY'S GOVERNANCE RULES

Among the functions that the Articles of Association, the Board of Directors Regulations and the Internal Code of Conduct in the Securities Markets attribute to the Audit and Control Committee is that of making the necessary proposals for improvement related to the Company's governance rules, when the Committee considers that to be appropriate.

In this regard, during the year 2016, proposals regarding the modification of the internal rules of the Company have been made. Specifically, the amendment of the Company's Articles of Association, the General Meeting Regulations and the Board of Director's Regulations were proposed with the objective of incorporating the latest regulatory changes introduced by the entry into force of Act 22/2015, of 20 July, of Accounts Audit, Act 15/2015 of 2 July on Voluntary Jurisdiction and Act 9/2015 of 25 May on urgent measures in insolvency matters, as well as other corporate governance improvements contained in the Listed Companies Good Governance Code and other technical improvements.

Likewise, an amendment to the Company's Internal Code of Conduct in the Securities Markets was proposed with the aim to introduce regulatory changes arising from the entry into force of Regulation (EU) 596/2014 of the European Parliament and the Council of 16 April 2014



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on market abuse, and its implementing regulations. The Committee also reviewed the interpretation of the secretary's and deputy secretary's reporting obligations to the CNMV in accordance with the new Internal Code of Conduct.

The Committee proposes to review in 2017 the new laws and regulations that have been published, if applicable introducing such reforms as may be necessary or appropriate.

This report, corresponding to the activities of the Audit and Control Committee during the period from 1 January to 31 December 2016, as provided in article 14.7 of the Board of Directors Regulations, will be available to shareholders and investors by way of the Company's website (www.larespana.com) from the call of the General Meeting of Shareholders.

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