



Telefónica Europe B.V.

*(incorporated with limited liability under
the laws of The Netherlands)*

**EUR 750,000,000 Undated 6 Year Non-Call
Deeply Subordinated Guaranteed Fixed Rate Reset Securities**

**EUR 1,000,000,000 Undated 10 Year Non-Call
Deeply Subordinated Guaranteed Fixed Rate Reset Securities**

**unconditionally and irrevocably guaranteed on a subordinated basis by
Telefónica, S.A.**

*(incorporated with limited liability under
the laws of the Kingdom of Spain)*

The EUR 750,000,000 Undated 6 Year Non-Call Deeply Subordinated Guaranteed Fixed Rate Reset Securities (the "**6 Year Non-Call Securities**") and the EUR 1,000,000,000 Undated 10 Year Non-Call Deeply Subordinated Guaranteed Fixed Rate Reset Securities (the "**10 Year Non-Call Securities**"), together with the 6 Year Non-Call Securities, the "**Securities**") are issued by Telefónica Europe B.V. (the "**Issuer**") and unconditionally and irrevocably guaranteed on a subordinated basis by Telefónica, S.A. (the "**Guarantee**", and the "**Guarantor**" or "**Telefónica**", respectively).

As described in the Terms and Conditions of the 6 Year Non-Call Securities (the "**6 Year Non-Call Conditions**"), the 6 Year Non-Call Securities will bear interest on their principal amount (i) at a fixed rate of 5.000% per annum from (and including) the Issue Date to (but excluding) the First Reset Date (as defined in the 6 Year Non-Call Conditions) payable annually in arrear on 31 March in each year, with the first Interest Payment Date on 31 March 2015; and (ii) from (and including) the First Reset Date (as defined in the 6 Year Non-Call Conditions), at the applicable 6 year Swap Rate in respect of the relevant Reset Period, plus: (A) in respect of the period commencing on the First Reset Date to (but excluding) 31 March 2024, 3.804 per cent. per annum; (B) in respect of the period commencing on 31 March 2024 to (but excluding) 31 March 2040, 4.054 per cent. per annum; and (C) from and including 31 March 2040, 4.804 per cent. per annum, all as determined by the Agent Bank, payable annually in arrear on 31 March in each year (each, an Interest Payment Date as defined in the 6 Year Non-Call Conditions), commencing on 31 March 2021.

As described in the Terms and Conditions of the 10 Year Non-Call Securities (the "**10 Year Non-Call Conditions**"), the 10 Year Non-Call Securities will bear interest on their principal amount (i) at a fixed rate of 5.875% per annum from (and including) the Issue Date to (but excluding) the First Reset Date (as defined in the 10 Year Non-Call Conditions) payable annually in arrear on 31 March in each year, with the first Interest Payment Date on 31 March 2015; and (ii) from (and including) the First Reset Date (as defined in the 10 Year Non-Call Conditions), at the applicable 10 year Swap Rate in respect of the relevant Reset Period plus: (A) in respect of the period commencing on the First Reset Date to (but excluding) 31 March 2044, 4.301 per cent. per annum; and (B) from and including 31 March 2044, 5.051 per cent. per annum, all as determined by the Agent Bank, payable annually in arrear on 31 March in each year (each, an Interest Payment Date as defined in the 10 Year Non-Call Conditions), commencing on 31 March 2025.

The Issuer may, at its sole discretion, elect to defer (in whole or in part) any payment of interest on the Securities, as more particularly described in the "*Terms and Conditions of the 6 Year Non-Call Securities — Optional Interest Deferral*" and "*Terms and Conditions of the 10 Year Non-Call Securities — Optional Interest Deferral*", respectively. Any amounts so deferred, together with further interest accrued thereon (at the Prevailing Interest Rate applicable from time to time), shall constitute Arrears of Interest (as defined in the Conditions of the relevant Securities). The Issuer may pay outstanding Arrears of Interest,

in whole or in part, at any time in accordance with the Conditions of the relevant Securities. Notwithstanding the foregoing, the Issuer shall pay any outstanding Arrears of Interest in whole, but not in part, on the first occurring Mandatory Settlement Date following the Interest Payment Date on which any outstanding Arrears of Interest was first deferred, all as more particularly described in "*Terms and Conditions of the 6 Year Non-Call Securities — Optional Interest Deferral — Mandatory Settlement of Arrears of Interest*" and "*Terms and Conditions of the 10 Year Non-Call Securities — Optional Interest Deferral — Mandatory Settlement of Arrears of Interest*", respectively.

The Securities will be undated securities in respect of which there is no specific maturity date and shall be redeemable (at the option of the Issuer) in whole, but not in part, on the applicable First Reset Date (as defined in the Conditions of the relevant Securities) or upon any Interest Payment Date (as defined in the Conditions of the relevant Securities) thereafter, at their principal amount together with any accrued and unpaid interest up to (but excluding) the Redemption Date (as defined in the Conditions of the relevant Securities) and any outstanding Arrears of Interest (including any Additional Interest Amounts thereon). In addition, upon the occurrence of an Accounting Event, a Capital Event, a Tax Event, a Withholding Tax Event, or a Substantial Purchase Event (each such term as defined in the Conditions of the relevant Securities), the Securities will be redeemable (at the option of the Issuer) in whole, but not in part, at the amount set out, and as more particularly described, in "*Terms and Conditions of the 6 Year Non-Call Securities — Redemption and Purchase*" and "*Terms and Conditions of the 10 Year Non-Call Securities — Redemption and Purchase*", respectively.

The Securities will constitute direct, unsecured and subordinated obligations of the Issuer and will at all times rank *pari passu* and without any preference among themselves, all as more particularly described in "*Terms and Conditions of the 6 Year Non-Call Securities — Status and Subordination of the 6 Year Non-Call Securities and Coupons*" and "*Terms and Conditions of the 10 Year Non-Call Securities — Status and Subordination of the 10 Year Non-Call Securities and Coupons*", respectively. The payment obligations of the Guarantor under the Guarantee will constitute direct, unsecured and subordinated obligations of the Guarantor and will at all times rank *pari passu* and without any preference among themselves. In the event of the Guarantor being declared in insolvency under Spanish Insolvency Law (as defined below), the rights and claims of Holders (as defined in the Conditions of the relevant Securities) against the Guarantor in respect of or arising under the Guarantee will rank, as against the other obligations of the Guarantor, in the manner more particularly described in "*Terms and Conditions of the 6 Year Non-Call Securities - Guarantee, Status and Subordination of the Guarantee*" and "*Terms and Conditions of the 10 Year Non-Call Securities — Guarantee, Status and Subordination of the Guarantee*", respectively.

Payments in respect of the Securities will be made without withholding or deduction for, or on account of, any present or future taxes, duties, assessments or governmental charges of whatever nature of The Netherlands or the Kingdom of Spain, unless such withholding or deduction is required by law. In the event that any such withholding or deduction is made, additional amounts will be payable by the Issuer or, as the case may be, the Guarantor, subject to certain exceptions as are more fully described in "*Terms and Conditions of the 6 Year Non-Call Securities - Taxation*" and "*Terms and Conditions of the 10 Year Non-Call Securities — Taxation*", respectively.

This Prospectus has been approved by the United Kingdom Financial Conduct Authority (the "**FCA**"), which is the United Kingdom competent authority for the purposes of Directive 2003/71/EC, as amended (the "**Prospectus Directive**") and relevant implementing measures in the United Kingdom as a prospectus issued in compliance with the Prospectus Directive and relevant implementing measures in the United Kingdom for the purpose of giving information with regard to the issue of the Securities. Applications have been made for the Securities to be admitted to listing on the Official List of the FCA and to trading on the Regulated Market of the London Stock Exchange plc (the "**London Stock Exchange**"). The Regulated Market of the London Stock Exchange is a regulated market for the purposes of Directive 2004/39/EC on markets in financial instruments.

The Securities have not been, and will not be, registered under the United States Securities Act of 1933 (the "**Securities Act**") and are subject to United States tax law requirements. The Securities are being offered outside the United States by the Joint Bookrunners (as defined in "*Subscription and Sale*") in accordance with Regulation S under the Securities Act ("**Regulation S**"), and may not be offered, sold or delivered within the United States or to, or for the account or benefit of, U.S. persons except pursuant to an exemption from, or in a transaction not subject to, the registration requirements of the Securities Act.

The Securities will be in bearer form and in the denomination of EUR 100,000 each. Each series of Securities will initially be represented by a temporary global security (the "**Temporary Global Security**"), without interest coupons or talons, which will be deposited with a common depository on behalf of Euroclear Bank SA/NV ("**Euroclear**") and Clearstream Banking, *Société Anonyme* ("**Clearstream, Luxembourg**") on or about the Issue Date. Interests in each Temporary Global Security will be exchangeable for interests in a permanent global security (the "**Permanent Global Security**" and together with the Temporary Global Security, the "**Global Securities**") in the circumstances set out in each Temporary Global Security. Each Permanent Global Security will be exchangeable for definitive Securities (the "**Definitive Securities**") in the circumstances set out in the relevant Permanent Global Security. See "*Summary of Provisions relating to the Securities while in Global Form*".

The Securities are expected to be rated BB+ by Standard & Poor's Credit Market Services Europe Limited ("**S&P**"), Ba1 by Moody's Investors Service Limited ("**Moody's**") and BBB- by Fitch Ratings Limited ("**Fitch**").

Each of S&P, Moody's and Fitch is established in the European Union and registered under Regulation (EU) No 1060/2009, as amended (the "**CRA Regulation**").

A security rating is not a recommendation to buy, sell or hold securities and may be subject to suspension, reduction or withdrawal at any time by the assigning rating agency.

Prospective investors should have regard to the factors described under the section headed "Risk Factors" in this Prospectus.

Joint Bookrunners

Banco Bilbao Vizcaya Argentaria, S.A.
CaixaBank
Mizuho Securities

Barclays
Goldman Sachs International
Santander Global Banking & Markets

The Royal Bank of Scotland

25 March 2014

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IMPORTANT NOTICES

Each of the Issuer and the Guarantor accepts responsibility for the information contained in this Prospectus and declares that, having taken all reasonable care to ensure that such is the case, the information contained in this Prospectus to the best of its knowledge is in accordance with the facts and contains no omission likely to affect its import. Information appearing in this Prospectus is only accurate as of the date on the front cover of this Prospectus. The business, financial condition, results of operations and prospects of the Issuer and the Guarantor may have changed since such date.

Each of the Issuer and the Guarantor has confirmed to the Joint Bookrunners named under "*Subscription and Sale*" below (the "**Joint Bookrunners**") that this Prospectus contains all information regarding the Issuer, the Guarantor and the Securities which is (in the context of the issue of the Securities) material; such information is true and accurate in all material respects and is not misleading in any material respect; any opinions, predictions or intentions expressed in this Prospectus on the part of the Issuer or (as the case may be) the Guarantor are honestly held or made and are not misleading in any material respect; this Prospectus does not omit to state any material fact necessary to make such information, opinions, predictions or intentions (in such context) not misleading in any material respect; and all proper enquiries have been made to ascertain and to verify the foregoing.

Neither the Issuer nor the Guarantor has authorised the making or provision of any representation or information regarding the Issuer, the Guarantor or the Securities other than as contained in this Prospectus or as approved for such purpose by the Issuer and the Guarantor. Any such representation or information should not be relied upon as having been authorised by the Issuer, the Guarantor or the Joint Bookrunners.

Neither the Joint Bookrunners nor any of their respective affiliates have authorised the whole or any part of this Prospectus and none of them makes any representation or warranty or accepts any responsibility as to the accuracy or completeness of the information contained in this Prospectus. Neither the delivery of this Prospectus nor the offering, sale or delivery of any Security shall in any circumstances create any implication that there has been no adverse change, or any event reasonably likely to involve any adverse change, in the condition (financial or otherwise) of the Issuer or the Guarantor since the date of this Prospectus.

This Prospectus does not constitute an offer of, or an invitation to subscribe for or purchase, any Securities.

The distribution of this Prospectus and the offering, sale and delivery of Securities in certain jurisdictions may be restricted by law. Persons into whose possession this Prospectus comes are required by the Issuer, the Guarantor and the Joint Bookrunners to inform themselves about and to observe any such restrictions. For a description of certain restrictions on offers, sales and deliveries of Securities and on distribution of this Prospectus and other offering material relating to the Securities, see "*Subscription and Sale*".

In particular, the Securities have not been and will not be registered under the Securities Act and are subject to United States tax law requirements. Subject to certain exceptions, Securities may not be offered, sold or delivered within the United States or to U.S. persons.

In this Prospectus, unless otherwise specified, references to a "**Member State**" are references to a Member State of the European Economic Area, references to "**U.S.\$**", and "**U.S. dollar**" are to United States dollars, the lawful currency of the United States of America, references to "**sterling**", "**pound sterling**" or "**£**" are to the currency of the United Kingdom and references to "**EUR**", "**euro**" or "**€**" are to the currency introduced at the start of the third stage of European economic and monetary union, and as defined in Article 2 of Council Regulation (EC) No 974/98 of 3 May 1998 on the introduction of the euro, as amended.

The Securities are securities which, because of their nature, are normally bought and traded by a limited number of investors who are particularly knowledgeable in investment matters, and may not be a suitable investment for all investors. Each potential investor in the Securities must determine the suitability of that investment in light of its own circumstances. In particular, each potential investor should:

- (i) have access to, and knowledge of, appropriate analytical tools to evaluate, in the context of its particular financial situation, an investment in the Securities and the impact the Securities will have on its overall investment portfolio;
- (ii) have sufficient financial resources and liquidity to bear all of the risks of an investment in the Securities, including where the currency for principal or interest payments is different from the potential investor's currency;
- (iii) understand thoroughly the terms of the Securities and be familiar with the behaviour of any relevant indices and financial markets; and
- (iv) be able to evaluate (either alone or with the help of a financial advisor) possible scenarios for economic, interest rate and other factors that may affect its investment and its ability to bear the applicable risks.

Sophisticated institutional investors generally do not purchase complex financial instruments as stand-alone investments. They purchase complex financial instruments as a way to reduce risk or enhance yield with an understood, measured, appropriate addition of risk to their overall portfolios. A potential investor should not invest in the Securities unless it has the knowledge and expertise (either alone or with a financial advisor) to evaluate how the Securities will perform under changing conditions, the resulting effects on the value of the Securities, and the impact this investment will have on the potential investor's overall investment portfolio.

Prior to making an investment decision, potential investors should consider carefully, in light of their own financial circumstances and investment objectives, all the information contained in this Prospectus or incorporated by reference herein. Potential investors should not construe anything in this Prospectus as legal, tax, business or financial advice. Each investor should consult with his or her own advisers as to the legal, tax, business, financial and related aspects of a purchase of the Securities.

In connection with the issue of the Securities, Barclays Bank PLC (the "Stabilising Manager") (or persons acting on behalf of the Stabilising Manager) may over allot Securities or effect transactions with a view to supporting the price of the Securities at a level higher than that which might otherwise prevail. However, there is no assurance that the Stabilising Manager (or persons acting on behalf of the Stabilising Manager) will undertake stabilisation action. Any stabilisation action may begin on or after the date on which adequate public disclosure of the terms of the offer of the Securities is made and, if begun, may be ended at any time, but it must end no later than the earlier of 30 days after the issue date of the Securities and 60 days after the date of the allotment of the Securities. Any stabilisation action or over-allotment must be conducted by the Stabilising Manager (or persons acting on behalf of the Stabilising Manager) in accordance with all applicable laws and rules.

Certain terms and conventions

As used herein, "**Telefónica**", "**Telefónica Group**", "**Group**", and "**the Company**" mean Telefónica, S.A. and its consolidated subsidiaries, unless the context requires otherwise.

Below are definitions of certain technical terms used in this Prospectus:

- "**Access**" refers to a connection to any of the telecommunications services offered by Telefónica. Because a single fixed customer may contract for multiple services, Telefónica counts the number of accesses, or services a customer has contracted for. For example, a customer that has fixed line telephony service and broadband service represents two accesses rather than one. The following are the main categories of accesses:
 - "**Fixed telephony accesses**": includes public switched telephone network, or PSTN, lines (including public use telephony), and integrated services digital network, or ISDN, lines and circuits. For purposes of calculating the number of fixed line accesses,

Telefónica multiplies its lines in service as follows: PSTN (x1); basic ISDN (x1); primary ISDN (x30, x20 or x10); 2/6 digital accesses (x30).

- **"Internet and data accesses"**: includes retail broadband accesses (retail asymmetrical digital subscriber line "ADSL," very high bit-rate digital subscriber line "VDSL", satellite, fiber optic and circuits over 2 Mbps), narrowband accesses (Internet service through the PSTN lines) and other accesses, including the remaining non-broadband final client circuits. "Naked ADSL" allows customers to subscribe for a broadband connection without a monthly fixed line fee.
- **"Pay TV"**: includes cable TV, direct to home satellite TV, or DTH, Internet Protocol TV, or IPTV.
- **"Mobile accesses"**: Telefónica counts each active SIM as an access regardless of the number of services contracted through the SIM. Includes accesses to mobile network for voice and/or data services (including connectivity). Mobile accesses are categorised into contract and prepaid accesses.
- **"Mobile broadband"**: includes mobile Internet (Internet access from devices also used to make voice calls e.g. smartphones-), and Mobile Connectivity (Internet access from devices that complement fixed broadband, such as PC Cards/dongles, which enable large amounts of data to be downloaded on the move).
- **"Unbundled/shared local loop", or "ULL"**: includes accesses to both ends of the copper local loop leased to other operators to provide voice and DSL services (fully unbundled loop, fully UL) or only DSL service (shared unbundled loop, "shared UL").
- **"ARPU"** is the average revenues per user per month. ARPU is calculated by dividing total gross service revenues (excluding inbound roaming in revenues) from sales to customers for the preceding 12 months by the weighted average number of accesses for the same period, and then divided by 12 months.
- **"Data ARPU"** is the average data revenues per user per month. ARPU is calculated by dividing total data revenues (SMS, MMS and other data revenues like mobile connectivity and mobile Internet, etc.) from sales to customers for the preceding 12 months by the weighted average number of accesses for the same period, and then divided by 12 months.
- **"CDMA"** means Code Division Multiple Access, which is a type of radio communication technology.
- **"Churn"** is the percentage of average customers disconnected over a period of time.
- **"Cloud computing"** is the delivery of computing as a service rather than a product, whereby shared resources, software, and information are provided to computers and other devices as a utility over a network (typically the Internet).
- **"Commercial activity"** includes the addition of new lines, replacement of handsets and migrations.
- **"Data revenues"** includes revenues from SMS, MMS and other data services like mobile connectivity and mobile Internet, etc. consumed by the customer.
- **"Data traffic"** includes all the traffic related to Internet access service, related to messaging service (SMS, MMS) and to connectivity service that is transported by the Telefónica's networks and that generates data revenue.
- **"Digital Dividend"** refers to the amount of spectrum that will be freed up in the switchover from analogue to digital terrestrial TV.
- **"Final client accesses"** means accesses provided to residential and corporate clients.

- "**FTTx**" is a generic term for any broadband network architecture that uses optical fiber to replace all or part of the metal local loop typically used for the last mile of telecommunications wiring.
- "**Gross adds**" means the gross increase in the customer base measured in terms of accesses in a period.
- "**HDTV**" or high definition TV has at least double resolution than SDTV, being able to show higher level of details compared to an analogue TV or to a common DVD.
- "**HSPA**"/ "**HSDPA**" means High Speed Downlink Packet Accesses, which is a 3G mobile telephony communications protocol in the High-Speed Packet Access (HSPA) family, which allows networks based on UMTS to have higher data transfers speeds and capacity.
- "**Interconnection revenues**" means revenues received from other operators which use Telefónica's networks to connect to their customers.
- "**Market share**" is the percentage of final accesses or revenues of one operator compared to the total market in its operating area.
- "**ISP**" means Internet service provider.
- "**IT**", or information technology, is the acquisition, processing, storage and dissemination of vocal, pictorial, textual and numerical information by a microelectronics-based combination of computing and telecommunications.
- "**Local loop**" means the physical circuit connecting the network termination point at the subscriber's premises to the main distribution frame or equivalent facility in the fixed public telephone network.
- "**LTE**" means Long Term Evolution, a 4G mobile access technology.
- "**M2M**", or machine to machine, refers to technologies that allow both mobile and wired systems to communicate with other devices of the same ability.
- "**MTR**" means mobile termination rate, which is the charge per minute or SMS paid by a telecommunications network operator when a customer makes a call to another network operator.
- "**MVNO**" means mobile virtual network operator, which is a mobile operator that is not entitled to use spectrum for the provision of mobile services. Consequently, an MVNO must subscribe to an access agreement with a mobile network operator in order to provide mobile access to their customers. An MVNO pays such mobile network operator for using the infrastructure to facilitate coverage to their customers.
- "**Net adds**" means the difference between the customer base measured in terms of accesses at the end of the period and the beginning of the period.
- "**Non SMS data revenues**" means data revenues excluding SMS revenues.
- "**OTT services**" or "**over the top services**" means services provided through the Internet (such as television).
- "**P2P SMS**" means person to person short messaging service (usually sent by mobile customers).
- "**Revenues**" means net sales and revenues from rendering of services.
- "**Service revenues**" means revenues less revenues from handset sales. Service revenues are related mainly with telecommunication services, especially voice and data services consumed by Telefónica's customers.
- "**SIM**" means subscriber identity module, a removable intelligent card used in mobile handsets, USB modems, etc. to identify the user in the network.

- "**Voice Traffic**" means voice minutes used by Telefónica's customers over a given period, both outbound and inbound.
- "**UMTS**" means Universal Mobile Telecommunications System.
- "**VoIP**" means voice over Internet protocol.
- "**Wholesale access**" means access Telefónica provides to its competitors, who then sell services over such accesses to their residential and corporate clients.

RISK FACTORS

Any investment in the Securities is subject to a number of risks. Prior to investing in the Securities, prospective investors should carefully consider risk factors associated with any investment in the Securities, the business of the Issuer and the Guarantor and the industries in which each of them operates together with all other information contained in this Prospectus, including, in particular the risk factors described below. Words and expressions defined in the "Terms and Conditions of the 6 Year Non-Call Securities" or in the "Terms and Conditions of the 10 Year Non-Call Securities" below, or elsewhere in this Prospectus, have the same meanings in this section.

The Issuer and the Guarantor have identified in this Prospectus a number of factors which could materially adversely affect their businesses and ability to make payments due under the Securities and believes that the factors described below represent the principal risks inherent in investing in the Securities.

The following is not an exhaustive list or explanation of all risks which investors may face when making an investment in the Securities and should be used as guidance only. Additional risks and uncertainties relating to the Issuer and the Guarantor that are not currently known to the Issuer and the Guarantor, or that either currently deems immaterial, may individually or cumulatively also have a material adverse effect on the business, prospects, results of operations and/or financial position of the Issuer and the Guarantor and, if any such risk should occur, the price of the Securities may decline and investors could lose all or part of their investment. Investors should consider carefully whether an investment in the Securities is suitable for them in light of the information in this Prospectus and their personal circumstances.

Risks relating to the Issuer and the Guarantor

The risk factors set out below are applicable to the Issuer as a member of the Telefónica Group, and the Guarantor.

Risks in relation to the Group

The Telefónica Group's business is conditioned by a series of intrinsic risk factors that affect exclusively the Group, as well as a series of external factors that are common to businesses of the same sector. The main risks and uncertainties facing the Company which could affect its business, financial position, reputation, corporate image and brand and its results, are as follows:

Risks relating to the Group's Business

Worsening of the economic and political environment could negatively affect business.

Telefónica's international presence enables the diversification of its activities across countries and regions, but entails the need of considering various legislations, as well as the political and economic environments of the countries in which it operates. Any adverse developments or even just uncertainties in this regard, or possible exchange-rate or sovereign-risk fluctuations may adversely affect the business, financial position, cash flows and/or the performance of some of the Group's economic and financial indicators.

With respect to the economic environment, the Telefónica Group's business is impacted by overall economic conditions in each of the countries in which it operates. Economic conditions may adversely affect the level of demand of existing and prospective customers, as they may no longer deem critical the services offered by the Group. The main macroeconomic factors that could have an adverse impact on consumption and, accordingly, on the level of demand for the Group's services and finally, on Telefónica Group's results, are: the shortage of credit in an environment of adjustment of banks' balance sheets; the evolution of the labour market; the worsening of consumer confidence, with an increase in saving rates as an immediate consequence; or the needs for greater fiscal adjustment, which would negatively impact on the household income levels and corporate investments, expenses and revenues.

This economic risk might be significant in some European countries which are on the road to recovery but are rebounding more slowly due to financial imbalances that must continue to be corrected. According to the European Economic and Financial Affairs Council, the European economy is expected to have shrunk by 0.4% in 2013 and will only grow 1.1% in 2014, assuming, therefore, that private consumption growth

may be weak in certain cases. In this region, Telefónica Group generated 47% of the Group's total revenues in 2013 (including 22.7% in Spain, 11.7% in the UK and 8.6% in Germany).

Also, the impact of the sovereign debt crisis and the rating downgrades in certain Euro Area countries should be taken into account. Any additional deterioration in the sovereign debt markets, doubts about developments in European projects (such as implementation of the banking union project, the results of the European elections or progress towards fiscal integration), as well as further credit restrictions by the banking sector could have an adverse effect on the Telefónica's ability to access funding and/or liquidity which could have a significant adverse effect on the Group's businesses, financial position, results of operations and cash flows. In addition, the Group's business may be affected by other possible effects from the economic crisis, including a possible insolvency of key customers and suppliers.

In Latin America, the most important challenge is the exchange-rate risk in Venezuela and Argentina (with a sustained accelerated depreciation of the peso against the U.S. dollar), given the negative impact that a higher than expected depreciation in their currencies could have on cash flows from both countries. The economic outlook for the entire region suggests that growth rates will remain stable at around 3%, supported by solid domestic demand fundamentals. The international scenario, despite being not so favourable as in the past periods, will remain to have a relatively benign impact on the region, except for, among others, potential periods of volatility linked to the evolution of the developed financial markets (especially long-term interest rates in the United States affected by the U.S. Federal Reserve's intervention that are not discounted in the market), a greater than envisaged economic slowdown in Asia (a key region for Latin America), and the slow progress being made with structural reforms projects in the majority of these countries which limits potentially higher growth rates. The most significant internal macroeconomic risk factors in the region would be the very high inflation rates in Venezuela and Argentina that could lead to economic stagnation in these countries, the delicate situation of Venezuela's public finance, and the deterioration in the external accounts of countries such as Argentina, Brazil, Chile and Peru; though with very different funding outlooks for the latter three (favourable) than the first.

In relation to the political environment, the Group's investments and operations in Latin America could be affected by a series of risks related to economic, political and social factors in these countries, collectively denominated "country risk.". On this point, approximately 15% of the Group's revenues in the telephony business are generated in countries that do not have investment grade status (in order of importance Venezuela, Argentina, Ecuador, Guatemala, Nicaragua, El Salvador and Costa Rica), and other countries are only one notch away from losing this threshold. Also note that despite clear improvements in Brazil, recent announcements by the ratings agencies considering a possible downgrading of its credit rating could, depending on the extent of the downgrading, result in strong exchange-rate volatility due to an outflow of investments, especially strong in fixed-income.

Among the factors included in the concept of "country risk" are highlighted:

- government regulation or administrative policies may change unexpectedly, including changes that modify the terms and conditions of licences and concessions and their renewal (or delay their approvals) which could negatively affect the Group's interests in such countries;
- abrupt exchange-rate fluctuations mainly due to situations of high levels of inflation and "twin deficits" (in public finance and the external sector) with the resulting exchange-rate overvaluation. This movement could lead to strong exchange-rate depreciation in the context of a floating exchange rate regime, to a significant devaluation off the back of abandoning fixed exchange rates regimes, or to the introduction of varying degrees of restrictions on capital movement. For example, in Venezuela, the official U.S. dollar to bolívar fuerte exchange rate is established by the Central Bank of Venezuela and the Minister of Finance, with an alternative market for attracting foreign currency through the Sistema Complementario de Administración de Divisas (SICAD) fortnightly auctions. Additionally, the acquisition of foreign currencies by Venezuelan or Argentinean companies (in some cases) to pay foreign debt or dividends is subject to the pre-authorisation of the relevant authorities. Also, the Argentinean peso is following a sustained accelerated depreciation against the U.S. dollar;
- governments may expropriate or nationalise assets, or make adverse tax decisions, or increase their participation in the economy and in companies;

- economic-financial downturns, political instability and civil disturbances may negatively affect the Telefónica Group's operations in such countries; and
- maximum profit margins limits may be imposed in order to limit the prices of goods and services through the analysis of cost structures. Thus, in Venezuela, a maximum profit margin has been introduced that will be set annually by the Superintendence for Defense of Socioeconomic Rights.

The Group's financial condition and results of operations may be adversely affected if it does not effectively manage its exposure to foreign currency exchange rates, interest rates or financial investment risks.

At 31 December 2013, 71% of the Group's net debt (in nominal terms) had its interest rates fixed over a year, while 23% was denominated in a currency other than the euro.

To illustrate the sensitivity of financial expenses to a change in short-term interest rates at 31 December 2013: (i) a 100 basis points increase in interest rates in all currencies in which Telefónica has a financial position at that date would lead to an increase in financial expenses of €118 million, (ii) whereas a 100 basis points decrease in interest rates in all currencies except the euro, the U.S. dollar and the pound sterling (these to zero rates in order to avoid negative rates), would lead to a reduction in financial expenses of €55 million. These calculations were made assuming a constant currency and balance position equivalent to the position at that date and bearing in mind the derivative financial instruments arranged.

According to the Group's calculations, the impact on results and specifically changes in the value of a 10% depreciation of Latin American currencies against the U.S. dollar and a 10% depreciation of the rest of the currencies against the euro would result in exchange losses of €42 million, primarily due to the weakening of the bolívar fuerte and, to a lesser extent, the Argentinean peso. These calculations had been made assuming a constant currency position with an impact on profit or loss at 31 December 2013 including derivative instruments in place.

The Telefónica Group uses a variety of strategies to manage this risk, mainly through the use of financial derivatives, which themselves are also exposed to risk, including counterparty risk. Furthermore, the Group's risk management strategies may not achieve the desired effect, which could adversely affect the Group's business, financial condition, results of operations and cash flows.

Existing or worsening conditions in the financial markets may limit the Group's ability to finance, and consequently, the ability to carry out its business plan.

The performance, expansion and improvement of the Telefónica Group's networks, the development and distribution of the Telefónica Group's services and products, the development and implementation of the Company's strategic plan, as well as the development and implementation of new technologies or the renewal of licences require a substantial amount of financing.

The performance of financial markets in terms of liquidity, cost of credit, access and volatility, continues to be overshadowed by persisting uncertainty regarding certain factors such as the pace of economic recovery, the health of the international banking system and the concerns regarding the burgeoning deficits of some European countries. The worsening international financial market credit conditions caused by some of these factors could make it more difficult and more expensive to refinance existing financial debt or arrange new debt if necessary, and more difficult and costly to raise funds from the Group's shareholders, and may negatively affect the Group's liquidity. At 31 December 2013, gross financial debt scheduled to mature in 2014 amounted to €9,214 million (which includes: (i) the net position of derivative financial instruments, certain current payables and (ii) €582 million of notes with an option of early repayment and no contractual obligation to be repaid), and gross financial debt scheduled to mature in 2015 amounted to €6,802 million. Despite having covered gross debt maturities of 2014 and 2015 by available cash and lines of credit at 31 December 2013, possible difficulties to maintain the current safety margin, or the risk that this could be significantly and unexpectedly exhausted, could force Telefónica to use resources allocated for other investments or commitments for payment of its financial debt, which could have a negative effect on the Group's businesses, financial position, results of operations or cash flows.

Although the Group maintains liquidity coverage on 24-month maturities, obtaining financing on the international capital markets could also be restricted, in terms of access and cost, if Telefónica's credit ratings are revised downwards, either due to lower solvency or operating performance, or as a result of a downgrade in the rating for Spanish sovereign risk by rating agencies. Any of these situations could have a negative impact on the Group's ability to deal with debt maturities.

Moreover, market conditions could make it harder to renew existing undrawn credit lines, 10% of which, at 31 December 2013, initially mature prior to 31 December 2014.

Risks relating to the Group's Industry

The Group operates in a highly regulated industry which requires government concessions for the provision of a large part of its services and the use of spectrum, which is a scarce and costly resource.

The telecommunications sector is subject to laws and regulations in different countries, and additionally, many of the services provided require the granting of a licence, concession or official approval, which usually requires certain obligations and investments to be made, such as those relating to spectrum availability. Among the main risks of this nature are the spectrum and licences/concessions, rates, universal service regulation, fiber networks, privacy, functional separation of businesses and network neutrality.

Thus, as the Group provides most of its services under licences, authorisations or concessions, it is vulnerable to administrative bodies' decisions, such as economic fines for serious breaches in the provision of services and, eventually, revocation or failure to renew these licences, authorisations or concessions, or the granting of new licences to competitors for the provisions of services in a specific market.

The Telefónica Group pursues its licence renewals in the terms referred in their respective contractual conditions, though it cannot guarantee that it will always complete this process successfully or under the most beneficial terms for the Group. In many cases complying with certain obligations is required, including, among others, minimum specified quality standards, service and coverage conditions and capital investment. Failure to comply with these obligations could result in the imposition of fines, revision of the contractual terms, or even the revocation of the licence, authorisation or concession. Additionally, the Telefónica Group could be affected by regulatory actions carried out by the antitrust authorities. These authorisations could prohibit certain actions, such as new acquisitions or specific practices, create obligations or lead to heavy fines. Any such measures implemented by the competition authorities could result in economic and/or reputational loss for the Group, in addition to a loss of market share and/or harm to the future growth of certain businesses.

Regulation of spectrum and government concessions:

The "Digital Single Market" package of measures is currently being amended by the European Parliament to include important measures affecting, *inter alia*, spectrum regulation. Although these measures are not yet final, they could have significant implications as they include new provisions on secondary markets, criteria to apply at auctions, renewals and terms of licences, etc.

In 2015/2016, in Germany, it is expected that frequencies in the 900/1800 MHz band licences, expiring at the end of 2016, will be renewed. The German regulator has adopted a proposal decision envisaging an auction of spectrum in the 900 MHz, 1800 MHz, 700 MHz and 1500 MHz bands. Furthermore, it is proposed, for operators holding 900 MHz GSM band licences, the reservation of 2X5 MHz in this band. The aforementioned reservation entails a 99% population coverage obligation. Moreover, European and National regulators are reviewing the implications of the merger of Telefónica Germany and E-Plus, and any potential remedies or conditions. Remedies could affect the spectrum finally available. In Spain, it is expected that the previously auctioned frequencies in the 800 MHz band from the digital dividend, will be allocated on 1 January 2015. For its part, in the UK a tax rate increase for the use of the spectrum in 900 and 1800 MHz band is under discussion, which outcome is uncertain.

Main allocation criteria for the 700 MHz band (Digital Dividend II) will be defined in coming years in Europe. This could involve facing new cash outflow ahead of schedule (most likely scenario is currently seen as to have this spectrum between 2018 and 2021).

In Latin America, spectrum auctions will take place entailing potential outflows to obtain new licences or to meet the coverage requirements associated with these licences. Specifically, the following procedures are in progress or expected to take place in 2014:

- Brazil: Auction of the 700 MHz band. Allocation of frequencies in the 700 MHz band for fixed-line and mobile telephone and broadband services has been approved. However, the allocation process requires television channels currently occupying this band to be migrated and the National Telecommunications Agency (Anatel) to complete its analysis regarding spectrum interference between mobile and television services.
- Chile: Auction of the 700 MHz band.
- Ecuador: Negotiations underway to obtain additional frequencies in the 1900 MHz band.
- El Salvador: The auction of one block in the 1900 MHz band and another in the AWS band has been postponed, although this issue might be resolved in the coming months.
- Venezuela: Auction in the AWS band (1710-2170 MHz frequencies) and in the 2.5 GHz band, has been suspended.

On the other hand, negotiations to renew 850 MHz/1900 MHz licences in Colombia (where a legal action regarding the reversion of assets at the end of the licence terms is in place) and 850/1900 MHz licences in Panama are under way. In Peru, an application for partial renewal of the concessions for the provision of the fixed-line service for another five years has been made, although assurance has been given that the concession will remain in force until November 2027. Also, a new law has been enacted establishing mobile virtual network operator (MVNOs) and Rural Mobile Infrastructure Operators (RMIOs) in the Peruvian market. In Mexico, it is envisaged, in development of the constitutional reform enacted due to the "Pact for Mexico" political initiative, the creation of a wholesale network publicly owned which will offer wholesale services in the 700 MHz band, the funding and the marketing model of this project have not been determined as at the date of this Prospectus.

On the other hand, Telefónica UK was awarded two 10 MHz blocks of spectrum in the 800 MHz band in 2013 to roll out a national 4G network. In Spain, the following licence extensions have been granted: in the 900 MHz band, 4 MHz from July 2025 to December 2030 and 1 MHz from February 2015 to December 2030, likewise, in the 1800 MHz band a 20 MHz licence has been extended from 2028 to December 2030. Moreover, in 2013, Telefónica also obtained spectrum licences in Uruguay (2x5 MHz in the 1900 MHz band), Colombia (30 MHz in the AWS band) and Peru (20+20 MHz in the 1700 MHz band). In 2013 Telefónica Brazil requested the amendment of the terms of authorisation for the "L" band in order to relocate the blocks of radiofrequencies. Currently, the "L" band is located in the 3G radiofrequencies (1.9/2.1GHz). The notice of the "L" band provided for such relocation and the request ensured a more efficient use of the spectrum for Telefónica Brazil. CapEX associated with the new spectrum in 2013 amounted to €1,224 million.

In 2012, Telefónica Ireland was awarded spectrum in the 800, 900 and 1800 MHz bands. In Brazil, Telefónica was awarded a block of the 2500 MHz "X" band (20+20 MHz), including the 450 MHz band in certain states. In the spectrum auction, Telefónica Brazil had to compensate the former licencees of this bandwidth, used for multichannel multipoint distribution services. The other operators also awarded spectrum shall, in turn, compensate Telefónica Brazil. Part of these compensation requirements is being legally contested. In Venezuela, the concession agreement between Telefónica Venezolana and the Regulator for an additional 20 MHz in the 1900 MHz band was executed. Telefónica Móviles Chile, S.A. was awarded radiofrequencies for 4G technology in the 2.6 GHz band (2x20 MHz), and in Nicaragua Telefónica was granted 36 MHz in the 700 MHz band.

The Company's failure to obtain sufficient or appropriate spectrum capacity in the jurisdictions discussed above or any others in which it operates or its capacity to assume the related costs, could have an adverse impact its ability to launch and provide new services and on the Company's ability to maintain the quality of existing services, which may adversely affect the Group's financial condition, results of operations and cash flows.

Regulation of wholesale and retail charges:

In terms of roaming, the regulated "Eurotariffs" will be reduced in July 2014, as per the Regulation approved in 2012. The structural roaming solutions which could lead to a price decrease in the intra-European Union roaming services, will also take effect in July 2014. Furthermore, the packet of "Digital Single Market" measures mentioned above also includes a proposal to eliminate European Union roaming charges in July 2016 as well as international charges.

The decreases in wholesale mobile network termination rates in Europe are also noteworthy. In the UK, wholesale mobile network termination rates will be reduced to 0.845 pence/minute from 1 April 2014 (representing a 0.3% reduction compared to the current rates), while the termination rate in Germany was set at 0.0179 euro/minute as from 31 December 2013 (3.24% lower than the previous termination rates). The European Commission has requested that the German regulator withdraw or amend its latest decision on mobile termination rates. There is a risk that the European Commission will initiate infringement proceedings against Germany, and rates may be further reduced. In Spain, the schedule for reducing mobile network termination rates has reached the target rate (0.0109 euro/minute) in July 2013, representing close to 61% lower than the wholesale prices in force until that date. As from July 2013, the target price reached will remain in force until new target prices are set. The Spanish regulator has yet to make its decision on this matter. Based on a High Court ruling in Ireland, a mobile termination rate of €0.026 was provisionally imposed (more favourable than the figure initially proposed by the regulator), applicable from 1 July 2013 (representing 29.35% lower the previous termination rates). The Irish regulator is also developing a more adverse cost model based on long-run incremental cost (LRIC) price calculation, which is expected to be announced in July 2014.

Also, in Latin America, there are moves to review mobile termination rates leading to these being reduced. Thus, for example, developments in Mexico are among the most relevant, where the declaration of dominant operators in the telecommunications market is expected to lead to asymmetric regulatory measures that must be set. The Company's competitive position may benefit to a greater or lesser extent depending on the scope of these measures. Telefónica México has filed an administrative appeal against the 2011 resolutions of the Federal Telecommunications Commission of México (Cofotel) regarding mobile network termination rates (representing a 61% reduction compared to the previous rates). As of the date of this Prospectus, no ruling has been made on this appeal. Once these appeals have been concluded, the rates applied may be further reduced retroactively. As of the date of this Prospectus, Cofotel has not approved the termination rates for 2012, 2013, or 2014.

In Brazil, in October 2011, the regulator (Anatel) approved the fixed-mobile rate adjustment regulation, which provides a progressive reduction of these rates until 2014 through a reduction factor, which will be deducted from the inflation, and implying a reduction of approximately 29% in 2012-2014. However, the Plano Geral de Metas de Competição (PGMC) of the end of 2012 extended application of the reduction to 2015 and amended the rates for 2014 and 2015 (75% of the 2013 rate in 2014 and 50% of the 2013 rate in 2015). A draft law has been prepared in Brazil to abolish the basic telephony service monthly fee. "Price protection" practices (reimbursement of price differences of a product to customers if this falls within a relative short period of time) may also have a negative effect, both in economic and image terms.

In Chile, a process to set new fixed-line termination charges is ongoing. A Tariff Decree has been passed for mobile networks covering the 2014-2019 five-year period. The new Tariff Decree entered into effect on 25 January 2014 and implies a reduction of 73.4% with respect to the previous rates. In Ecuador the rate-related risks also concern a reduction in rural and urban telephony charges, a reimbursement of top-up balances, as well as rounding to the nearest minute.

The implementation of the Enabling Act (*Ley Habilitante*) in Venezuela also confers full powers to the President to implement price controls measures, and it is therefore expected that it will not be possible to raise Movistar retail rates in line with high Venezuela inflation. In relation to mobile termination rates with the national operator of reference, these have been reduced 6% compared to the previous rates.

In Peru, the previously applicable rate was reduced by 24.24% in October 2013.

In Colombia, a decision was adopted establishing a gradual reduction for termination mobile rates. Regarding the termination model for time, the reduction for 2014 is 19.8 % and 24.6% for 2015. For the capacity model the reduction will be 10.9% for 2014 and 12.3% for 2015. In relation with fix networks (for extended local networks) the reduction will be 50% for 2014 and 100% for 2015.

Regulation of universal services:

The European Commission on its formal obligation to review the Universal Service Directive will launch a public consultation whose objective will be to modify the scope of their obligations and include, at a European level, far higher broadband speeds than are currently provided. Depending on the terms set forth in the new regulation, implementation at a local level could lead to higher costs for both the universal service provider and the operators forced to finance the Universal Service.

The regulator in Brazil has modified the universal service targets. This represents a risk on the Company's positive balance resulted from the fulfilment of 2003 universal service targets, whose implementation was less costly than the initially established targets, leaving a positive balance for the Company.

The new requirements that cause this positive balance could apply until 2025, and extend beyond on issues such as, for example, rural telephony services and the expansion of the backhaul network. Rural telephony services are another risk in Brazil given the obligations arising from the switched fixed-line telephone services model and the obligations to provide mobile coverage in certain rural areas of the country.

Regulation of fiber networks:

It is expected that in 2014 the Spanish National Competition Authority (*Comisión Nacional de los Mercados y la Competencia*) will study broadband market regulation in Spain. This could increase Telefónica's regulatory obligations in Spain, especially wholesale market obligations concerning access to fiber networks, and its pricing.

Regulations on privacy:

In Europe, a new Data Protection Regulation is in the pipeline before the end of the European legislative term in place as at the date of this Prospectus (spring 2014). This could lead to certain critical provisions laid down in the current draft of the Regulation (presently under debate) being worded in such a way that stops or hinders Telefónica from launching some services, that focus on the processing of personal data.

Regulation of functional separation:

The new principles established in Europe's common regulatory framework, adopted in 2009 and transposed in the national legislation of each Member State in which Telefónica operated during 2011 and 2012, could result in greater regulatory pressure on the local competitive environment. Specifically, this framework supports the possibility of national regulators, in specific cases and under exceptional conditions, forcing operators with significant market power and vertically-integrated operators to separate their wholesale and retail businesses at a functional level. They would therefore be required to offer equal wholesale terms to third-party operators that acquire these products.

Regulation of network neutrality:

In Europe, application of the current regulatory framework means that it is likely that during 2014, the Body of European Regulators for Electronic Communications (BEREC) and national regulators will strengthen their supervision of operators with regard to blocking of access, discrimination of applications or Internet service quality. The European Parliament and the Council are simultaneously debating the draft of the European Digital Market Regulation proposed by the European Commission, in particular concerning network neutrality, network management or differentiation of Internet access service characteristics. All of them are aspects of great importance that have a direct impact on potential business models that can be developed in the future.

As at the date of this Prospectus, Telefónica has presence in countries where net neutrality has already been ruled, such as Chile and Colombia, but this remains a live issue and with varying degree of development in the other countries. In Germany, the Economy Minister published a draft law on 20 June 2013 to regulate neutrality, especially with regard to blocking and discrimination of content and Internet services. The text is pending approval by parliament in 2014 after the new government was sworn in during December 2013.

In Brazil, the Civil Rights Framework for Internet Governance is being debated by Congress and is expected to be approved in the first quarter of 2014. It includes policies on the Internet such as network

neutrality. Activities regarding net neutrality have been, as of the date of this Prospectus, focused in supervision of the quality of the services: in October 2011, Anatel approved the regulations of the Service Quality of Multimedia Communication Service (including fixed Internet) and Personal Mobile Service (including mobile Internet). The aforementioned regulations regulate the measurement made from independent entities on quality delivered and perceived by ISPs to customers.

If changes to regulation such as those described above, or otherwise, occur in the various jurisdictions where the Telefónica Group operates, it could have a material adverse effect its business and results of operations.

Customers' perceptions of services offered by the Company may put it at a disadvantage compared to competitors' offerings.

Customers' perceptions of the services and products offered are critical to operating in highly-competitive markets. The ability to predict and respond to the changing needs and demands of customers affects the Company's competitive position relative to other technology sector companies, and its ability to extract the value generated during this process of transformation. Failure to do so appropriately could have an adverse impact on the Group's financial condition, results of operations and cash flows.

Company may not be able to adequately foresee and respond to technological changes and sector trends.

In a sector characterised by rapid technological change, it is essential to be able to offer the products and services demanded by the market, and consider the impacts of changes in the life cycle of technical assets, finely adjust margins, and select the right investments to make.

The Telefónica Group operates in markets that are highly competitive and subject to constant technological development. Therefore, as a consequence of both characteristics, it is subject to the effects of actions by competitors in these markets and to its ability to anticipate and adapt to constant technological changes taking place in the industry.

To compete effectively in these markets, the Telefónica Group needs to successfully market its products and services and respond to both commercial actions by competitors and other competitive factors affecting these markets, anticipating and adapting promptly to technological changes, changes in consumer preferences and general economic, political and social conditions. Failure to do so appropriately could have an adverse impact on the Group's financial condition, results of operations and cash flows.

New products and technologies arise constantly, while the development can render obsolete the products and services the Telefónica Group offers and the technology it uses. This means that Telefónica must invest in the development of new products, technology and services so it can continue to compete effectively with current or future competitors, and which may result in the decrease of the Group's profits and revenue margins. In this respect, margins from traditional voice and data business are shrinking, while new sources of revenues are deriving from mobile Internet and connectivity services that are being launched. Research and development costs amounted to €1,046 million and €1,071 million in 2013 and 2012, respectively, representing 1.8% and 1.7% of the Group's consolidated revenue, respectively. One technology that telecommunications operators, including Telefónica (in Spain and Latin America), are focused on is the new FTTx-type network, which offers broadband access using optical fiber with superior services, such as Internet speed of up to 100MB or HD television services. However, substantial investment is required to deploy these networks, which entails fully or partially substituting copper loop access with optic fiber. An increasing demand for the capabilities offered by these new networks to end users exist, however, the high level of the investments requires a continuous analysis of the return on investment.

The explosion of the digital market, and entry of new players in the communications market, such as Mobile Virtual Network Operators (MVNOs), Internet companies or device manufacturers, may cause the loss of value of certain assets, and affect its ability to generate income. Therefore, it is necessary to update the business model, encouraging the pursuit of incomes and additional efficiencies to those followed traditionally. Failure to do so appropriately could have an adverse impact on the Group's financial condition, results of operations and cash flows.

In addition, the ability of the Telefónica Group's IT systems (operational and backup) to respond the Company's operating requirements is a key factor to be taken into account with respect to the commercial development, customer satisfaction and business efficiency.

The Company depends on the suppliers.

The existence of critical suppliers in the supply chain, especially in areas such as network infrastructure, information systems or handsets, with a high concentration in a small number of suppliers, poses risks that may affect the operation, and may cause contingencies or damages to the Company's image in the event that inappropriate practices were produced by a participant in the supply chain.

As of 31 December 2013, the Telefónica Group depends on 8 handset suppliers and 12 network infrastructure suppliers, which together accounted for 80% of orders. These suppliers may, among other things, extend delivery times, raise prices and limit supply due to their own shortages and business requirements.

If these suppliers fail to deliver products and services to the Telefónica Group on a timely basis, it could jeopardise network deployment and expansion plans, which in some cases could adversely affect the Telefónica Group's ability to satisfy its licence terms and requirements or have an adverse impact on the Group's business, financial condition, results of operations and cash flows.

Unanticipated network interruptions can lead to quality loss or the interruption of the service.

Unanticipated network interruptions as a result of system failures, including those due to network, hardware or software or cyber-attacks, which affect the quality of or cause an interruption in the Telefónica Group's service, could lead to customer dissatisfaction, reduced revenues and traffic, costly repairs, penalties or other measures imposed by regulatory authorities and could harm the Telefónica Group's image and reputation.

Telefónica attempts to mitigate these risks through a number of measures, including backup systems and protective systems such as firewalls, virus scanners and other physical and logical security. However, these measures are not always effective. Although the Telefónica Group has insurance policies to cover this type of incidents and risks, these policies may not be sufficient to cover all possible monetary losses, although the claims and loss in revenue caused by service interruptions to date have been covered by these policies.

The telecommunications industry may be affected by the possible effects of electromagnetic fields, emitted by mobile devices and base stations, may have on human health.

In some countries, there is a concern regarding potential effects of electromagnetic fields, emitted by mobile devices and base stations, on human health. This public concern has caused certain governments and administrations to take measures that have hindered the deployment of the infrastructures necessary to ensure quality of service, and affected the deployment criteria of new networks and digital services such as smart meters development.

There is a consensus between various expert groups and public health agencies, including the World Health Organisation (WHO), who claim that at the moment there have not been established risks for exposure to low frequency signals in mobile communications. The scientific community is still investigating this issue especially on mobile devices. Exposure limits for radio frequency suggested in the guidelines of the Protection of Non-Ionising Radiation Protection Committee (ICNIRP) have been internationally recognised. The mobile industry has adopted these exposure limits and works to request authorities worldwide to adopt these standards.

Society's worries about radiofrequency emissions may discourage the use of mobile devices and new digital services, which could cause the public authorities to implement measures restricting where transmitters and cell sites can be located, how they operate, the use of the Group's mobile telephones and the massive deployment of smart meters and other products using mobile technology. This could lead to the Company being unable to expand or improve its mobile network.

The adoption of new measures by governments or administrations or other regulatory interventions in this respect, and any future assessment on the adverse impact of electromagnetic fields on health, may negatively affect the business, financial conditions, results and cash flows of the Telefónica Group.

Possible regulatory, business, economic or political changes could lead to asset impairment.

The Telefónica Group reviews on an annual basis, or more frequently when the circumstances require it, the value of assets and cash-generating units, to assess whether their carrying values can be supported by the future expected cash flows, including, in some cases synergies allowed for in acquisition cost. Potential changes in the regulatory, business, economic or political environment may result in the need to introduce changes to estimates made and to recognise impairment losses in goodwill, intangible assets or fixed assets. Although the recognition of impairments of property, plant and equipment, intangible assets and financial assets results in a non-cash charge on the income statement, it could adversely affect the results of the Telefónica Group's operations. In this respect, the Telefónica Group has experienced impairment losses on certain of its investments, affecting the results of the year in which they were made. Thus, with respect to the investment in Telco, S.p.A. ("**Telco**"), value adjustments were made in fiscal years 2012 and 2013 for €1,277 million and €267 million, respectively. Also in 2012, the revision of the value of Telefónica operations in Ireland, resulted in a negative impact of €527 million.

Telefónica Group's networks carry and store huge volumes of confidential, personal and corporate data, and its Internet access and hosting services may lead to claims for illegal or illicit use of the Internet.

Telefónica Group's networks carry and store huge volumes of confidential, personal and business data, through both voice and data traffic. Telefónica stores increasing quantities and types of customer data in both business and consumer segments. Despite best efforts to prevent it, Telefónica may be found liable for the loss, transfer, or inappropriate modification of the customer data or general public data stored on its servers or transmitted through its networks which could involve many people and have an impact on the Group's reputation, or lead to legal claims and liabilities that are difficult to measure in advance.

Telefónica's Internet access and hosting servers could lead to claims for illegal or unlawful use of the Internet. Telefónica, like other telecommunications providers, may be held liable for the loss, transfer or inappropriate modification of the customer data stored on its servers or carried by its networks.

In most countries in which Telefónica operates, the provision of its Internet access and hosting services (including the operation of websites with shelf-generated content) are regulated under a limited liability regime applicable to the content that it makes available to the public as a technical service provider, particularly content protected by copyright or similar laws. However, regulatory changes have been introduced imposing additional obligations on access providers (such as blocking access to a website) as part of the struggle against some illegal or illicit uses of the Internet, notably in Europe.

Telefónica and Telefónica Group companies are party to lawsuits, tax claims, antitrust and other legal proceedings.

Telefónica and Telefónica Group companies are party to lawsuits, tax claims and other legal proceedings in the ordinary course of their businesses, the financial outcome of which is unpredictable. An adverse outcome or settlement in these or other proceedings could result in significant costs and may have a material adverse effect on the Group's business, financial condition, results of operations, reputation and cash flows. In particular, regarding tax and antitrust claims, Telefónica Group has open judicial procedures in Peru concerning the clearance of previous years' income tax, which contentious-administrative appeal is currently on its way; as well as in Brazil CADE's (*Conselho Administrativo de Defesa Econômica*) as regards the acquisition of a 50% stake in Vivo and tax open procedures, primarily relating to the CIMS (tax on telecommunication services).

Risks relating to Withholding

Risks in relation to Spanish Taxation

With respect to any payment of interest under the Guarantee, the Guarantor is required to receive certain information relating to the Securities. If such information is not received by the Guarantor in a timely manner, the Guarantor will be required to apply Spanish withholding tax to any payment of interest (as this term is defined under "*Taxation — Spanish Tax — Payments made by the Guarantor*") in respect of the relevant Securities.

Under Spanish Law 13/1985 and Royal Decree 1065/2007, each as amended, payments of interest in respect of the Securities will be made without withholding tax in Spain provided that the Fiscal Agent

provides the Guarantor in a timely manner with a certificate containing certain information in accordance with section 44 paragraph 5 of the Royal Decree 1065/2007 relating to the Securities.

This information must be provided by the Fiscal Agent to the Guarantor, before the close of business on the Business Day (as defined in the Terms and Conditions of each series of Securities) immediately preceding the date on which any payment of interest, principal or of any amounts in respect of the early redemption of the Securities (each a "**Payment Date**") is due.

The Issuer, the Guarantor and the Fiscal Agent have arranged certain procedures to facilitate the collection of information concerning the Securities. If, despite these procedures, the relevant information is not received by the Guarantor on each Payment Date, the Guarantor will withhold tax at the then-applicable rate (currently 21 per cent.) from any payment of interest in respect of the relevant Securities. Neither the Issuer nor the Guarantor will pay any additional amounts with respect to any such withholding.

The Fiscal Agency Agreement provides that the Fiscal Agent will, to the extent applicable, comply with the relevant procedures to deliver the required information concerning the Securities to the Guarantor in a timely manner.

These procedures may be modified, amended or supplemented, among other reasons, to reflect a change in applicable Spanish law, regulation, ruling or an administrative interpretation thereof. None of the Issuer, the Guarantor or the Joint Bookrunners assumes any responsibility therefor.

Royal Decree 1145/2011, of 29 July which amends Royal Decree 1065/2007, of 27 July provides that any payment of interest made under securities originally registered in a non-Spanish clearing and settlement entity recognised by Spanish legislation or by the legislation of another OECD country will be made with no withholding or deduction from Spanish taxes provided that the relevant paying agent submits in a timely manner certain information about the Securities to the Issuer. In the opinion of the Guarantor, any payment of interest under the Guarantee will be made without deduction or withholding of taxes in Spain provided that the relevant information about the Securities is timely submitted by the Fiscal Agent to the Guarantor, notwithstanding the information obligations of the Guarantor under general provisions of Spanish tax legislation, by virtue of which identification of Spanish tax resident investors may be provided to the Spanish tax authorities (see "*Taxation — Spanish Tax — Payments made by the Guarantor*").

Risks related to the structure of the Securities

The Issuer's obligations under the Securities and the Coupons are subordinated.

The Issuer's obligations under the Securities will be unsecured and subordinated obligations of the Issuer and will rank junior to the claims of unsubordinated and other subordinated creditors of the Issuer, except for subordinated creditors whose claims are expressed to rank *pari passu* with the Securities. See Condition 2 (*Status and Subordination of the 6 Year Non-Call Securities and Coupons*) of the Terms and Conditions of the 6 Year Non-Call Securities and Condition 2 (*Status and Subordination of the 10 Year Non-Call Securities and Coupons*) of the Terms and Conditions of the 10 Year Non-Call Securities, respectively. By virtue of such subordination, payments to a Holder of Securities will, in the event of an Issuer Winding-up (as described in the relevant Conditions) only be made after, and any set-off by a Holder of Securities shall be excluded until, all obligations of the Issuer resulting from higher ranking claims have been satisfied. A Holder of Securities may therefore recover less than the holders of unsubordinated or other subordinated liabilities of the Issuer. Subject to applicable law, no Holder may exercise or claim any right of set-off in respect of any amount owed to it by the Issuer arising under or in connection with the Securities and each Holder shall, by virtue of being the Holder of any Security, be deemed to have waived all such rights of set-off. Although subordinated debt securities may pay a higher rate of interest than comparable debt securities which are not subordinated, there is a real risk that an investor in subordinated securities such as the Securities will lose all or some of his investment should the Issuer become insolvent.

The Guarantee is a subordinated obligation.

The Guarantor's obligations under the Guarantee will be unsecured and subordinated obligations of the Guarantor. In the event of the Guarantor being declared in insolvency ("*concurso*") under Spanish

Insolvency Law, the Guarantor's obligations under the Guarantee will be subordinated in right of payment to the prior payment in full of all other liabilities of the Guarantor, except for obligations which rank equally with or junior to the Guarantee. See Condition 3 (*Guarantee, Status and Subordination of the Guarantee*) of the Terms and Conditions of the 6 Year Non-Call Securities and of the Terms and Conditions of the 10 Year Non-Call Securities, respectively.

Holders of the Securities are advised that unsubordinated liabilities of the Guarantor may also arise out of events that are not reflected on the balance sheet of the Guarantor including, without limitation, the issuance of guarantees on an unsubordinated basis. Claims made under such guarantees will become unsubordinated liabilities of the Guarantor that in the insolvency of the Guarantor will need to be paid in full before the obligations under the Guarantee may be satisfied.

There are no events of default under the Securities.

The Conditions of each series of Securities do not provide for events of default allowing acceleration of the Securities if certain events occur. Accordingly, if the Issuer or the Guarantor fails to meet any obligations under the Securities or the Guarantee, as the case may be, including the payment of any interest, investors will not have the right to require the early redemption of principal. Upon a payment default, the sole remedy available to the Holders for recovery of amounts owing in respect of any payment of principal or interest on the Securities will be the institution of proceedings to enforce such payment. Notwithstanding the foregoing, in no event shall the Issuer or the Guarantor, by virtue of the institution of any such proceedings, be obliged to pay any sum or sums sooner than the same would otherwise have been payable by it.

The Securities are undated securities.

The Securities are undated securities, with no specified maturity date. The Issuer is under no obligation to redeem or repurchase the Securities at any time and the Holders have no right to require redemption of the Securities. Therefore, prospective investors should be aware that they may be required to bear the financial risks of an investment in the Securities for an indefinite period of time and may not recover their investment in the foreseeable future.

The Issuer may redeem the Securities under certain circumstances.

Holders should be aware that the Securities may be redeemed at the option of the Issuer in whole, but not in part, at their principal amount (plus any accrued and outstanding interest and any outstanding Arrears of Interest) on the First and Reset Date and on any Interest Payment Date thereafter (in each case, as defined in the Terms and Conditions of the 6 Year Non-Call Securities and the Terms and Conditions of the 10 Year Non-Call Securities, respectively).

The redemption at the option of the Issuer may affect the market value of the Securities. During any period when the Issuer may elect to redeem the Securities, the market value of the Securities generally will not rise substantially above the price at which they can be redeemed.

The Issuer may be expected to redeem the Securities when its cost of borrowing is lower than the interest rate on the Securities. At those times, an investor generally would not be able to reinvest the redemption proceeds at an effective interest rate as high as the interest rate on the Securities being redeemed and may only be able to do so at a significantly lower rate of return. Potential investors should consider reinvestment risk in light of other investments available at that time.

The Securities are also subject to redemption in whole, but not in part, at the Issuer's option upon the occurrence of an Accounting Event, a Capital Event, a Tax Event, a Withholding Tax Event or a Substantial Purchase Event (each as defined in Condition 17 (*Definitions*) of the Terms and Conditions of the 6 Year Non-Call Securities and of the Terms and Conditions of the 10 Year Non-Call Securities, respectively). The relevant redemption amount may be less than the then current market value of the Securities.

The Issuer may redeem the Securities after a Tax Event relating to an intra-group loan.

The net proceeds of the issue of the Securities will be on-lent by the Issuer to the Guarantor pursuant to a Subordinated Loan (as defined in the Conditions of the relevant Securities). The Issuer may redeem the Securities in certain circumstances, including if, as a result of a Tax Law Change (as defined in the

Conditions of the relevant Securities), in respect of (i) the Issuer's obligation to make any payment under the Securities (including any Interest Payment) on the next following Interest Payment Date; or (ii) the obligation of the Guarantor to make any payment in favour of the Issuer under the Subordinated Loan on the next following due date for such payment, the Issuer or the Guarantor (as the case may be) would no longer be entitled to claim a deduction in respect of computing its tax liabilities in The Netherlands or in Spain (as the case may be), or such entitlement is materially reduced.

The direct connection between a Tax Event and the Subordinated Loan may limit the Issuer's ability to prevent the occurrence of a Tax Event, and may increase the possibility of the Issuer exercising its option to redeem the Securities upon the occurrence thereof.

The Issuer has the right to defer interest payments on the Securities.

The Issuer may, at its discretion, elect to defer (in whole or in part) any payment of interest on the Securities. Any such deferral of interest payment shall not constitute a default for any purpose. See Condition 5 (*Optional Interest Deferral*) of the Terms and Conditions of the 6 Year Non-Call Securities and of the Terms and Conditions of the 10 Year Non-Call Securities, respectively. Any interest in respect of the Securities the payment of which is deferred will, so long as the same remains outstanding, constitute Arrears of Interest. Arrears of Interest will be payable as outlined in Conditions 5(b) and 5(c) of the Terms and Conditions of the 6 Year Non-Call Securities and of the Terms and Conditions of the 10 Year Non-Call Securities, respectively. While the deferral of payment of interest continues, the Issuer is not prohibited from making payments on any instrument ranking senior to the Securities and in such event, the Holders are not entitled to claim immediate payment of interest so deferred.

As a result of the interest deferral provision of the Securities, the market price of the Securities may be more volatile than the market prices of other debt securities on which original issue discount or interest payments are not subject to such deferrals and may be more sensitive generally to adverse changes in the Issuer's and/or the Guarantor's financial condition. Investors should be aware that any deferral of interest payments may have an adverse effect on the market price of the Securities.

Changes in rating methodologies may lead to the early redemption of the Securities.

S&P, Moody's and Fitch (in each case as defined in the Conditions of the relevant series of Securities) may change their rating methodology or may apply a different set of criteria after the Issue Date (due to changes in the rating previously assigned to the Issuer and/or the Guarantor or to any other reasons), and as a result the Securities may no longer be eligible for the same or a higher amount of "equity credit" attributable to the Securities at the date of their issue, in which case the Issuer may redeem all of the Securities (but not some only), as provided in Condition 6(e) (*Redemption and Purchase – Redemption for Rating Reasons*) of the Terms and Conditions of the 6 Year Non-Call Securities and of the Terms and Conditions of the 10 Year Non-Call Securities, respectively.

No limitation on issuing senior or pari passu securities or other liabilities.

There is no restriction on the amount of securities or other liabilities which the Issuer or the Guarantor may issue, incur or guarantee and which rank senior to, or *pari passu* with, the Securities or the Guarantee (as the case may be). The issue of any such securities, the granting of any such guarantees or the incurrence of any such other liabilities may reduce the amount (if any) recoverable by Holders on the insolvency, winding-up, liquidation or dissolution of the Issuer or the Guarantor (as the case may be) and/or may increase the likelihood of a deferral of Interest Payments under the Securities.

If the Issuer's and/or the Guarantor's financial condition were to deteriorate, the Holders could suffer direct and materially adverse consequences, including loss of interest and, if the Issuer and/or the Guarantor were liquidated (whether voluntarily or not), the Holders could suffer loss of their entire investment.

Fixed rate securities have a market risk.

A holder of a security with a fixed interest rate is exposed to the risk that the price of such security falls as a result of changes in the current interest rate on the capital market (the "**Market Interest Rate**"). While the nominal interest rate of a security with a fixed interest rate is fixed during the life of such security or during a certain period of time, the Market Interest Rate typically changes on a daily basis. A change of the Market Interest Rate causes the price of such security to change. If the Market Interest Rate increases,

the price of such security typically falls. If the Market Interest Rate falls, the price of a security with a fixed interest rate typically increases. Investors should be aware that movements of the Market Interest Rate can adversely affect the price of the Securities and can lead to losses for the Holders if they sell the Securities.

Interest rate reset may result in a decline of yield.

A Holder with a fixed interest rate that will be reset during the term of the Securities is exposed to the risk of fluctuating interest rate levels and uncertain interest income. Fluctuating interest rate levels make it impossible to determine the yield of such securities in advance.

Any decline in the credit ratings of the Issuer and/or the Guarantor may affect the market value of the Securities.

The Securities have been assigned a rating by S&P, Moody's and Fitch. The rating granted by each of S&P, Moody's and Fitch or any other rating assigned to the Securities may not reflect the potential impact of all risks related to structure, market and other factors that may affect the value of the Securities. A credit rating is not a recommendation to buy, sell or hold securities and may be revised or withdrawn by the rating agency at any time. A credit rating is not a statement as to the likelihood of deferral of interest on the Securities. Holders have a greater risk of deferral of interest payments than persons holding other securities with similar credit ratings but no, or more limited, interest deferral provisions.

In addition, each of S&P, Moody's and Fitch, or any other rating agency may change its methodologies for rating securities with features similar to the Securities in the future. This may include the relationship between ratings assigned to an issuer's senior securities and ratings assigned to securities with features similar to the Securities sometimes called "notching". If the rating agencies were to change their practices for rating such securities in the future and the ratings of the Securities were to be subsequently lowered, this may have a negative impact on the trading price of the Securities.

Risks arising in connection with the Dutch Insolvency Law

Pursuant to Council Regulation (EC) no. 1346/2000 on insolvency proceedings (the "**EU Insolvency Regulation**"), the court that shall have jurisdiction to open insolvency proceedings in relation to a company will be the court of the EU Member State (other than Denmark) where the company concerned has its "centre of main interest" (as that term is used in Article 3(1) of the EU Insolvency Regulation). The determination of where any such company has its "centre of main interest" is a question of fact on which the courts of the different EU Member States may have differing and even conflicting views.

Furthermore, the term "centre of main interest" is not a static concept and may change from time to time. Although there is a rebuttable presumption under Article 3(1) of the EU Insolvency Regulation that any such company has its "centre of main interest" in the Member State in which it has its registered office, Preamble 13 of the EU Insolvency Regulation states that the "centre of main interest" of a debtor should correspond to the place where the debtor conducts the administration of its interests on a regular basis and is therefore ascertainable by third parties. In that respect, factors such as where board meetings are held and the perception of the company's creditors as regards the centre of the company's business operations may all be relevant in the determination of the place where the company has its "centre of main interest".

If the centre of main interest of a company is and will remain located in the state in which it has its registered office, the main insolvency proceedings with respect to the company under the EU Insolvency Regulation would be commenced in such jurisdiction and accordingly a court in such jurisdiction would be entitled to commence the types of insolvency proceedings referred to in Annex A to the EU Insolvency Regulation. Insolvency proceedings opened in one EU Member State under the EU Insolvency Regulation are to be recognised in the other EU Member States (other than Denmark), although secondary proceedings may be opened in another EU Member State. If the "centre of main interest" of a debtor is in one EU Member State (other than Denmark), under Article 3(2) of the EU Insolvency Regulation, the courts of another EU Member State (other than Denmark) have jurisdiction to open "territorial proceedings" only in the event that such debtor has an "establishment" in the territory of such other EU Member State. The effects of those territorial proceedings are restricted to the assets of the debtor situated in the territory of such other EU Member State. If the company does not have an establishment in any other EU Member State, no court of any other EU Member State has jurisdiction to open territorial proceedings with respect to such company under the EU Insolvency Regulation.

In the event that the Issuer experiences financial difficulty, it is not possible to predict with certainty in which jurisdiction or jurisdictions insolvency or similar proceedings would be commenced or the outcome of such proceedings. Applicable insolvency laws may affect the enforceability of the obligations of the Issuer.

Where a company (incorporated in the Netherlands or elsewhere) has its "centre of main interest" or an "establishment" in the Netherlands, it may be subjected to insolvency proceedings in this jurisdiction. This is particularly relevant for the Issuer, which has its corporate seat (*statutaire zetel*) in Amsterdam, the Netherlands, and is therefore presumed (subject to proof to the contrary) to have its "centre of main interests" in the Netherlands.

There are two primary insolvency regimes under Dutch law. The first, moratorium of payments (*surseance van betaling*), is intended to facilitate the reorganisation of a debtor's indebtedness and enable the debtor to continue as a going concern. The second, bankruptcy (*faillissement*), is primarily designed to liquidate and distribute the proceeds of the assets of a debtor to its creditors. Both insolvency regimes are set forth in the Dutch Bankruptcy Act. The consequences of both proceedings are roughly equal from the perspective of a creditor, with creditors being treated on a *pari passu* basis subject to exceptions. A general description of the principles of both insolvency regimes is set forth below.

Under Dutch law secured creditors (and in case of suspension of payment also preferential creditors (including tax and social security authorities)) may enforce their rights against assets of the company to satisfy their claims as if there were insolvency proceedings. A recovery under Dutch law could, therefore, involve a sale of assets that does not reflect the going concern value of the debtor. Consequently, a creditor's potential recovery could be reduced in Dutch insolvency proceedings.

Any pending executions of judgments against the debtor will be suspended by operation of law when suspension of payments is granted and terminate by operation of law when bankruptcy is declared. In addition, all attachments on the debtor's assets will cease to have effect upon the suspension of payments having become definitive, a composition having been ratified by the court or the declaration of bankruptcy (as the case may be) subject to the ability of the court to set an earlier date for such termination.

In a suspension of payments and bankruptcy, a composition (*akkoord*) may be offered to creditors. A composition will be binding on all unsecured and non-preferential creditors if it is (i) approved by a simple majority of the creditors being present or represented at the creditors' meeting, representing at least 50 per cent of the amount of the claims that are admitted for voting purposes, and (ii) subsequently ratified (*gehomologeerd*) by the Dutch courts. Consequently, Dutch insolvency laws could preclude or inhibit the ability of the holders of the Securities to effect a restructuring and could reduce the recovery of a holder of Securities.

Claims against a company subject to Dutch insolvency proceedings will have to be verified in the insolvency proceedings in order to be entitled to vote and, in a bankruptcy liquidation, to be entitled to distributions. "Verification" under Dutch law means, in the case of suspension of payments, that the treatment of a disputed claim for voting purposes is determined and, in the case of a bankruptcy, that the value of the claim is determined and whether and to what extent it will be admitted in the insolvency proceedings. The valuation of claims that would not otherwise have been payable at the time of the proceedings may be based on a net present value analysis. Unless secured by a pledge or a mortgage, interest accruing after the date on which insolvency proceedings are opened cannot be verified. Where interest accrues after the date of opening of the proceedings, it can be admitted *pro memoria*.

The existence, value and ranking of any claims submitted by the holders of the Securities may be challenged in the Dutch insolvency proceedings. Generally, in a creditors' meeting (*verificatievergadering*), the receiver in bankruptcy, the administrator in suspension of payments proceedings, the insolvent debtor and all verified creditors may dispute the verification of claims of other creditors. Creditors whose claims or value thereof are disputed in the creditors' meeting may be referred to separate court proceedings (*renvooiprocedure*) in bankruptcy, while in suspension of payments the court will decide how a disputed claim will be treated for voting purposes. These situations could cause holders of Securities to recover less than the principal amount of their Securities. *Renvooi* procedures could also cause payments to the holders of Securities to be delayed compared to holders of undisputed claims.

The Dutch Bankruptcy Act does not in itself recognise the concept of classes of creditors. Remaining amounts, if any, after satisfaction of the secured and the preferential creditors are distributed among the unsecured non-preferential creditors, who will be satisfied on a *pro rata* basis. Contractual subordination may to a certain extent be given effect in Dutch insolvency proceedings, with the actual effect largely depending on the way such subordination is construed.

Secured creditors may enforce their rights against assets of the debtor to satisfy their claims under a Dutch bankruptcy as if there is no bankruptcy. As in moratorium of payments proceedings, the court may order a "cooling down period" for a maximum of four months during which enforcement actions by secured creditors are barred unless such creditors have obtained leave for enforcement from the supervisory judge. Further, a receiver in bankruptcy can force a secured creditor to enforce its security interest within a reasonable period of time, failing which the receiver will be entitled to sell the secured assets, if any, and the secured creditor will have to share in the bankruptcy costs. Excess proceeds of enforcement must be returned to the bankrupt estate; they may not be set-off against an unsecured claim of the secured creditor in the bankruptcy. Such setoff is allowed prior to the bankruptcy, although a set-off prior to bankruptcy may be subject to clawback in the case of fraudulent conveyance or bad faith in obtaining the claim used for set-off.

Under Dutch law, a legal act performed by a person (including, without limitation, an agreement pursuant to which it guarantees the performance of the obligations of a third party or agrees to provide or provides security for any of its or a third party's obligations, enters into additional agreements benefiting from existing security and any other legal act having a similar effect) can be challenged in an insolvency proceeding or otherwise and may be nullified by any of its creditors or its receiver in bankruptcy, if (a) it performed such act without an obligation to do so (*onverplicht*), (b) the creditor concerned or, in the case of its bankruptcy, any creditor was prejudiced as a consequence of the act, and (c) at the time the act was performed both it and (unless the act was for no consideration (*om niet*)) the party with or towards which it acted, knew or should have known that one or more of its creditors (existing or future) would be prejudiced. In addition, in the case of a person's bankruptcy, the receiver in bankruptcy may nullify its performance of any due and payable obligation (including (without limitation) an obligation under a guarantee or to provide security for any of its or a third party's obligations) if (i) the recipient of the payment or performance knew, at the time of the payment or performance, that a request for bankruptcy had been filed, or (ii) the performance of the obligation was the result of a consultation between the debtor and the payee with a view to give preference to the latter over the debtor's other creditors.

Risks arising in connection with the Spanish Insolvency Law

Subordination of the claims of the Holders under the Guarantee as a result of a contractual subordination.

The Law 22/2003 of 9 July, on Insolvency, as amended (the "**Spanish Insolvency Law**") regulates court insolvency proceedings, as opposed to out-of-court liquidation, which is only available when the debtor has sufficient assets to meet its liabilities.

The insolvency proceedings, which are called "*concurso de acreedores*" are applicable to all persons or entities. These proceedings may lead either to the restructuring of the business or to the liquidation of the assets of the debtor.

A debtor (and in the case of a company, its directors) is required to apply for insolvency proceedings when it is not able to meet its current obligations. The debtor is also entitled to apply for such insolvency proceedings when it expects that it will shortly be unable to do so. Insolvency proceedings are available as a type of legal protection that the debtor may request in order to avoid the attachment of its assets by its creditors.

Creditors will not be able to accelerate the maturity of their credits based only in the declaration of the insolvency ("*declaración de concurso*") of the debtor. Any provision to the contrary will be null and void. The insolvency order contains an express request for the creditors to declare debts owed to them, within a one-month period, providing original documentation to justify such credits. Based on the documentation provided by the creditors and that held by the debtor, the court receivers draw up a list of acknowledged creditors and classify them according to the categories established under law: (i) debts against the insolvency estate, (ii) debt benefiting from special privileges, (iii) debt benefiting from general privileges, (iv) ordinary debt and (v) subordinated debt:

- (i) Debts against the insolvency estate (*créditos contra la masa*) are not considered part of the debtor's general debt and are payable when due according to their own terms (and, therefore, are paid before other debts under insolvency proceedings). Debt against the insolvency estate includes, among others, (i) certain amounts of the employee payroll, (ii) costs and expenses of the insolvency proceedings, (iii) certain amounts arising from services provided by the insolvent debtor under reciprocal contracts and outstanding obligations that remain in force after insolvency proceedings are declared and deriving from obligations to return and indemnify in cases of voluntary termination or breach by the insolvent debtor, (iv) those that derive from the exercise of a clawback action within the insolvency proceedings of acts performed by the insolvent debtor and correspond to a refund of consideration received by it (except in cases of bad faith), (v) certain amounts arising from obligations created by law or from the non-contractual liability of the insolvent debtor after the declaration of insolvency and until its conclusion, (vi) 50% of the funds lent under a refinancing arrangement entered into in compliance with the requirements set forth in Article 71.6 of the Spanish Insolvency Law and (vii) certain debts incurred by the debtor following the declaration of insolvency.
- (ii) Debts benefiting from special privileges, representing attachments on certain assets (basically *in rem* security). These privileges may entail separate proceedings, though subject to certain restrictions derived from a waiting period that may last up to one year. However within such waiting period or while any enforcement proceedings remain suspended under the Spanish Insolvency Law, the insolvency administrators shall have the option to pay the relevant claims against the insolvency estate under specific payment rules. Privileged creditors are not subject to the arrangement, except if they give their express support by voting in favour of the arrangement. In the event of liquidation, they shall be the first to collect payment against the attached assets.
- (iii) Debts benefiting from general privileges, including among others certain labour debts and certain debts with public administrations. Other debts with public administrations corresponding to tax debts and social security obligations are recognised as privileged for half their amount, and debts held by the creditor applying for the corresponding insolvency proceedings, to the extent such application has been approved, up to a 50% of the amount of such debt. Funds under a refinancing arrangement entered into in compliance with the requirements set forth in Article 71.6 of Spanish Insolvency Law in the amount not admitted as a debt against the insolvency estate (*crédito contra la masa*) will also be credits with general privileges. The holders of general privileges are not to be affected by the restructuring if they do not agree to the arrangement and, in the event of liquidation, they are the first to collect payment, in the order established under law.
- (iv) Ordinary debts (non-subordinated and non-privileged creditors). They will be paid on a pro-rata basis.
- (v) Subordinated debts (thus classified by virtue of law). Subordinated debts include, among others, those credits held by parties in special relationships with the debtor: in the case of an individual, his/her relatives; in the case of a legal entity, the administrators and any shareholders holding more than 5% (for companies which have issued securities listed on an official secondary market) or 10% (for companies which have not issued securities listed on an official secondary market) of the share capital and companies pertaining to the same group as the debtor and their common shareholders, provided that such shareholders meet the minimum shareholding requirements set forth before. Likewise, credits which have been contractually subordinated (as the Securities) are classified as subordinated credits.

As a general rule, insolvency proceedings are not compatible with other enforcement proceedings. When compatible, in order to protect the interests of the debtor and creditors, the law extends the jurisdiction of the court dealing with insolvency proceedings, which is, then, legally authorised to handle any enforcement proceedings or interim measures affecting the debtor's assets (whether based upon civil, labour or administrative law).

Creditors holding security *in rem*, that had been traditionally allowed to enforce their debts against the secured asset notwithstanding the initiation of insolvency proceedings, are also generally subject to certain restrictions in order to initiate separate enforcement proceedings (or to continue with such proceedings, if they were being carried out), and if the secured asset is deemed to be necessary for the debtor's activities, enforcement cannot be carried out outside the insolvency proceedings. In summary, enforcement by the creditor is subject to a delay of a maximum of one year unless such asset is deemed to

be necessary for the debtors activities in which case enforcement cannot be carried out outside the insolvency proceedings.

There is no claw-back date. Therefore, there are no prior transactions that automatically become void as a result of initiation of the insolvency proceedings. The court receivers may only challenge those transactions that could be deemed as having "damaged" the debtor's interests, provided that they have taken place within two years prior to the declaration of insolvency (transactions taking place earlier than two years before insolvency has been declared are subject to the general regime of rescission in accordance with Article 71.7 of the Spanish Insolvency Law). Those transactions that are executed in the ordinary course of business, according to the business of the debtor, are not subject to challenge.

"Damage" does not refer to the intention of the parties, but to the consequences of the transaction on the debtor's interests. In any case, the law refers to transactions that are somehow exceptional: damage exists (as a non-rebuttable presumption) in the case of donations and early payment of unsecured obligations maturing after the insolvency declaration and damage is deemed to exist (as a rebuttable presumption) in the case of transactions entered into with special related persons and the creation of rights *in rem* in order to secure existing obligations or those incurred to replace existing obligations and the cancellation of obligations secured by an *in rem* security interest falling due after the declaration of Insolvency; in the remaining cases, damage would have to be justified.

The agreements in relation to the Securities could be challenged only if those transactions were deemed to have caused damage, as explained above.

Holders should be aware (i) of the effects of a declaration of insolvency ("declaración de concurso") of the Guarantor set out above, (ii) that their claims against the Guarantor would therefore be subordinated and (iii) subordinated creditors may not vote on an arrangement and have very limited chances of collection, according to the ranking established by law.

Risks related to the Securities generally

Set out below is a brief description of certain risks relating to the Securities generally:

Majority decisions bind all Holders.

The Conditions of each series of Securities contain provisions for calling meetings of Holders of the relevant series to consider matters affecting their interests generally. These provisions permit defined majorities to bind all Holders of the relevant series of Securities including Holders of such series who did not attend and vote at the relevant meeting and Holders who voted in a manner contrary to the majority.

Change of law.

The Conditions of each series of Securities are based on laws in effect as at the date of this Prospectus. No assurance can be given as to the impact of any possible judicial decision or change to relevant law or administrative practice after the date of this Prospectus.

There is no active trading market for the Securities.

The Securities are new securities which may not be widely distributed and for which there is currently no active trading market. If the Securities are traded after their initial issuance, they may trade at a discount to their initial offering price, depending upon prevailing interest rates, the market for similar securities, general economic conditions and the financial condition of the Issuer and the Guarantor. Although applications have been made for the Securities to be admitted to listing on the Official List of the FCA and to trading on the Regulated Market of the London Stock Exchange, there is no assurance that such applications will be accepted or that an active trading market will develop. Accordingly, there is no assurance as to the development or liquidity of any trading market for the Securities.

Because the Global Securities are held by or on behalf of Euroclear and Clearstream, Luxembourg, investors will have to rely on their procedures for transfer, payment and communication with the Issuer and/or the Guarantor.

The Securities will be represented by the Global Securities except in certain limited circumstances described in each Permanent Global Security. The Global Securities will be deposited with a common

depository for Euroclear and Clearstream, Luxembourg. Except in certain limited circumstances described in each Permanent Global Security, investors will not be entitled to receive Definitive Securities. Euroclear and Clearstream, Luxembourg will maintain records of the beneficial interests in the Global Securities. While the Securities are represented by the Global Securities, investors will be able to trade their beneficial interests only through Euroclear and Clearstream, Luxembourg.

The Issuer and the Guarantor will discharge their payment obligations under the Securities by making payments to or to the order of the common depository for Euroclear and Clearstream, Luxembourg for distribution to their account holders. A holder of a beneficial interest in a Global Security must rely on the procedures of Euroclear and Clearstream, Luxembourg to receive payments under the Securities. The Issuer and the Guarantor have no responsibility or liability for the records relating to, or payments made in respect of, beneficial interests in the Global Securities.

Holders of beneficial interests in the Global Securities will not have a direct right to vote in respect of the Securities. Instead, such holders will be permitted to act only to the extent that they are enabled by Euroclear and Clearstream, Luxembourg to appoint appropriate proxies.

EU Savings Directive on the taxation of savings income.

Under EC Council Directive 2003/48/EC on the taxation of savings income (for the purposes of the following paragraph, the "**Directive**"), each Member State is required to provide to the tax authorities of another Member State details of payments of interest or other similar income paid by a person within its jurisdiction to, or collected by such a person for, an individual resident or certain limited types of entity established in that other Member State; however, for a transitional period, Austria and Luxembourg may instead apply a withholding system in relation to such payments, deducting tax at a rate of 35%. The transitional period is to terminate at the end of the first full fiscal year following agreement by certain non-EU countries to the exchange of information relating to such payments. Luxembourg has announced that it will no longer apply the withholding tax system as from 1 January 2015 and will provide details of payments of interest (or similar income) as from this date.

A number of non EU countries, and certain dependent or associated territories of certain Member States, have adopted similar measures (either provision of information or transitional withholding) in relation to payments made by a person within its jurisdiction to, or collected by such a person for, an individual resident or certain limited types of entity established in a Member State. In addition, the Member States have entered into provision of information or transitional withholding arrangements with certain of those dependent or associated territories in relation to payments made by a person in a Member State to, or collected by such a person for, an individual resident or certain limited types of entity established in one of those territories.

The European Commission has proposed certain amendments to the Directive, which may, if implemented, amend or broaden the scope of the requirements described above. Investors who are in any doubt as to their position should consult their professional advisors.

If a payment were to be made or collected through a Member State which has opted for a withholding system and an amount of, or in respect of tax were to be withheld from that payment, neither the Issuer nor any Paying Agent nor any other person would be obliged to pay additional amounts with respect to any Securities as a result of the imposition of such withholding tax. If a withholding tax is imposed on payment made by a Paying Agent, the Issuer will be required to maintain a Paying Agent in a Member State that will not be obliged to withhold or deduct tax pursuant to the Directive.

Exchange rate fluctuations may affect the value of the Securities.

The Issuer will pay principal and interest on the Securities in euro. This presents certain risks relating to currency conversions if an investor's financial activities are denominated principally in a currency or currency unit (the "**Investor's Currency**") other than euro. These include the risk that exchange rates may significantly change (including changes due to devaluation of euro or revaluation of the Investor's Currency) and the risk that authorities with jurisdiction over the Investor's Currency may impose or modify exchange controls. An appreciation in the value of the Investor's Currency relative to euro would decrease (1) the Investor's Currency-equivalent yield on the Securities, (2) the Investor's Currency-equivalent value of the principal payable on the Securities and (3) the Investor's Currency equivalent market value of the Securities.

Government and monetary authorities may impose exchange controls that could adversely affect an applicable exchange rate. As a result, investors may receive less interest or principal than expected, or no interest or principal. Any of the foregoing events could adversely affect the price of the Securities.

OVERVIEW OF THE 6 YEAR NON-CALL SECURITIES

This overview must be read as an introduction to this Prospectus and any decision to invest in the 6 Year Non-Call Securities should be based on a consideration of the Prospectus as a whole, including the documents incorporated by reference.

Words and expressions defined in the "Terms and Conditions of the 6 Year Non-Call Securities" below have the same meanings in this overview.

Issuer:	Telefónica Europe B.V.
Guarantor:	Telefónica, S.A.
Description of 6 Year Non-Call Securities:	€750,000,000 Undated 6 Year Non-Call Deeply Subordinated Guaranteed Fixed Rate Reset Securities (the " 6 Year Non-Call Securities "), to be issued by the Issuer on 31 March 2014 (the " Issue Date ").
Joint Bookrunners:	Banco Bilbao Vizcaya Argentaria, S.A., Banco Santander, S.A., Barclays Bank PLC, CaixaBank, S.A., Goldman Sachs International, Mizuho International plc and The Royal Bank of Scotland plc.
Fiscal Agent:	The Bank of New York Mellon, London Branch.
Issue Price:	100% of the principal amount of the 6 Year Non-Call Securities.
Issue Date:	31 March 2014.
Maturity Date:	Undated.
Interest:	The 6 Year Non-Call Securities will bear interest on their principal amount: <ul style="list-style-type: none">(i) from (and including) the Issue Date to (but excluding) the First Reset Date at a rate of 5.000 per cent. per annum, payable annually in arrear on each Interest Payment Date, commencing on 31 March 2015; and(ii) from (and including) the First Reset Date, at the applicable 6 year Swap Rate in respect of the relevant Reset Period plus:<ul style="list-style-type: none">(A) in respect of the period commencing on the First Reset Date to (but excluding) 31 March 2024, 3.804 per cent. per annum;(B) in respect of the period commencing on 31 March 2024 to (but excluding) 31 March 2040, 4.054 per cent. per annum¹; and(C) from and including 31 March 2040, 4.804 per cent. per annum²,

¹ Step-up of 25 basis points 10 years after the Issue Date

² Step-up of 75 basis points 26 years after the Issue Date

all as determined by the Agent Bank, payable annually in arrear on each Interest Payment Date, commencing on 31 March 2021, subject to Condition 5.

All as more particularly described in Condition 4 (*Interest Payments*) of the Terms and Conditions of the 6 Year Non-Call Securities.

Interest Payment Dates: Interest payments in respect of the 6 Year Non-Call Securities will be payable annually in arrear on 31 March in each year, commencing on 31 March 2015.

Status of the 6 Year Non-Call Securities: The 6 Year Non-Call Securities and the Coupons constitute direct, unsecured and subordinated obligations of the Issuer (senior only to Junior Obligations of the Issuer) and will at all times rank *pari passu* and without any preference among themselves.

Subordination of the 6 Year Non-Call Securities: In the event of an Issuer Winding-up, the rights and claims of the Holders against the Issuer in respect of or arising under the 6 Year Non-Call Securities and the Coupons will rank (i) junior to the claims of all holders of Senior Obligations of the Issuer, (ii) *pari passu* with the claims of holders of all Parity Obligations of the Issuer and (iii) senior to the claims of holders of all Junior Obligations of the Issuer.

Subject to applicable law, no Holder may exercise or claim any right of set-off in respect of any amount owed to it by the Issuer arising under or in connection with the 6 Year Non-Call Securities or the Coupons and each Holder shall, by virtue of being the Holder, be deemed to have waived all such rights of set-off. Condition 2(b) is an irrevocable stipulation (*derdenbeding*) for the benefit of the creditors of Senior Obligations of the Issuer and each such creditor may rely on and enforce Condition 2(b) under Section 6:253 of the Dutch Civil Code.

Guarantee and Status of Guarantee: Payment of all sums expressed to be payable by the Issuer under the 6 Year Non-Call Securities and the Coupons will be unconditionally and irrevocably guaranteed by the Guarantor on a subordinated basis.

The payment obligations of the Guarantor under the Guarantee constitute direct, unsecured and subordinated obligations of the Guarantor (senior only to Junior Obligations of the Guarantor) and will at all times rank *pari passu* and without preference among themselves.

Subordination of the Guarantee: Subject to mandatory provisions of Spanish applicable law, in the event of the Guarantor being declared in insolvency (*concurso*) under Spanish Insolvency Law, the rights and claims of Holders against the Guarantor in respect of or arising under the Guarantee will rank (i) junior to the claims of the holders of all Senior Obligations of the Guarantor, (ii) *pari passu* with the claims of the holders of all Parity Obligations of the Guarantor, and (iii) senior to the claims of the holders of all Junior Obligations of the Guarantor.

Optional Interest Deferral: The Issuer may, at its sole discretion, elect to defer (in whole or in part) any payment of interest on the 6 Year Non-Call Securities, as more particularly described in "*Terms and Conditions of the 6 Year Non-Call Securities – Optional Interest Deferral*". Non-payment of interest so deferred shall not constitute a default by the Issuer or Guarantor under the 6 Year Non-Call Securities or the Guarantee or for any other purpose. Any amounts so deferred, together with further interest accrued thereon (at the Prevailing Interest Rate applicable from time to time), shall constitute Arrears of Interest.

Optional Settlement of Arrears of Interest of Arrears of Interest may be satisfied at the option of the Issuer, in whole or in part, at any given time upon giving not more than 14 and no less than seven Business Days' notice to the Holders, the Fiscal Agent and the Paying Agents prior to the relevant Optional Deferred Interest Settlement Date informing them of its election so to satisfy such Arrears of Interest (or part thereof) and specifying the relevant Optional Deferred Interest Settlement Date. See Condition 5(b) (*Mandatory Settlement of Arrears of Interest*) of the Terms and Conditions of the 6 Year Non-Call Securities.

Mandatory Settlement of Arrears of Interest: The Issuer shall pay any outstanding Arrears of Interest in whole, but not in part, on the first occurring Mandatory Settlement Date following the Interest Payment Date on which any outstanding Arrears of Interest was first deferred.

"Mandatory Settlement Date" means the earliest of:

- (i) as soon as reasonably practicable (but no later than the fifth business day) following the date on which a Compulsory Arrears of Interest Settlement Event occurs;
- (ii) following any Deferred Interest Payment, on the next scheduled Interest Payment Date on which the Issuer does not elect to defer in whole the interest accrued in respect of the relevant Interest Period; and
- (iii) the date on which the 6 Year Non-Call Securities are redeemed or repaid in accordance with Condition 6 (*Redemption and Purchase*) or become due and payable in accordance with Condition 9 (*Enforcement Events and No Events of Default*).

Subject to certain exceptions, as more particularly described in Condition 5 (*Optional Interest Deferral*) of the Terms and Conditions of the 6 Year Non-Call Securities, a "Compulsory Arrears of Interest Settlement Event" shall have occurred if:

- (i) a Dividend Declaration is made in respect of any Junior Obligations or any Parity Obligations (other than in respect of any such dividend, distribution or payment paid or made (i) in respect of the 2002 Preferred Securities; or (ii) exclusively in Ordinary Shares of the Guarantor); or
- (ii) the Guarantor or any of its subsidiaries has repurchased, redeemed or otherwise acquired any Junior Obligations or any Parity Obligations (other than any repurchase, redemption or acquisition of any 2002 Preferred Securities),

all as more particularly described in Condition 5 (*Optional Interest Deferral*) of the Terms and Conditions of the 6 Year Non-Call Securities.

If a Mandatory Settlement Date does not occur prior to the calendar day which is the fifth anniversary of the Interest Payment Date on which the relevant Deferred Interest Payment was first deferred, it is the intention, though not an obligation, of the Issuer to pay all outstanding Arrears of Interest (in whole but not in part) on the next following Interest Payment Date.

Optional Redemption: The Issuer may redeem the 6 Year Non-Call Securities in whole, but not in part, on the First Reset Date and on any Interest Payment Date thereafter at their principal amount together with any accrued and unpaid interest up to (but excluding) the Redemption Date and any outstanding Arrears of Interest.

In addition, upon the occurrence of an Accounting Event, a Capital Event, a Tax Event, a Withholding Tax Event or a Substantial Purchase Event, the 6 Year Non-Call Securities will be redeemable (at the option of the Issuer) in whole, but not in part, at the prices set out, and as more particularly described, in Condition 6 (*Redemption and Purchase*) of the Terms and Conditions of the 6 Year Non-Call Securities.

Events of Default There are no events of default in respect of the 6 Year Non-Call Securities. However, if an Issuer Winding-up occurs, or an order is made or an effective resolution passed for the winding-up, dissolution or liquidation of the Guarantor, or the Guarantor becomes insolvent (*en estado de insolvencia*) pursuant to article 2 of the Spanish Insolvency Law, any Holder of a 6 Year Non-Call Security, in respect of such 6 Year Non-Call Security and provided that such Holder does not contravene an Extraordinary Resolution (if any) may, by written notice to the Issuer and the Guarantor, declare that such 6 Year Non-Call Security and all interest then accrued but unpaid on such 6 Year Non-Call Security shall be forthwith due and payable, whereupon the same shall become immediately due and payable, together with all interest accrued thereon.

In such case the Holder of a 6 Year Non-Call Security may, at its sole discretion, institute steps in order to obtain a judgment against the Issuer and/or the Guarantor for any amounts due in respect of the 6 Year Non-Call Securities, including the institution of proceedings for the declaration of insolvency (*declaración de concurso*) under Spanish Insolvency Law of the Guarantor and/or proving and/or claiming in an Issuer Winding-up or in the winding-up, dissolution, liquidation or insolvency proceeding of the Guarantor for such amount.

Additional Amounts: Payments in respect of the 6 Year Non-Call Securities and the Coupons by the Issuer or (as the case may be) the Guarantor under the Guarantee will be made without withholding or deduction for, or on account of, Taxes of The Netherlands or the Kingdom of Spain, unless such withholding or deduction is required by law. In the event that any such withholding or deduction is made, additional amounts will be payable by the Issuer or, as the case may be, the Guarantor, subject to certain exceptions as are more fully described in Condition 8(a) (*Taxation - Additional Amounts*) of the Terms and Conditions of the 6 Year Non-Call Securities.

Form: The 6 Year Non-Call Securities will be in bearer form and will initially be represented by a Temporary Global Security, without interest coupons or talons, which will be deposited with a common depository on behalf of Euroclear and Clearstream, Luxembourg on or about the Issue Date. Interests in the Temporary Global Security will be exchangeable for interests in a Permanent Global Security as set out in the Temporary Global Security. The Permanent Global Security will be exchangeable for Definitive Securities in the circumstances set out in the Permanent Global Security. See "*Summary of Provisions relating to the Securities while in Global Form*".

Denominations: The 6 Year Non-Call Securities will be issued in denominations of €100,000.

Governing Law:

The Fiscal Agency Agreement, the 6 Year Non-Call Securities, the Coupons and the Guarantee and any non-contractual obligations arising out of or in connection with them are governed by and shall be construed in accordance with English law, other than the provisions of Condition 2(b) (*Status and Subordination of the 6 Year Non-Call Securities and Coupons – Subordination of the 6 Year Non-Call Securities*) relating to the subordination of the 6 Year Non-Call Securities which are governed by and construed in accordance with the laws of The Netherlands, and the provisions of Conditions 3(b) (*Guarantee, Status and Subordination of the Guarantee – Status of the Guarantee*) and Condition 3(c) (*Guarantee, Status and Subordination of the Guarantee – Subordination of the Guarantee*) relating to the subordination of the Guarantee and the corresponding provisions of the Guarantee which are governed by and construed in accordance with the laws of the Kingdom of Spain. See Condition 16 (*Governing Law*) of the Terms and Conditions of the 6 Year Non-Call Securities.

Replacement Intention:

The Guarantor intends (without thereby assuming any obligation) at any time that it or the Issuer will redeem or repurchase the 6 Year Non-Call Securities only to the extent that the aggregate principal amount of the 6 Year Non-Call Securities to be redeemed or repurchased does not exceed such part of the net proceeds received by the Guarantor or any Subsidiary of the Guarantor during the 360-day period prior to the date of such redemption or repurchase from the sale or issuance by the Guarantor or such Subsidiary to third party purchasers (other than group entities of the Guarantor) of securities which are assigned by S&P, at the time of sale or issuance, an aggregate "equity credit" (or such similar nomenclature used by S&P from time to time) that is equal to or greater than the "equity credit" assigned to the 6 Year Non-Call Securities to be redeemed or repurchased at the time of their issuance (but taking into account any changes in hybrid capital methodology or another relevant methodology or the interpretation thereof since the issuance of the 6 Year Non-Call Securities), unless:

- (i) the rating assigned by S&P to the Guarantor is at least "BBB" (or such similar nomenclature then used by S&P) and the Guarantor is of the view that such rating would not fall below this level as a result of such redemption or repurchase, or
- (ii) in the case of a repurchase, such repurchase is of less than (a) 10 per cent. of the aggregate principal amount of the 6 Year Non-Call Securities originally issued in any period of 12 consecutive months or (b) 25 per cent. of the aggregate principal amount of the 6 Year Non-Call Securities originally issued in any period of 10 consecutive years, or
- (iii) the 6 Year Non-Call Securities are redeemed pursuant to a Tax Event, a Capital Event, an Accounting Event or a Withholding Tax Event, or
- (iv) such redemption or repurchase occurs on or after the Reset Date falling on 31 March 2040.

Rating:

The 6 Year Non-Call Securities will be rated BB+ by S&P, Ba1 by Moody's and BBB- by Fitch. Each of S&P, Moody's and Fitch is established in the European Union and registered under the CRA Regulation. A security rating is not a recommendation to buy, sell or hold securities and may be subject to suspension, reduction or withdrawal at any time by the assigning rating agency.

Listing and Admission to Trading:	This Prospectus has been approved by the FCA, which is the United Kingdom competent authority for the purposes of the Prospectus Directive and relevant implementing measures in the United Kingdom as a prospectus issued in compliance with the Prospectus Directive for the purpose of giving information with regard to the issue of the 6 Year Non-Call Securities. Applications have been made for the 6 Year Non-Call Securities to be admitted to listing on the Official List of the FCA and to trading on the Regulated Market of the London Stock Exchange. The Regulated Market of the London Stock Exchange is a regulated market for the purposes of Directive 2004/39/EC on markets in financial instruments.
Selling Restrictions:	The United States, the United Kingdom, The Netherlands and the Kingdom of Spain. See " <i>Subscription and Sale</i> ". Category 2 selling restrictions will apply for the purposes of Regulation S under the Securities Act.
Use of Proceeds:	The net proceeds of the issue of the 6 Year Non-Call Securities, expected to amount to €745,500,000 will be used for general corporate purposes of the Guarantor and its Group, including the preservation of the liquidity cushion and debt refinancing
Risk Factors:	Prospective investors should carefully consider the information set out in " <i>Risk Factors</i> " in conjunction with the other information contained or incorporated by reference in this Prospectus.
ISIN:	XS1050460739.
Common Code:	105046073.

OVERVIEW OF THE 10 YEAR NON-CALL SECURITIES

This overview must be read as an introduction to this Prospectus and any decision to invest in the 10 Year Non-Call Securities should be based on a consideration of the Prospectus as a whole, including the documents incorporated by reference.

Words and expressions defined in the "Terms and Conditions of the 10 Year Non-Call Securities" below have the same meanings in this overview.

Issuer:	Telefónica Europe B.V.
Guarantor:	Telefónica, S.A.
Description of 10 Year Non-Call Securities:	€1,000,000,000 Undated 10 Year Non-Call Deeply Subordinated Guaranteed Fixed Rate Reset Securities (the " 10 Year Non-Call Securities "), to be issued by the Issuer on 31 March 2014 (the " Issue Date ").
Joint Bookrunners:	Banco Bilbao Vizcaya Argentaria, S.A., Banco Santander, S.A., Barclays Bank PLC, CaixaBank, S.A., Goldman Sachs International, Mizuho International plc and The Royal Bank of Scotland plc.
Fiscal Agent:	The Bank of New York Mellon, London Branch.
Issue Price:	100% of the principal amount of the 10 Year Non-Call Securities.
Issue Date:	31 March 2014.
Maturity Date:	Undated.
Interest:	<p>The 10 Year Non-Call Securities will bear interest on their principal amount:</p> <ul style="list-style-type: none">(i) from (and including) the Issue Date to (but excluding) the First Reset Date at a rate of 5.875 per cent. per annum, payable annually in arrear on each Interest Payment Date, commencing on 31 March 2015; and(ii) from (and including) the First Reset Date, at the applicable 10 year Swap Rate in respect of the relevant Reset Period, plus:<ul style="list-style-type: none">(A) in respect of the period commencing on the First Reset Date to (but excluding) 31 March 2044, 4.301 per cent. per annum³; and(B) from and including 31 March 2044, 5.051 per cent. per annum⁴, <p>all as determined by the Agent Bank, payable annually in arrear on each Interest Payment Date, commencing on 31 March 2025, subject to Condition 5.</p> <p>All as more particularly described in Condition 4 (<i>Interest Payments</i>) of the Terms and Conditions of the 10 Year Non-Call Securities.</p>

³ Step-up of 25 basis points 10 years after the Issue Date

⁴ Step-up of 75 basis points 30 years after the Issue Date

Interest Payment Dates:	Interest payments in respect of the 10 Year Non-Call Securities will be payable annually in arrear on 31 March in each year, commencing on 31 March 2015.
Status of the 10 Year Non-Call Securities:	The 10 Year Non-Call Securities and the Coupons constitute direct, unsecured and subordinated obligations of the Issuer (senior only to Junior Obligations of the Issuer) and will at all times rank <i>pari passu</i> and without any preference among themselves.
Subordination of the 10 Year Non-Call Securities:	<p>In the event of an Issuer Winding-up, the rights and claims of the Holders against the Issuer in respect of or arising under the 10 Year Non-Call Securities and the Coupons will rank (i) junior to the claims of all holders of Senior Obligations of the Issuer, (ii) <i>pari passu</i> with the claims of holders of all Parity Obligations of the Issuer and (iii) senior to the claims of holders of all Junior Obligations of the Issuer.</p> <p>Subject to applicable law, no Holder may exercise or claim any right of set-off in respect of any amount owed to it by the Issuer arising under or in connection with the 10 Year Non-Call Securities or the Coupons and each Holder shall, by virtue of being the Holder, be deemed to have waived all such rights of set-off. Condition 2(b) is an irrevocable stipulation (<i>derdenbeding</i>) for the benefit of the creditors of Senior Obligations of the Issuer and each such creditor may rely on and enforce Condition 2(b) under Section 6:253 of the Dutch Civil Code.</p>
Guarantee and Status of Guarantee:	<p>Payment of all sums expressed to be payable by the Issuer under the 10 Year Non-Call Securities and the Coupons will be unconditionally and irrevocably guaranteed by the Guarantor on a subordinated basis.</p> <p>The payment obligations of the Guarantor under the Guarantee constitute direct, unsecured and subordinated obligations of the Guarantor (senior only to Junior Obligations of the Guarantor) and will at all times rank <i>pari passu</i> and without preference among themselves.</p>
Subordination of the Guarantee:	Subject to mandatory provisions of Spanish applicable law, in the event of the Guarantor being declared in insolvency (<i>concurso</i>) under Spanish Insolvency Law, the rights and claims of Holders against the Guarantor in respect of or arising under the Guarantee will rank (i) junior to the claims of the holders of all Senior Obligations of the Guarantor, (ii) <i>pari passu</i> with the claims of the holders of all Parity Obligations of the Guarantor, and (iii) senior to the claims of the holders of all Junior Obligations of the Guarantor.
Optional Interest Deferral:	The Issuer may, at its sole discretion, elect to defer (in whole or in part) any payment of interest on the 10 Year Non-Call Securities, as more particularly described in " <i>Terms and Conditions of the 10 Year Non-Call Securities – Optional Interest Deferral</i> ". Non-payment of interest so deferred shall not constitute a default by the Issuer or Guarantor under the 10 Year Non-Call Securities or the Guarantee or for any other purpose. Any amounts so deferred, together with further interest accrued thereon (at the Prevailing Interest Rate applicable from time to time), shall constitute Arrears of Interest.

Optional Settlement of Arrears of Interest of Arrears of Interest may be satisfied at the option of the Issuer, in whole or in part, at any given time upon giving not more than 14 and no less than seven Business Days' notice to the Holders, the Fiscal Agent and the Paying Agents prior to the relevant Optional Deferred Interest Settlement Date informing them of its election so to satisfy such Arrears of Interest (or part thereof) and specifying the relevant Optional Deferred Interest Settlement Date. See Condition 5(b) (*Mandatory Settlement of Arrears of Interest*) of the Terms and Conditions of the 10 Year Non-Call Securities.

Mandatory Settlement of Arrears of Interest: The Issuer shall pay any outstanding Arrears of Interest in whole, but not in part, on the first occurring Mandatory Settlement Date following the Interest Payment Date on which any outstanding Arrears of Interest was first deferred.

"**Mandatory Settlement Date**" means the earliest of:

- (i) as soon as reasonably practicable (but no later than the fifth business day) following the date on which a Compulsory Arrears of Interest Settlement Event occurs;
- (ii) following any Deferred Interest Payment, on the next scheduled Interest Payment Date on which the Issuer does not elect to defer in whole the interest accrued in respect of the relevant Interest Period; and
- (iii) the date on which the 10 Year Non-Call Securities are redeemed or repaid in accordance with Condition 6 (*Redemption and Purchase*) or become due and payable in accordance with Condition 9 (*Enforcement Events and No Events of Default*).

Subject to certain exceptions, as more particularly described in Condition 5 (*Optional Interest Deferral*) of the Terms and Conditions of the 10 Year Non-Call Securities, a "Compulsory Arrears of Interest Settlement Event" shall have occurred if:

- (i) a Dividend Declaration is made in respect of any Junior Obligations or any Parity Obligations (other than in respect of any such dividend, distribution or payment paid or made (i) in respect of the 2002 Preferred Securities; or (ii) exclusively in Ordinary Shares of the Guarantor); or
- (ii) the Guarantor or any of its subsidiaries has repurchased, redeemed or otherwise acquired any Junior Obligations or any Parity Obligations (other than any repurchase, redemption or acquisition of any 2002 Preferred Securities),

all as more particularly described in Condition 5 (*Optional Interest Deferral*) of the Terms and Conditions of the 10 Year Non-Call Securities.

If a Mandatory Settlement Date does not occur prior to the calendar day which is the fifth anniversary of the Interest Payment Date on which the relevant Deferred Interest Payment was first deferred, it is the intention, though not an obligation, of the Issuer to pay all outstanding Arrears of Interest (in whole but not in part) on the next following Interest Payment Date.

Optional Redemption: The Issuer may redeem the 10 Year Non-Call Securities in whole, but not in part, on the First Reset Date and on any Interest Payment Date thereafter at their principal amount together with any accrued and unpaid interest up to (but excluding) the Redemption Date and any outstanding Arrears of Interest.

In addition, upon the occurrence of an Accounting Event, a Capital Event, a Tax Event, a Withholding Tax Event or a Substantial Purchase Event, the 10 Year Non-Call Securities will be redeemable (at the option of the Issuer) in whole, but not in part, at the prices set out, and as more particularly described, in Condition 6 (*Redemption and Purchase*) of the Terms and Conditions of the 10 Year Non-Call Securities.

Events of Default There are no events of default in respect of the 10 Year Non-Call Securities. However, if an Issuer Winding-up occurs, or an order is made or an effective resolution passed for the winding-up, dissolution or liquidation of the Guarantor, or the Guarantor becomes insolvent (*en estado de insolvencia*) pursuant to article 2 of the Spanish Insolvency Law, any Holder of a 10 Year Non-Call Security, in respect of such 10 Year Non-Call Security and provided that such Holder does not contravene an Extraordinary Resolution (if any) may, by written notice to the Issuer and the Guarantor, declare that such 10 Year Non-Call Security and all interest then accrued but unpaid on such 10 Year Non-Call Security shall be forthwith due and payable, whereupon the same shall become immediately due and payable, together with all interest accrued thereon.

In such case the Holder of a 10 Year Non-Call Security may, at its sole discretion, institute steps in order to obtain a judgment against the Issuer and/or the Guarantor for any amounts due in respect of the 10 Year Non-Call Securities, including the institution of proceedings for the declaration of insolvency (*declaración de concurso*) under Spanish Insolvency Law of the Guarantor and/or proving and/or claiming in an Issuer Winding-up or in the winding-up, dissolution, liquidation or insolvency proceeding of the Guarantor for such amount.

Additional Amounts: Payments in respect of the 10 Year Non-Call Securities and the Coupons by the Issuer or (as the case may be) the Guarantor under the Guarantee will be made without withholding or deduction for, or on account of, Taxes of The Netherlands or the Kingdom of Spain, unless such withholding or deduction is required by law. In the event that any such withholding or deduction is made, additional amounts will be payable by the Issuer or, as the case may be, the Guarantor, subject to certain exceptions as are more fully described in Condition 8(a) (*Taxation - Additional Amounts*) of the Terms and Conditions of the 10 Year Non-Call Securities.

Form: The 10 Year Non-Call Securities will be in bearer form and will initially be represented by a Temporary Global Security, without interest coupons or talons, which will be deposited with a common depository on behalf of Euroclear and Clearstream, Luxembourg on or about the Issue Date. Interests in the Temporary Global Security will be exchangeable for interests in a Permanent Global Security as set out in the Temporary Global Security. The Permanent Global Security will be exchangeable for Definitive Securities in the circumstances set out in the Permanent Global Security. See "*Summary of Provisions relating to the Securities while in Global Form*".

Denominations: The 10 Year Non-Call Securities will be issued in denominations of €100,000.

Governing Law: The Fiscal Agency Agreement, the 10 Year Non-Call Securities, the Coupons and the Guarantee and any non-contractual obligations arising out of or in connection with them are governed by and shall be construed in accordance with English law, other than the provisions of Condition 2(b) (*Status and Subordination of the 10 Year Non-Call Securities and Coupons – Subordination of the 10 Year Non-Call Securities*) relating to the subordination of the 10 Year Non-Call Securities which are governed by and construed in accordance with the laws of The Netherlands, and the provisions of Conditions 3(b) (*Guarantee, Status and Subordination of the Guarantee – Status of the Guarantee*) and Condition 3(c) (*Guarantee, Status and Subordination of the Guarantee – Subordination of the Guarantee*) relating to the subordination of the Guarantee and the corresponding provisions of the Guarantee which are governed by and construed in accordance with the laws of the Kingdom of Spain. See Condition 16 (*Governing Law*) of the Terms and Conditions of the 10 Year Non-Call Securities.

Replacement Intention: The Guarantor intends (without thereby assuming any obligation) at any time that it or the Issuer will redeem or repurchase the 10 Year Non-Call Securities only to the extent that the aggregate principal amount of the 10 Year Non-Call Securities to be redeemed or repurchased does not exceed such part of the net proceeds received by the Guarantor or any Subsidiary of the Guarantor during the 360-day period prior to the date of such redemption or repurchase from the sale or issuance by the Guarantor or such Subsidiary to third party purchasers (other than group entities of the Guarantor) of securities which are assigned by S&P, at the time of sale or issuance, an aggregate "equity credit" (or such similar nomenclature used by S&P from time to time) that is equal to or greater than the "equity credit" assigned to the 10 Year Non-Call Securities to be redeemed or repurchased at the time of their issuance (but taking into account any changes in hybrid capital methodology or another relevant methodology or the interpretation thereof since the issuance of the 10 Year Non-Call Securities), unless:

- (i) the rating assigned by S&P to the Guarantor is at least "BBB" (or such similar nomenclature then used by S&P) and the Guarantor is of the view that such rating would not fall below this level as a result of such redemption or repurchase, or
- (ii) in the case of a repurchase, such repurchase is of less than (a) 10 per cent. of the aggregate principal amount of the 10 Year Non-Call Securities originally issued in any period of 12 consecutive months or (b) 25 per cent. of the aggregate principal amount of the 10 Year Non-Call Securities originally issued in any period of 10 consecutive years, or
- (iii) the 10 Year Non-Call Securities are redeemed pursuant to a Tax Event, a Capital Event, an Accounting Event or a Withholding Tax Event, or
- (iv) such redemption or repurchase occurs on or after the Interest Payment Date falling on 31 March 2044.

Rating:	The 10 Year Non-Call Securities will be rated BB+ by S&P, Ba1 by Moody's and BBB- by Fitch. Each of S&P, Moody's and Fitch is established in the European Union and registered under the CRA Regulation. A security rating is not a recommendation to buy, sell or hold securities and may be subject to suspension, reduction or withdrawal at any time by the assigning rating agency.
Listing and Admission to Trading:	This Prospectus has been approved by the FCA, which is the United Kingdom competent authority for the purposes of the Prospectus Directive and relevant implementing measures in the United Kingdom as a prospectus issued in compliance with the Prospectus Directive for the purpose of giving information with regard to the issue of the 10 Year Non-Call Securities. Applications have been made for the 10 Year Non-Call Securities to be admitted to listing on the Official List of the FCA and to trading on the Regulated Market of the London Stock Exchange. The Regulated Market of the London Stock Exchange is a regulated market for the purposes of Directive 2004/39/EC on markets in financial instruments.
Selling Restrictions:	The United States, the United Kingdom, The Netherlands and the Kingdom of Spain. See " <i>Subscription and Sale</i> ". Category 2 selling restrictions will apply for the purposes of Regulation S under the Securities Act.
Use of Proceeds:	The net proceeds of the issue of the 10 Year Non-Call Securities, expected to amount to €994,000,000 will be used for general corporate purposes of the Guarantor and its Group, including the preservation of the liquidity cushion and debt refinancing.
Risk Factors:	Prospective investors should carefully consider the information set out in " <i>Risk Factors</i> " in conjunction with the other information contained or incorporated by reference in this Prospectus.
ISIN:	XS1050461034.
Common Code:	105046103.

INFORMATION INCORPORATED BY REFERENCE

The information set out in the table below shall be deemed to be incorporated in, and to form part of, this Prospectus **provided however that** any statement contained in any document incorporated by reference in, and forming part of, this Prospectus shall be deemed to be modified or superseded for the purpose of this Prospectus to the extent that a statement contained herein modifies or supersedes such statement.

Such documents will be made available, free of charge, during usual business hours at the specified offices of the Fiscal Agent, unless such documents have been modified or superseded. In addition the financial statements of Telefónica Europe B.V. for the year ended 31 December 2013 are available on http://www.rns-pdf.londonstockexchange.com/rns/6682C_-2014-3-19.pdf; the financial statements of Telefónica Europe B.V. for the year ended 31 December 2012 are available on http://www.rns-pdf.londonstockexchange.com/rns/1276D_-2013-4-24.pdf; the consolidated financial statements of Telefónica, S.A. for the year ended 31 December 2013 are available on http://www.rns-pdf.londonstockexchange.com/rns/7907C_2-2014-3-20.pdf; and the consolidated financial statements of Telefónica, S.A. for the year ended 31 December 2012 are available on http://www.rns-pdf.londonstockexchange.com/rns/5445A_2-2013-3-21.pdf.

For ease of reference, the tables below set out:

- (i) the relevant page references for the financial statements, the notes to the financial statements and the Auditors' reports for the years ended 31 December 2013 and 2012 for the Issuer; and
- (ii) the relevant page references for the consolidated financial statements, the notes to the consolidated financial statements and the Auditors' reports for the years ended 31 December 2013 and 2012 for the Guarantor.

Telefónica Europe B.V.

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Where only certain parts of a document are incorporated by reference, the non-incorporated parts of the document are either not relevant to investors or are covered elsewhere in this Prospectus.

TERMS AND CONDITIONS OF THE 6 YEAR NON-CALL SECURITIES

The following are the terms and conditions substantially in the form in which they will be endorsed on the 6 Year Non-Call Securities. Sentences in italics shall not form part of these terms and conditions.

The issue of the 6 Year Non-Call Securities was authorised by a resolution of the Board of Managing Directors of the Issuer dated 14 March 2014 and the guarantee of the 6 Year Non-Call Securities was authorised by a resolution of the Delegated Committee of the Board of Directors of the Guarantor dated 14 March 2014, by a resolution of the Board of Directors of the Guarantor dated 31 May 2013, and by a resolution of the shareholders acting through the General Shareholders' Meeting of the Guarantor dated 31 May 2013. A fiscal agency agreement dated 31 March 2014 (the "**Fiscal Agency Agreement**") has been entered into in relation to the 6 Year Non-Call Securities between the Issuer, the Guarantor, The Bank of New York Mellon, London Branch as fiscal agent, The Bank of New York Mellon, London Branch as agent bank and the paying agents named therein. The fiscal agent, the agent bank and the paying agents for the time being are referred to below respectively as the "**Fiscal Agent**", the "**Agent Bank**" and the "**Paying Agents**" (which expression shall include the Fiscal Agent). The Fiscal Agency Agreement includes the form of the 6 Year Non-Call Securities and the coupons relating to them (the "**Coupons**", which expression includes, where the context so permits, talons for further coupons (the "**Talons**")). Copies of the Fiscal Agency Agreement are available for inspection during normal business hours at the specified offices of the Paying Agents. The Holders of the 6 Year Non-Call Securities and the Holders of the Coupons (each as defined in Condition 1(b) below) (whether or not attached to the relevant 6 Year Non-Call Securities) are deemed to have notice of all the provisions of the Fiscal Agency Agreement applicable to them.

1. **Form, Denomination and Title**

- (a) **Form and denomination:** The 6 Year Non-Call Securities are serially numbered and in bearer form in the denominations of €100,000, each with Coupons attached on issue.
- (b) **Title:** Title to the 6 Year Non-Call Securities and Coupons passes by delivery. The holder of any 6 Year Non-Call Security or Coupon (a "**Holder**") will (except as otherwise required by applicable law or regulatory requirement) be treated as its absolute owner for all purposes (whether or not it is overdue and regardless of any notice of ownership, trust or any interest in it, any writing on it, or its theft or loss) and no person shall be liable for so treating the Holder.

2. **Status and Subordination of the 6 Year Non-Call Securities and Coupons**

- (a) **Status of the 6 Year Non-Call Securities and Coupons:** The 6 Year Non-Call Securities and the Coupons constitute direct, unsecured and subordinated obligations of the Issuer (senior only to Junior Obligations of the Issuer) and shall at all times rank *pari passu* and without any preference among themselves.
- (b) **Subordination of the 6 Year Non-Call Securities:** In the event of an Issuer Winding-up, the rights and claims of the Holders against the Issuer in respect of or arising under the 6 Year Non-Call Securities and the Coupons will rank (i) junior to the claims of all holders of Senior Obligations of the Issuer, (ii) *pari passu* with the claims of holders of all Parity Obligations of the Issuer and (iii) senior to the claims of holders of all Junior Obligations of the Issuer.

Subject to applicable law, no Holder may exercise or claim any right of set-off in respect of any amount owed to it by the Issuer arising under or in connection with the 6 Year Non-Call Securities or the Coupons and each Holder shall, by virtue of being the Holder, be deemed to have waived all such rights of set-off. This Condition 2(b) is an irrevocable stipulation (*derdenbeding*) for the benefit of the creditors of Senior Obligations of the Issuer and each such creditor may rely on and enforce this Condition 2(b) under Section 6:253 of the Dutch Civil Code.

The Issuer does not have any Preferred Shares of the Issuer outstanding and the Issuer's Articles of Association do not provide for the issuance of such shares by the Issuer. For

so long as any of the 6 Year Non-Call Securities remains outstanding, the Guarantor and the Issuer do not intend to issue any Preferred Shares of the Issuer.

3. **Guarantee, Status and Subordination of the Guarantee**

- (a) **Guarantee:** The Guarantor has unconditionally and irrevocably guaranteed the due payment of all sums expressed to be payable by the Issuer under the 6 Year Non-Call Securities and the Coupons on a subordinated basis. Its obligations in that respect (the "**Guarantee**") are set out in the deed of guarantee dated the Issue Date and made by the Guarantor for the benefit of the Holders.
- (b) **Status of the Guarantee:** The payment obligations of the Guarantor under the Guarantee constitute direct, unsecured and subordinated obligations of the Guarantor (senior only to Junior Obligations of the Guarantor) and shall at all times rank *pari passu* and without any preference among themselves.
- (c) **Subordination of the Guarantee:** Subject to mandatory provisions of Spanish applicable law, in the event of the Guarantor being declared in insolvency (*concurso*) under Spanish insolvency law, the rights and claims of Holders against the Guarantor in respect of or arising under the Guarantee will rank (i) junior to the claims of the holders of all Senior Obligations of the Guarantor, (ii) *pari passu* with the claims of the holders of all Parity Obligations of the Guarantor and (iii) senior to the claims of the holders of all Junior Obligations of the Guarantor.

4. **Interest Payments**

(a) **General**

The 6 Year Non-Call Securities bear interest at the Prevailing Interest Rate from (and including) 31 March 2014 (the "**Issue Date**") in accordance with the provisions of this Condition 4.

Subject to Condition 5, interest shall be payable on the 6 Year Non-Call Securities with respect to any Interest Period annually in arrear on each Interest Payment Date in each case as provided in this Condition 4.

(b) **Interest Accrual**

The 6 Year Non-Call Securities will cease to bear interest from (and including) the date of redemption thereof pursuant to Condition 6 unless, upon due presentation, payment of all amounts due in respect of the 6 Year Non-Call Securities is not made, in which event interest shall continue to accrue in respect of unpaid amounts on the 6 Year Non-Call Securities, both before and after judgment, and shall be payable, as provided in these Conditions up to (but excluding) the Relevant Date.

Interest in respect of any 6 Year Non-Call Security shall be calculated per €100,000 in principal amount thereof (the "**Calculation Amount**"). The interest payable on each 6 Year Non-Call Security on any Interest Payment Date shall be calculated by multiplying the Prevailing Interest Rate for the Interest Period ending immediately prior to such Interest Payment Date by the Calculation Amount and rounding the resulting figure to the nearest cent (half a cent being rounded upwards). Interest in respect of any 6 Year Non-Call Security for any Interest Period and where it is necessary to compute an amount of interest in respect of any 6 Year Non-Call Security for a period which is less than a complete year, shall be calculated on the basis of the actual number of days in the relevant period from (and including) the first day of such period to (but excluding) the last day of such period divided by the actual number of days in the period from (and including) the most recent Interest Payment Date (or, if none, the Issue Date) to (but excluding) the next succeeding Interest Payment Date.

(c) **Prevailing Interest Rate**

Unless previously redeemed or repurchased and cancelled in accordance with these Conditions and subject to the further provisions of this Condition 4, the 6 Year Non-Call Securities will bear interest on their principal amount as follows:

- (i) from (and including) the Issue Date to (but excluding) the First Reset Date, at the rate of 5.000 per cent. per annum, payable annually in arrear on each Interest Payment Date, commencing on 31 March 2015; and
- (ii) from (and including) the First Reset Date, at the applicable 6 year Swap Rate in respect of the relevant Reset Period plus:
 - (A) in respect of the period commencing on the First Reset Date to (but excluding) 31 March 2024, 3.804 per cent. per annum;
 - (B) in respect of the period commencing on 31 March 2024 to (but excluding) 31 March 2040, 4.054 per cent. per annum⁵; and
 - (C) from and including 31 March 2040, 4.804 per cent. per annum⁶,

all as determined by the Agent Bank (each a "**Subsequent Fixed Interest Rate**"), payable annually in arrear on each Interest Payment Date, commencing on 31 March 2021, subject to Condition 5,

and where:

"**6 year Swap Rate**" means, in respect of any Reset Period, the mid-swap rate as displayed on Reuters screen "ISDAFIX2" (the "**Reset Screen Page**") as at 11:00 a.m. (Central European time) on the relevant Reset Interest Determination Date.

In the event that the relevant 6 year Swap Rate does not appear on the Reset Screen Page on the relevant Reset Interest Determination Date, the 6 year Swap Rate will be the Reset Reference Bank Rate on such Reset Interest Determination Date. "**Reset Reference Bank Rate**" means the percentage rate determined by the Agent Bank on the basis of the 6 year Swap Rate Quotations provided by five leading swap dealers in the interbank market (the "**Reset Reference Banks**") to the Agent Bank at approximately 11:00 a.m. (Central European time) on the relevant Reset Interest Determination Date. If at least three quotations are provided, the 6 year Swap Rate will be determined by the Agent Bank on the basis of the arithmetic mean of the quotations provided, eliminating the highest quotation (or, in the event of equality one of the highest) and the lowest quotation (or, in the event of equality, one of the lowest).

The "**6 year Swap Rate Quotations**" means, in relation to any Reset Period, the arithmetic mean of the bid and offered rates for the annual fixed leg (calculated on a 30/360 Day Count basis) of a fixed-for-floating euro interest rate swap which (i) has a term of six years commencing on the relevant Reset Date, (ii) is in an amount that is representative of a single transaction in the relevant market at the relevant time with an acknowledged dealer of good credit in the swap market, and (iii) has a floating leg based on the 6-month EURIBOR rate (calculated on the basis of the actual number of days elapsed and a year of 360 days).

(d) **Publication of Subsequent Fixed Interest Rates**

The Issuer shall cause notice of each Subsequent Fixed Interest Rate and the corresponding amount payable per Calculation Amount determined in accordance with this Condition 4 and the relevant dates scheduled for payment to be given to the Fiscal

⁵ Step-up of 25 basis points 10 years after the Issue Date

⁶ Step-up of 75 basis points 26 years after the Issue Date

Agent, the Paying Agents, any stock exchange on which the 6 Year Non-Call Securities are for the time being listed or admitted to trading and, in accordance with Condition 14, the Holders of the 6 Year Non-Call Securities and the Coupons, in each case as soon as practicable after its determination but in any event not later than the fourth Business Day thereafter.

The relevant Subsequent Fixed Interest Rate and the dates scheduled for payment so notified may subsequently be amended (or appropriate alternative arrangements made by way of adjustment) without notice in the event of any extension or shortening of the relevant period in accordance with these Conditions.

(e) **Agent Bank and Reset Reference Banks**

With effect from the first Reset Interest Determination Date, the Issuer will maintain an Agent Bank and the number of Reset Reference Banks provided above where the Prevailing Interest Rate is to be calculated by reference to them. The name of the initial Agent Bank is The Bank of New York Mellon, London Branch and its initial specified office is One Canada Square, London E14 5AL, United Kingdom.

The Issuer may from time to time replace the Agent Bank or any Reset Reference Bank with another leading financial institution in London. If the Agent Bank is unable or unwilling to continue to act as the Agent Bank or fails duly to determine the Prevailing Interest Rate in respect of any Reset Period as provided in Condition 4(c), the Issuer shall forthwith appoint another leading financial institution in London to act as such in its place. The Agent Bank may not resign its duties or be removed without a successor having been appointed as aforesaid.

(f) **Determinations of Agent Bank Binding**

All notifications, opinions, determinations, certificates, calculations, quotations and decisions given, expressed, made or obtained for the purposes of this Condition 4 by the Agent Bank shall (in the absence of wilful default, fraud or manifest error) be binding on the Issuer, the Agent Bank the Fiscal Agent, the Paying Agents and all Holders and (in the absence as aforesaid) no liability to the Holders or the Issuer shall attach to the Agent Bank in connection with the exercise or non-exercise by it of any of its powers, duties and discretions.

5. **Optional Interest Deferral**

- (a) **Deferral of Interest Payments:** The Issuer may, subject as provided in Conditions 5(b) and 5(c) below, elect in its sole discretion to defer (in whole or in part) any Interest Payment that is otherwise scheduled to be paid on an Interest Payment Date by giving notice (a "**Deferral Notice**") of such election to the Holders in accordance with Condition 14, the Fiscal Agent and the Paying Agents not more than 14 and not less than 7 Business Days prior to the relevant Interest Payment Date. Any Interest Payment that the Issuer has elected to defer pursuant to this Condition 5(a) and that has not been satisfied is referred to as a "**Deferred Interest Payment**".

If any Interest Payment is deferred pursuant to this Condition 5(a) then such Deferred Interest Payment shall itself bear interest (such further interest together with the Deferred Interest Payment, being "**Arrears of Interest**"), at the relevant Prevailing Interest Rate applicable from time to time, from (and including) the date on which (but for such deferral) the Deferred Interest Payment would otherwise have been due to be made to (but excluding) the date on which such Deferred Interest Payment is paid in accordance with Condition 5(c), in each case such further interest being compounded on each Interest Payment Date.

Non-payment of interest deferred pursuant to this Condition 5(a) shall not constitute a default by the Issuer or the Guarantor under the 6 Year Non-Call Securities or the Guarantee or for any other purpose.

- (b) **Optional Settlement of Arrears of Interest:** Arrears of Interest may be satisfied at the option of the Issuer, in whole or in part, at any given time (the "**Optional Deferred Interest Settlement Date**") following delivery of a notice to such effect given by the Issuer to the Holders in accordance with Condition 14, the Fiscal Agent and the Paying Agents not more than 14 and no less than 7 Business Days prior to the relevant Optional Deferred Interest Settlement Date informing them of its election so to satisfy such Arrears of Interest (or part thereof) and specifying the relevant Optional Deferred Interest Settlement Date.
- (c) **Mandatory Settlement of Arrears of Interest:** Notwithstanding the provisions of Condition 5(b), the Issuer shall pay any outstanding Arrears of Interest in whole, but not in part, on the first occurring Mandatory Settlement Date following the Interest Payment Date on which any outstanding Arrears of Interest was first deferred.

Notice of the occurrence of any Mandatory Settlement Date shall be given to the Holders in accordance with Condition 14, the Fiscal Agent and the Paying Agents not more than 14 and no less than 7 Business Days prior to the relevant Mandatory Settlement Date.

If a Mandatory Settlement Date does not occur prior to the calendar day which is the fifth anniversary of the Interest Payment Date on which the relevant Deferred Interest Payment was first deferred, it is the intention, though not an obligation, of the Issuer to pay all outstanding Arrears of Interest (in whole but not in part) on the next following Interest Payment Date.

"**Mandatory Settlement Date**" means the earliest of:

- (i) as soon as reasonably practicable (but not later than the fifth business day) following the date on which a Compulsory Arrears of Interest Settlement Event occurs;
- (ii) following any Deferred Interest Payment, on the next scheduled Interest Payment Date on which the Issuer does not elect to defer in whole the interest accrued in respect of the relevant Interest Period; and
- (iii) the date on which the 6 Year Non-Call Securities are redeemed or repaid in accordance with Condition 6 or become due and payable in accordance with Condition 9.

A "**Compulsory Arrears of Interest Settlement Event**" shall have occurred if:

- (i) a Dividend Declaration is made in respect of any Junior Obligations or any Parity Obligations (other than in respect of any such dividend, distribution or payment paid or made (i) in respect of the 2002 Preferred Securities; or (ii) exclusively in Ordinary Shares of the Guarantor); or
- (ii) the Guarantor or any of its subsidiaries has repurchased, redeemed or otherwise acquired any Junior Obligations or any Parity Obligations (other than any repurchase, redemption or acquisition of any 2002 Preferred Securities),

save, in the case of (a) any such Dividend Declaration or such redemption, repurchase or acquisition that is mandatory under the terms of any such Parity Obligations; (b) any Dividend Declaration in respect of any such dividend, distribution or payment by the Issuer to the Guarantor, (c) any Dividend Declaration or repurchase which is required to be validly resolved on, declared, paid or made in respect of, share option, or free share allocation plan in each case reserved for directors, officers and/or employees of the Guarantor or any of its Affiliates or any associated liquidity agreements or any associated hedging transactions; (d) any purchase of Ordinary Shares of the Guarantor by or on behalf of the Guarantor as part of an intra-day transaction that does not result in an increase in the aggregate number of Ordinary Shares of the Guarantor held by or on behalf of the Guarantor as treasury shares at 8:30 a.m. Madrid time on the Interest Payment Date on which any outstanding Arrears of Interest was first deferred; (e) any repurchase or acquisition of Parity Obligations that is made for a consideration less than

the aggregate nominal or par value of such Parity Obligations that are purchased or acquired: (f) any repurchase or acquisition of Ordinary Shares of the Guarantor resulting from mandatory obligations or hedging of any convertible securities issued by the Issuer or the Guarantor; or (g) any repurchase or acquisition of Ordinary Shares of the Guarantor resulting from the settlement of existing equity derivatives after the Interest Payment Date on which any outstanding Arrears of Interest was first deferred.

"Dividend Declaration" means the authorisation by resolution of the general meeting of shareholders or the board of directors or other competent corporate body (as the case may be) of the Issuer or the Guarantor (as applicable) of the payment, or the making of, a dividend or other distribution or payment (or, if no such authorisation is required, the payment, or the making of, a dividend or other distribution or payment).

6. **Redemption and Purchase**

- (a) **Final redemption:** Subject to any early redemption described below, the 6 Year Non-Call Securities are undated securities with no specified maturity date. The 6 Year Non-Call Securities may not be redeemed at the option of the Issuer other than in accordance with Condition 6(b), 6(c), 6(d), 6(e), or 6(f).
- (b) **Issuer's Call Option:** The Issuer may, by giving not less than 30 nor more than 60 days' notice to the Fiscal Agent, the Paying Agents and, in accordance with Condition 14, the Holders (which notice shall be irrevocable), redeem the 6 Year Non-Call Securities in whole, but not in part, on the First Reset Date and on any Interest Payment Date thereafter at their principal amount together with any accrued and unpaid interest up to (but excluding) the Redemption Date and any outstanding Arrears of Interest.
- (c) **Redemption for Taxation Reasons:** If, immediately prior to the giving of the notice referred to below, a Tax Event or a Withholding Tax Event has occurred and is continuing, then the Issuer may, subject to having given not less than 30 nor more than 60 days' notice to the Fiscal Agent, the Paying Agents and, in accordance with Condition 14, the Holders (which notice shall be irrevocable) and subject to Condition 6(g), redeem the 6 Year Non-Call Securities in whole, but not in part, in accordance with these Conditions at any time, in each case at (i) their Early Redemption Amount (in the case of a Tax Event if the Redemption Date falls prior to the First Reset Date) or (ii) their principal amount (in the case of (a) a Withholding Tax Event or (b) a Tax Event if the Redemption Date falls on or after the First Reset Date), together, in each case, with any accrued and unpaid interest up to (but excluding) the Redemption Date and any outstanding Arrears of Interest. Upon the expiry of such notice, the Issuer shall redeem the 6 Year Non-Call Securities.
- (d) **Redemption for Accounting Reasons:** If, immediately prior to the giving of the notice referred to below, an Accounting Event has occurred and is continuing, then the Issuer may, subject to having given not less than 30 nor more than 60 days' notice to the Fiscal Agent, the Paying Agent and, in accordance with Condition 14, the Holders (which notice shall be irrevocable) and subject to Condition 6(g), redeem the 6 Year Non-Call Securities in accordance with these Conditions in whole, but not in part, at any time, in each case (i) at their Early Redemption Amount if the Redemption Date falls before the First Reset Date, or (ii) at their principal amount if the Redemption Date falls on or after the First Reset Date, together with any accrued and unpaid interest up to (but excluding) the Redemption Date and any outstanding Arrears of Interest. Upon the expiry of such notice, the Issuer shall redeem the 6 Year Non-Call Securities.
- (e) **Redemption for Rating Reasons:** If, immediately prior to the giving of the notice referred to below, a Capital Event has occurred and is continuing, then the Issuer may, subject to having given not less than 30 nor more than 60 days' notice to the Fiscal Agent, the Paying Agent and, in accordance with Condition 14, the Holders (which notice shall be irrevocable) and subject to Condition 6(g), redeem the 6 Year Non-Call Securities in accordance with these Conditions in whole, but not in part, at any time, in each case (i) at their Early Redemption Amount if the Redemption Date falls before the First Reset Date, or (ii) at their principal amount if the Redemption Date falls on or after the First

Reset Date, together with any accrued and unpaid interest up to (but excluding) the Redemption Date and any outstanding Arrears of Interest. Upon the expiry of such notice, the Issuer shall redeem the 6 Year Non-Call Securities.

- (f) **Redemption following a Substantial Purchase Event:** If, immediately prior to the giving of the notice referred to below, a Substantial Purchase Event has occurred, then the Issuer may, subject to having given not less than 30 nor more than 60 days' notice to the Fiscal Agent, the Paying Agents and, in accordance with Condition 14, the Holders (which notice shall be irrevocable) and subject to Condition 6(g), redeem the 6 Year Non-Call Securities in whole, but not in part, in accordance with these Conditions at any time, in each case at their principal amount, together with any accrued and unpaid interest up to (but excluding) the Redemption Date and any outstanding Arrears of Interest. Upon expiry of such notice, the Issuer shall redeem the 6 Year Non-Call Securities.
- (g) **Preconditions to Redemption:** Prior to serving any notice of redemption pursuant to this Condition 6 (other than Condition 6(b)), the Guarantor shall
- (i) deliver to the Fiscal Agent a certificate signed by two directors of the Guarantor stating that the relevant requirement or circumstance giving rise to the right to redeem is satisfied;
 - (ii) in the case of a Tax Event or Withholding Tax Event deliver to the Fiscal Agent an opinion of independent legal or other tax advisers to the effect set out in paragraph (i) above;
 - (iii) in the case of an Accounting Event, deliver to the Fiscal Agent the relevant opinion from the relevant accountancy firm; and
 - (iv) in the case of a Capital Event, deliver to the Fiscal Agent the relevant confirmation from the relevant Rating Agency.
- (h) **Purchase:** Each of the Issuer, the Guarantor and their respective subsidiaries may at any time purchase 6 Year Non-Call Securities in the open market or otherwise at any price (provided that, if they should be cancelled pursuant to this Condition 6(h), they are purchased together with all unmatured Coupons and all unexchanged Talons relating to them). The 6 Year Non-Call Securities so purchased may be held, re-issued or re-sold or, at the option of the relevant purchaser, surrendered to the Fiscal Agent for cancellation, but while held by or on behalf of the Issuer, the Guarantor or any such subsidiary, shall not entitle the holder to vote at any meetings of the Holders of 6 Year Non-Call Securities and shall not be deemed to be outstanding for the purposes of calculating quorums at meetings of the Holders of 6 Year Non-Call Securities or for the purposes of Condition 12.
- (i) **Cancellation:** All 6 Year Non-Call Securities so redeemed and any unmatured Coupons attached to or surrendered with them will be cancelled and may not be re-issued or re-sold.

The Guarantor intends (without thereby assuming any obligation) at any time that it or the Issuer will redeem or repurchase the 6 Year Non-Call Securities only to the extent that the aggregate principal amount of the 6 Year Non-Call Securities to be redeemed or repurchased does not exceed such part of the net proceeds received by the Guarantor or any subsidiary of the Guarantor during the 360-day period prior to the date of such redemption or repurchase from the sale or issuance by the Guarantor or such subsidiary to third party purchasers (other than group entities of the Guarantor) of securities which are assigned by S&P, at the time of sale or issuance, an aggregate "equity credit" (or such similar nomenclature used by S&P from time to time) that is equal to or greater than the "equity credit" assigned to the 6 Year Non-Call Securities to be redeemed or repurchased at the time of their issuance (but taking into account any changes in hybrid capital methodology or another relevant methodology or the interpretation thereof since the issuance of the 6 Year Non-Call Securities), unless:

- (i) *the rating assigned by S&P to the Guarantor is at least "BBB" (or such similar nomenclature then used by S&P) and the Guarantor is of the view that such rating would not fall below this level as a result of such redemption or repurchase, or*
- (ii) *in the case of a repurchase, such repurchase is of less than (a) 10 per cent. of the aggregate principal amount of the 6 Year Non-Call Securities originally issued in any period of 12 consecutive months or (b) 25 per cent. of the aggregate principal amount of the 6 Year Non-Call Securities originally issued in any period of 10 consecutive years, or*
- (iii) *the 6 Year Non-Call Securities are redeemed pursuant to a Tax Event, a Capital Event, an Accounting Event or a Withholding Tax Event, or*
- (iv) *such redemption or repurchase occurs on or after the Reset Date falling on 31 March 2040.*

7. **Payments**

- (a) **Method of Payment:** Payments of principal and interest will be made against presentation and surrender (or, in the case of a partial payment, endorsement) of 6 Year Non-Call Securities or the appropriate Coupons (as the case may be) at the specified office of any Paying Agent by transfer to a euro account maintained by the payee with a bank in city in which banks have access to the TARGET System. Payments of interest due in respect of any 6 Year Non-Call Security other than on presentation and surrender of matured Coupons shall be made only against presentation and either surrender or endorsement (as appropriate) of the relevant 6 Year Non-Call Security.
- (b) **Payments subject to fiscal laws:** All payments are subject in all cases to any applicable fiscal or other laws and regulations in the place of payment, but without prejudice to the provisions of Condition 8. No commissions or expenses shall be charged to the Holders in respect of such payments.
- (c) **Unmatured Coupons:** Upon the due date for redemption of any 6 Year Non-Call Security, unmatred Coupons relating to such 6 Year Non-Call Security (whether or not attached) shall become void and no payment shall be made in respect of them. Where any 6 Year Non-Call Security is presented for redemption without all unmatred Coupons relating to it, redemption shall be made only against the provision of such indemnity as the Issuer and the Guarantor may require.
- (d) **Exchange of Talons:** On or after the Interest Payment Date for the final Coupon forming part of a Coupon sheet issued in respect of any 6 Year Non-Call Securities, the Talon forming part of such Coupon sheet may be surrendered at the specified office of the Fiscal Agent in exchange for a further Coupon sheet (and another Talon for a further Coupon sheet) (but excluding any Coupons that may have become void pursuant to Condition 10).
- (e) **Payments on business days:** A 6 Year Non-Call Security or Coupon may only be presented for payment on a day which is a business day in the place of presentation (and, in the case of payment by transfer to a euro account, a day that is a Business Day). No further interest or other payment will be made as a consequence of the day on which the relevant 6 Year Non-Call Security or Coupon may be presented for payment under this Condition 7 falling after the due date. In this Condition "**business day**" means a day on which commercial banks and foreign exchange markets settle payments and are open in the relevant city.
- (f) **Paying Agents:** The initial Paying Agents and their initial specified offices are listed below. The Issuer and the Guarantor reserve the right at any time to vary or terminate the appointment of any Paying Agent and appoint additional or other Paying Agents, provided that they will maintain (i) a Fiscal Agent, (ii) a Paying Agent (which may be the Fiscal Agent) having specified offices in London and (iii) a Paying Agent with a

specified office in a European Union member state that will not be obliged to withhold or deduct tax pursuant to any law implementing European Council Directive 2003/48/EC or any other Directive implementing the conclusions of the ECOFIN Council meeting of 26-27 November 2000. Notice of any change in the Paying Agents or their specified offices will promptly be given to the Holders in accordance with Condition 14.

8. Taxation

- (a) **Additional Amounts:** All payments of principal and interest in respect of the 6 Year Non-Call Securities and the Coupons by the Issuer or (as the case may be) the Guarantor under the Guarantee will be made without withholding or deduction for, or on account of, any present or future taxes, duties, assessments or governmental charges (collectively, "**Taxes**") of whatever nature imposed or levied by or on behalf of The Netherlands or the Kingdom of Spain or, in each case, any authority therein or thereof having power to tax (each a "**Taxing Authority**"), unless the withholding or deduction of such Taxes is required by law.

In that event, the Issuer or, as the case may be, the Guarantor will pay such additional amounts ("**Additional Amounts**") as may be necessary in order that the net amounts received by the Holders after such withholding or deduction of Taxes shall equal the respective amounts of principal and interest which would have been received in respect of the 6 Year Non-Call Securities or (as the case may be) Coupons, in the absence of such withholding or deduction of Taxes; except that no Additional Amounts shall be payable with respect to any payment in respect of any 6 Year Non-Call Security or Coupon or (as the case may be) under the Guarantee:

- (i) to, or to a third party on behalf of, a Holder or to the beneficial owner of any 6 Year Non-Call Security or Coupon who is liable for Taxes in respect of such 6 Year Non-Call Security or Coupon by reason of his having some connection with The Netherlands or the Kingdom of Spain other than the mere holding of the 6 Year Non-Call Security or Coupon;
- (ii) presented for payment more than 30 days after the Relevant Date except to the extent that the relevant Holder or the beneficial owner thereof would have been entitled to such Additional Amounts on presenting the same for payment on the thirtieth such day;
- (iii) in relation to any estate, inheritance, gift, sales, transfer or similar Taxes;
- (iv) while the 6 Year Non-Call Securities are represented by Global 6 Year Non-Call Securities and the Global 6 Year Non-Call Securities are deposited with a common depository for Euroclear and/or Clearstream, Luxembourg, to, or to a third party on behalf of, a Holder or to the beneficial owner of any 6 Year Non-Call Security or Coupon if the Issuer or the Guarantor does not receive in a timely manner a duly executed and completed certificate from the Fiscal Agent, pursuant to Law 13/1985 of May 25, as amended ("**Law 13/1985**"), and Royal Decree 1065/2007 of July 27, as amended by Royal Decree 1145/2011 of July 29, and any implementing legislation or regulation;
- (v) while the 6 Year Non-Call Securities are represented by Definitive 6 Year Non-Call Securities, where such withholding or deduction of Taxes is imposed, withheld or deducted by reason of the failure of the Holder or the beneficial owner of any 6 Year Non-Call Security or Coupon to comply with the Issuer's or the Guarantor's request addressed to the Holder or the beneficial owner to provide a valid certificate of tax residence duly issued by the tax authorities of the country of tax residence of the beneficial owner of any 6 Year Non-Call Security or Coupon, which the Holder or the beneficial owner is required to provide by the applicable tax laws and regulations of the relevant Taxing Authority as a precondition to exemption from, or reduction in the rate of deduction or withholding of, Taxes imposed by such relevant Taxing Authority

- (vi) presented for payment in the Kingdom of Spain;
- (vii) where such withholding or deduction is imposed on a payment to an individual and is required to be made pursuant to European Council Directive 2003/48/EC on the taxation of savings income or any other Directive implementing the conclusions of the ECOFIN Council meeting of 26 to 27 November 2000 on the taxation of savings income or any law implementing or complying with, or introduced in order to conform to, such Directive; or
- (viii) presented for payment by or on behalf of a Holder who would have been able to avoid such withholding or deduction by presenting the relevant 6 Year Non-Call Security to another Paying Agent in a Member State of the European Union.

In addition, Additional Amounts will not be payable with respect to (i) any Taxes that are imposed in respect of any combination of the items set forth above and to (ii) any Holder of any 6 Year Non-Call Security who is a fiduciary, a partnership, a limited liability company or other than the sole beneficial owner of that payment, to the extent that payment would be required by the laws of the relevant Taxing Authority to be included in the income, for tax purposes, of a beneficiary or settlor with respect to the fiduciary, a member of that partnership, an interest holder in that limited liability company or a beneficial owner who would not have been entitled to the Additional Amounts had it been the Holder.

- (b) **Tax Credit Payment:** If any Additional Amounts are paid by the Issuer or, as the case may be, the Guarantor under this Condition for the benefit of any Holder and such Holder, in its sole discretion, determines that it has obtained (and has derived full use and benefit from) a credit against, a relief or remissions for, or repayment of, any tax, then, if and to the extent that such Holder, in its sole opinion, determines that (i) such credit, relief, remission or repayment is in respect of or calculated with reference to the Additional Amounts paid pursuant to this Condition; and (ii) its tax affairs for its tax year in respect of which such credit, relief, remission or repayment was obtained have been finally settled, such Holder shall, to the extent that it can do so without prejudice to the retention of the amount of such credit, relief, remission or repayment, pay to the Issuer or, as the case may be, the Guarantor such amount as such Holder shall in its sole opinion, determine to be the amount which will leave such Holder (after such payment) in no worse after tax position than it would have been in had the additional payment in question not been required to be made by the Issuer or, as the case may be, the Guarantor.
- (c) **Tax Credit Clawback:** If any Holder makes any payment to the Issuer or, as the case may be, the Guarantor pursuant to this Condition and such Holder subsequently determines in its sole opinion, that the credit, relief, remission or repayment in respect of which such payment was made was not available or has been withdrawn or that it was unable to use such credit, relief, remission or repayment in full, the Issuer or, as the case may be, the Guarantor shall reimburse such Holder such amount as such Holder determines, in its sole opinion, is necessary to place it in the same after tax position as it would have been in if such credit, relief, remission or repayment had been obtained and fully used and retained by such Holder, such amount not exceeding in any case the amount paid by the Holder to the Issuer or, as the case may be, the Guarantor.
- (d) **Tax Affairs:** Nothing in Conditions 8(b) and (c) above shall interfere with the right of any Holder to arrange its tax or any other affairs in whatever manner it thinks fit, oblige any Holder to claim any credit, relief, remission or repayment in respect of any payment made under this Condition in priority to any credit, relief, remission or repayment available to it nor oblige any Holder to disclose any information relating to its tax or other affairs or any computations in respect thereof.
- (e) **Definitions:** References in these Conditions to (i) "Principal" shall be deemed to include all amounts in the nature of principal payable pursuant to Condition 7 or any amendment or supplement to it; (ii) "interest" shall be deemed to include all Arrears of Interest and all other amounts payable pursuant to Condition 4 or any amendment or supplement to it; and (iii) "principal" and/or "interest" shall be deemed to include any Additional Amounts.

- (f) **Applicable law for Spanish tax purposes:** The Guarantor will apply Additional Provision Two of Law 13/1985 to the 6 Year Non-Call Securities for Spanish tax purposes.

Payments in respect of the 6 Year Non-Call Securities and the Coupons by the Guarantor under the Guarantee will be exempt from Spanish Non-Resident Income Tax to the extent that the Holder or beneficial owner is not acting through a permanent establishment in Spain.

The Guarantor will comply with the reporting obligations set out in Section 3 of Additional Provision Two of Law 13/1985 in respect of Holders or beneficial owners who are taxpayers of the Spanish Individual Income Tax or taxpayers of the Spanish Corporation Tax, as well as taxpayers of the Spanish Non-resident Income Tax who hold the 6 Year Non-Call Securities through a permanent establishment located in Spanish territory.

9. **Enforcement Events and No Events of Default**

There are no events of default in respect of the 6 Year Non-Call Securities.

However, if an Issuer Winding-up occurs, or an order is made or an effective resolution passed for the winding-up, dissolution or liquidation of the Guarantor, or the Guarantor becomes insolvent ("*en estado de insolvencia*") pursuant to article 2 of the Spanish insolvency law, any Holder of a 6 Year Non-Call Security, in respect of such 6 Year Non-Call Security and provided that such Holder does not contravene a previously adopted Extraordinary Resolution (if any) may, by written notice to the Issuer and the Guarantor, declare that such 6 Year Non-Call Security and all interest then accrued but unpaid on such 6 Year Non-Call Security shall be forthwith due and payable, whereupon the same shall become immediately due and payable, together with all interest accrued thereon.

In such case the Holder of a 6 Year Non-Call Security may, at its sole discretion, institute steps in order to obtain a judgment against the Issuer and/or the Guarantor for any amounts due in respect of the 6 Year Non-Call Securities, including the institution of proceedings for the declaration of insolvency ("*declaración de concurso*") under Spanish insolvency law of the Guarantor and/or proving and/or claiming in an Issuer Winding-up or in the winding-up, dissolution, liquidation or insolvency proceeding of the Guarantor for such amount.

Each Holder may, at its discretion and without further notice, institute such proceedings as it may think fit to enforce any term or condition binding on the Issuer or the Guarantor under the 6 Year Non-Call Securities or the Guarantee but in no event shall the Issuer or the Guarantor by the virtue of such proceedings be obliged to pay any sum or sums sooner than the same would otherwise have been payable by it.

No remedy against the Issuer or the Guarantor, other than as referred to in this Condition 9 shall be available to the Holders, whether for the recovery of amounts owing in respect of the 6 Year Non-Call Securities or the Guarantee or in respect of any other breach by the Issuer or the Guarantor of any of their respective other obligations under or in respect of the 6 Year Non-Call Securities or the Guarantee.

10. **Prescription**

Claims in respect of principal and interest or any other amount will become void unless presentation for payment is made as required by Condition 7 within a period of 10 years in the case of principal (or any other amount in the nature of principal) and five years in the case of interest (or any other amount in the nature of interest, including Arrears of Interest) from the appropriate Relevant Date.

11. **Replacement of 6 Year Non-Call Securities and Coupons**

If any 6 Year Non-Call Security or Coupon is lost, stolen, mutilated, defaced or destroyed it may be replaced at the specified office of the Fiscal Agent subject to all applicable laws and stock exchange or other relevant authority requirements, upon payment by the claimant of the expenses

incurred in connection with such replacement and on such terms as to evidence, security, indemnity and otherwise as the Issuer, the Guarantor and the Fiscal Agent may require (provided that the requirement is reasonable in the light of prevailing market practice). Mutilated or defaced 6 Year Non-Call Securities or Coupons must be surrendered before replacements will be issued. In case any such lost, stolen, mutilated, defaced or destroyed Coupon has become or is about to become due and payable, the Issuer in its discretion may, instead of delivering replacements therefor, pay such Coupon when due.

12. **Meetings of Holders of 6 Year Non-Call Securities and Modification**

- (a) **Meetings of Holders of 6 Year Non-Call Securities:** The Fiscal Agency Agreement contains provisions for convening meetings of Holders of 6 Year Non-Call Securities to consider matters affecting their interests, including the sanctioning by Extraordinary Resolution (as defined in the Fiscal Agency Agreement) of a modification of any of these Conditions. Such a meeting may be convened by Holders of 6 Year Non-Call Securities holding not less than one twentieth in principal amount of the 6 Year Non-Call Securities for the time being outstanding. The quorum for any meeting convened to consider an Extraordinary Resolution will be one or more persons holding or representing at least two thirds of the aggregate principal amount of the 6 Year Non-Call Securities for the time being outstanding, or at any adjourned meeting one or more persons being or representing Holders of 6 Year Non-Call Securities whatever the principal amount of the 6 Year Non-Call Securities held or represented. Any Extraordinary Resolution duly passed shall be binding on Holders of 6 Year Non-Call Securities (whether or not they were present at the meeting at which such resolution was passed) and on all Holders of Coupons.

The Fiscal Agency Agreement provides that a resolution in writing signed by or on behalf of the holders of not less than 90 per cent. in principal amount of the 6 Year Non-Call Securities outstanding shall for all purposes be as valid and effective as an Extraordinary Resolution passed at a meeting of Holders of 6 Year Non-Call Securities duly convened and held. Such a resolution in writing may be contained in one document or several documents in the same form, each signed by or on behalf of one or more Holders of 6 Year Non-Call Securities.

- (b) **Modification:** The 6 Year Non-Call Securities, these Conditions, the Deed of Covenant and the Deed of Guarantee may be amended without the consent of the Holders of 6 Year Non-Call Securities to correct a manifest error. No other modification may be made to the 6 Year Non-Call Securities, these Conditions the Deed of Covenant or the Deed of Guarantee except with the sanction of a resolution of the Holders of the 6 Year Non-Call Securities.

In addition, the parties to the Fiscal Agency Agreement may agree to modify any provision thereof, but the Issuer shall not agree, without the consent of the Holders of 6 Year Non-Call Securities, to any such modification unless, in the opinion of the Issuer and the Guarantor, (i) it is of a formal, minor or technical nature; (ii) it is made to correct a manifest error; or (iii) it is not materially prejudicial to the interests of the Holders of 6 Year Non-Call Securities.

13. **Further Issues**

The Issuer may from time to time without the consent of the Holders create and issue further securities either having the same terms and conditions as the 6 Year Non-Call Securities in all respects (or in all respects except for the first payment of interest on them) and so that such further issue shall be consolidated and form a single series with the outstanding securities of any series (including the 6 Year Non-Call Securities) or upon such terms as the Issuer may determine at the time of their issue. References in these Conditions to the 6 Year Non-Call Securities include (unless the context requires otherwise) any other securities issued pursuant to this Condition and forming a single series with the 6 Year Non-Call Securities.

14. **Notices**

Notices to Holders of 6 Year Non-Call Securities will be deemed to be validly given if published in a leading daily newspaper having general circulation in London (which is expected to be the *Financial Times*) or, if such publication is not practicable, if published in a leading English language daily newspaper having general circulation in Europe. The Issuer shall also ensure that all notices are duly published in a manner which complies with the rules and regulations of any stock exchange or other relevant authority on which the 6 Year Non-Call Securities are for the time being listed and/or admitted to trading. Any such notice shall be deemed to have been validly given on the date of the first such publication or, if published more than once on the first date on which publication is made.

Notwithstanding the above, while all the 6 Year Non-Call Securities are represented by Global 6 Year Non-Call Securities and the Global 6 Year Non-Call Securities are deposited with a common depository for Euroclear and/or Clearstream, Luxembourg, notices to Holders of 6 Year Non-Call Securities may be given by delivery of the relevant notice to Euroclear or Clearstream, Luxembourg in accordance with their respective rules and operating procedures, and such notices shall be deemed to have been given to Holders on the date of delivery to Euroclear and/or Clearstream, Luxembourg. Holders of Coupons will be deemed for all purposes to have notice of the contents of any notice given to the Holders of 6 Year Non-Call Securities in accordance with this Condition.

15. **Contracts (Rights of Third Parties) Act 1999**

No person shall have any right to enforce any term or condition of the 6 Year Non-Call Securities under the Contracts (Rights of Third Parties) Act 1999.

16. **Governing Law**

- (a) **Governing Law:** The Fiscal Agency Agreement, the 6 Year Non-Call Securities, the Coupons and the Guarantee and any non-contractual obligations arising out of or in connection with them are governed by and shall be construed in accordance with English law, other than the provisions of Condition 2(b) which are governed by and construed in accordance with the laws of The Netherlands, and the provisions of Conditions 3(b) and 3(c), and the corresponding provisions of the Guarantee, which are governed by and construed in accordance with the laws of the Kingdom of Spain.
- (b) **Jurisdiction:** The courts of England have exclusive jurisdiction to settle any dispute (a "**Dispute**") arising from or connected with the 6 Year Non-Call Securities or the Coupons (including a dispute relating to the existence, validity or termination of the 6 Year Non-Call Securities or any non-contractual obligations arising out of or in connection with the 6 Year Non-Call Securities or the consequences of their nullity). The Issuer agrees that the courts of England are the most appropriate and convenient courts to settle any Dispute and, accordingly, that it will not argue to the contrary. This Condition is for the benefit of the Holders only. As a result, nothing in this Condition 16 prevents any Holder from taking proceedings relating to a Dispute ("**Proceedings**") in any other courts with jurisdiction. To the extent allowed by law, Holders may take concurrent Proceedings in any number of jurisdictions.
- (c) **Agent for Service of Process:** The Issuer agrees that the documents which start any Proceedings and any other documents required to be served in relation to those Proceedings may be served on it by being delivered to Telefónica UK Limited, 260 Bath Road, Slough, SL1 4DX, United Kingdom, or, if different, its registered office for the time being or at any address of the Issuer in England at which process may be served on it. If such person is not or ceases to be effectively appointed to accept service of process on behalf of the Issuer, the Issuer shall forthwith appoint a further person in England to accept service of process on its behalf in England and notify the name and address of such person to the Fiscal Agent and, failing such appointment within 15 days, any Holder shall be entitled to appoint such a person by written notice addressed to the Issuer and delivered to the Issuer or to the specified office of the Fiscal Agent. Nothing in this

paragraph shall affect the right of any Holder to serve process in any other manner permitted by law. This Condition applies to Proceedings in England.

17. **Definitions**

In these Conditions:

"**2002 Preferred Securities**" means the €2,000,000,000 preferred securities (*participaciones preferentes*) issued by Telefónica Finance USA LLC on 30 December 2002 (*of which, as of the date hereof, €58,765,000 were outstanding*);

"**2013 Non-Call Securities**" means the September 2013 5 Year Non-Call Securities, the September 2013 8 Year Non-Call Securities and the November 2013 Non-Call Securities;

"**30/360 Day Count**" means, in respect of any period, the number of days in the relevant period, from (and including) the first day in such period to (but excluding) the last day in such period (such number of days being calculated on the basis of a 360 day year consisting of 12 months of 30 days each), divided by 360;

"**6 year Swap Rate**" has the meaning given to it in Condition 4(c);

"**6 year Swap Rate Quotations**" has the meaning given to it in Condition 4(c);

"**10 Year Non-Call Securities**" means the €1,000,000,000 Undated 10 Year Non-Call Deeply Subordinated Guaranteed Fixed Rate Reset Securities issued by the Issuer concurrently with the 6 Year Non-Call Securities and unconditionally and irrevocably guaranteed on a subordinated basis by the Guarantor;

an "**Accounting Event**" shall be deemed to occur if the Issuer or the Guarantor has received, and notified the Holders in accordance with Condition 14 that it has so received, an opinion of a recognised accountancy firm of international standing, stating that, as a result of a change in the accounting rules or methodology effective after the Issue Date, the 6 Year Non-Call Securities must not or must no longer be recorded as "equity" pursuant to IFRS-EU or any other accounting standards that may replace IFRS-EU for the purposes of the consolidated financial statements of the Guarantor;

"**Additional Amounts**" has the meaning given to it in Condition 8(a);

"**Affiliates**" means an entity that directly, or indirectly through one or more intermediaries, controls, or is controlled by, or is under common control with, the Guarantor;

"**Arrears of Interest**" has the meaning given to it in Condition 5(a);

"**business day**" has the meaning given to it in Condition 7(e);

"**Business Day**" means a day, other than a Saturday, Sunday or public holiday, on which the Target System is operating;

"**Calculation Amount**" has the meaning given to it in Condition 4(b);

a "**Capital Event**" shall be deemed to occur if the Issuer or the Guarantor has received, and notified the Holders in accordance with Condition 14 that it has so received, confirmation from any Rating Agency that, due to (i) any amendment to, clarification of, or change in hybrid capital methodology or a change in the interpretation thereof, in each case occurring or becoming effective after the Issue Date; or (ii) the application of a different hybrid capital methodology or set of criteria by the relevant Rating Agency after the Issue Date (due to changes in the rating previously assigned to the Issuer and/or the Guarantor or to any other reasons), the 6 Year Non-Call Securities will no longer be eligible for the same or a higher amount of "equity credit" (or such other nomenclature that the relevant Rating Agency may then use to describe the degree to which an instrument exhibits the characteristics of an ordinary share) attributed to the 6 Year Non-Call Securities at the Issue Date;

"**Compulsory Arrears of Interest Settlement Event**" has the meaning given to it in Condition 5(c);

"**Condition**" means the terms and conditions of the 6 Year Non-Call Securities;

"**Deferral Notice**" has the meaning given to it in Condition 5(a);

"**Deferred Interest Payment**" has the meaning given to it in Condition 5(a);

"**Early Redemption Amount**" means in respect of a redemption of the 6 Year Non-Call Securities following the occurrence of a Tax Event, an Accounting Event or a Capital Event, 101 per cent. of the principal amount of such 6 Year Non-Call Securities;

"**First Reset Date**" means 31 March 2020;

"**Fitch Ratings**" means Fitch Ratings Limited;

"**Further 6 Year Non-Call Securities**" means any 6 Year Non-Call Securities issued pursuant to Condition 13 and forming a single series with the outstanding 6 Year Non-Call Securities;

"**Guarantor**" means Telefónica, S.A.;

"**Holder**" has the meaning given to it in Condition 1(b);

"**IFRS-EU**" means International Financial Reporting Standards, as adopted by the European Union;

"**Interest Payment**" means, in respect of an interest payment on an Interest Payment Date, the amount of interest payable on the presentation and surrender of the relevant Coupon for the relevant Interest Period in accordance with Condition 4;

"**Interest Payment Date**" means 31 March in each year;

"**Interest Period**" means the period beginning on (and including) the Issue Date and ending on (but excluding) the first Interest Payment Date and each successive period beginning on (and including) an Interest Payment Date and ending on (but excluding) the next succeeding Interest Payment Date;

"**Issue Date**" means 31 March 2014;

"**Issuer**" means Telefónica Europe B.V.;

"**Issuer Winding-up**" means a situation where (i) an order is made or a decree or resolution is passed for the winding-up, liquidation or dissolution of the Issuer, except for the purposes of a solvent merger, reconstruction or amalgamation, or (ii) a trustee (*curator*) is appointed by the competent District Court in The Netherlands in the event of bankruptcy (*faillissement*) affecting the whole or a substantial part of the undertaking or assets of the Issuer and such appointment is not discharged within 30 days;

"**Junior Obligations**" means the Junior Obligations of the Guarantor and the Junior Obligations of the Issuer;

"**Junior Obligations of the Guarantor**" means all obligations of the Guarantor issued or incurred directly or indirectly by it, which rank or are expressed to rank junior to the Guarantee, including Ordinary Shares of the Guarantor;

"**Junior Obligations of the Issuer**" means all obligations of the Issuer, issued or incurred directly or indirectly by it, which rank or are expressed to rank junior to the 6 Year Non-Call Securities, including (i) Ordinary Shares of the Issuer, (ii) Preferred Shares of the Issuer, if any, and, (iii) if there are any Preferred Shares of the Issuer outstanding and any 2013 Non-Call Securities outstanding which by their terms are expressed to rank *pari passu* with Preferred Shares of the Issuer, such 2013 Non-Call Securities;

"**Law 13/1985**" means the Additional Provision Two of Law 13/1985 of the Kingdom of Spain (as amended or replaced from time to time);

"**Mandatory Settlement Date**" has the meaning given to it in Condition 5(c);

"**Moody's**" means Moody's Investors Service Limited;

"**November 2013 Non-Call Securities**" means the £600,000,000 Undated 7 Year Non-Call Deeply Subordinated Guaranteed Fixed Rate Reset Securities (ISIN: XS0997326441) issued by the Issuer on 26 November 2013 and unconditionally and irrevocably guaranteed on a subordinated basis by the Guarantor;

"**Ordinary Shares of the Guarantor**" means ordinary shares in the capital of the Guarantor, having at the Issue Date a nominal value of €1.00 each;

"**Ordinary Shares of the Issuer**" means ordinary shares in the capital of the Issuer, having on the Issue Date a nominal amount of €460.00 each;

"**Parity Obligations**" means the Parity Obligations of the Guarantor and the Parity Obligations of the Issuer;

"**Parity Obligations of the Guarantor**" means any and all present or future series of preferred securities (*participaciones preferentes*) issued directly by the Guarantor or indirectly through a wholly-owned subsidiary with the guarantee of the Guarantor in accordance with Law 13/1985, obligations equivalent to preferred securities (*participaciones preferentes*) issued directly by the Guarantor or indirectly through a wholly-owned subsidiary with the guarantee of the Guarantor (whether issued under Law 13/1985 or any other law or regulation of Spain or of any other jurisdiction) (which include the guarantee granted by the Guarantor in connection with the 2002 Preferred Securities) and obligations of the Guarantor, issued directly by it or indirectly through a wholly-owned subsidiary with the guarantee of the Guarantor, which rank or are expressed to rank *pari passu* with the Guarantee (which include the guarantees granted by the Guarantor in connection with the 10 Year Non-Call Securities and the 2013 Non-Call Securities);

"**Parity Obligations of the Issuer**" means any obligations of the Issuer, issued or incurred directly or indirectly by it, which rank, or are expressed to rank, *pari passu* with the 6 Year Non-Call Securities including (i) the 10 Year Non-Call Securities and, (ii) the 2013 Non-Call Securities, except in the event that such 2013 Non-Call Securities are Junior Obligations of the Issuer (as defined above);

"**Preferred Shares of the Issuer**" means any preference shares in the capital of the Issuer (and, if divided into classes, each class thereof);

"**Prevailing Interest Rate**" means the rate of interest payable on the 6 Year Non-Call Securities applicable from time to time pursuant to Condition 4;

"**Proceedings**" has the meaning given to it in Condition 16(b);

"**Rating Agency**" means S&P, Moody's or Fitch Ratings;

"**Redemption Date**" means the date fixed for redemption of the 6 Year Non-Call Securities pursuant to Condition 6;

"**Relevant Date**" means (i) in respect of any payment other than a sum to be paid by the Issuer or the Guarantor in a winding-up or administration of the Issuer or Guarantor, as the case may be, the date on which such payment first becomes due and payable, but if the full amount of moneys payable on such date has not been received by the Fiscal Agent on or prior to such date, the Relevant Date means the date on which such moneys shall have been so received and notice to that effect shall have been given to the Holders of 6 Year Non-Call Securities in accordance with Condition 14 and (ii) in respect of a sum to be paid by the Issuer or the Guarantor in a winding-up or administration of the Issuer or the Guarantor, as the case may be, the date that is one day prior to the date on which an order is made or a resolution is passed for the winding-up, or in the case of an administration, one day prior to the date on which any dividend is distributed;

"Reset Date" means the First Reset Date and each date falling on the sixth anniversary thereafter;

"Reset Interest Determination Date" means, in respect of any Reset Period, the day falling two Business Days prior to the beginning of the relevant Reset Period;

"Reset Period" means each period from and including the First Reset Date to but excluding the next following Reset Date and thereafter from and including each Reset Date to but excluding the next following Reset Date;

"Reset Reference Banks" has the meaning given to it in Condition 4(c);

"Reset Reference Bank Rate" has the meaning given to it in Condition 4(c);

"Reset Screen Page" has the meaning given to it in Condition 4(c);

"S&P" means Standard & Poor's Credit Market Services Europe Limited;

"Senior Obligations of the Guarantor" means all obligations of the Guarantor, including subordinated obligations of the Guarantor according to Spanish insolvency law, other than Parity Obligations of the Guarantor and Junior Obligations of the Guarantor;

"Senior Obligations of the Issuer" means all obligations of the Issuer, including subordinated obligations of the Issuer according to Dutch insolvency law, other than Parity Obligations of the Issuer and Junior Obligations of the Issuer;

"September 2013 5 Year Non-Call Securities" means the €1,125,000,000 Undated 5 Year Non-Call Deeply Subordinated Guaranteed Fixed Rate Reset Securities (ISIN: XS0972570351) issued by the Issuer on 18 September 2013 and unconditionally and irrevocably guaranteed on a subordinated basis by the Guarantor;

"September 2013 8 Year Non-Call Securities" means the €625,000,000 Undated 8 Year Non-Call Deeply Subordinated Guaranteed Fixed Rate Reset Securities (ISIN: XS0972588643) issued by the Issuer on 18 September 2013 and unconditionally and irrevocably guaranteed on a subordinated basis by the Guarantor;

"Subordinated Loan" means the subordinated loan made by the Issuer to the Guarantor dated 31 March 2014, pursuant to which the proceeds of the issue of the 6 Year Non-Call Securities are on-lent to the Guarantor;

a **"Substantial Purchase Event"** shall be deemed to have occurred if at least 80 per cent. of the aggregate principal amount of the 6 Year Non-Call Securities originally issued (which for these purposes shall include any Further 6 Year Non-Call Securities) is purchased by the Issuer, the Guarantor or any subsidiary of the Guarantor (and in each case is cancelled in accordance with Condition 6(i));

a **"Tax Event"** shall be deemed to have occurred if, as a result of a Tax Law Change, in respect of (i) the Issuer's obligation to make any payment under the 6 Year Non-Call Securities (including any Interest Payment) on the next following Interest Payment Date; or (ii) the obligation of the Guarantor to make any payment in favour of the Issuer under the Subordinated Loan on the next following due date for such payment, the Issuer or the Guarantor (as the case may be) would no longer be entitled to claim a deduction in respect of computing its tax liabilities in The Netherlands or in Spain (as the case may be), or such entitlement is materially reduced.

For the avoidance of doubt, a Tax Event shall not occur if payments of interest under the Subordinated Loan by the Guarantor are not deductible in whole or in part for Spanish corporate income tax purposes solely as a result of general tax deductibility limits set forth by Article 20 of the consolidated text of the Spanish Corporate Income Tax Law, approved by the Royal Legislative Decree 4/2004, dated 5 March, as at 24 March 2014;

"Tax Law Change" means a change in or proposed change in, or amendment to, or proposed amendment to, the laws or regulations of The Netherlands or Spain or, in either case, any

political subdivision or any authority thereof or therein having power to tax, including, without limitation, any treaty to which The Netherlands or Spain is a party, or any change in the official or generally published interpretation of such laws or regulations, including a decision of any court or tribunal, or any interpretation or pronouncement by any relevant tax authority that provides for a position with respect to such laws or regulations or interpretations thereof that differs from the previously generally accepted position in relation to similar transactions, which change, amendment or interpretation becomes or would become, effective after 24 March 2014;

"Taxing Authority" has the meaning given to it in Condition 8(a); and

a **"Withholding Tax Event"** shall be deemed to occur if as a result of a Tax Law Change, in making any payments in respect of the 6 Year Non-Call Securities or the Guarantee the Issuer or the Guarantor has paid or will or would on the next Interest Payment Date be required to pay Additional Amounts in respect of the 6 Year Non-Call Securities or the Guarantee that cannot be avoided by the Issuer or the Guarantor, as the case may be, taking measures reasonably available to it.

TERMS AND CONDITIONS OF THE 10 YEAR NON-CALL SECURITIES

The following are the terms and conditions substantially in the form in which they will be endorsed on the 10 Year Non-Call Securities. Sentences in italics shall not form part of these terms and conditions.

The issue of the 10 Year Non-Call Securities was authorised by a resolution of the Board of Managing Directors of the Issuer dated 14 March 2014 and the guarantee of the 10 Year Non-Call Securities was authorised by a resolution of the Delegated Committee of the Board of Directors of the Guarantor dated 14 March 2014, by a resolution of the Board of Directors of the Guarantor dated 31 May 2013, and by a resolution of the shareholders acting through the General Shareholders' Meeting of the Guarantor dated 31 May 2013. A fiscal agency agreement dated 31 March 2014 (the "**Fiscal Agency Agreement**") has been entered into in relation to the 10 Year Non-Call Securities between the Issuer, the Guarantor, The Bank of New York Mellon, London Branch as fiscal agent, The Bank of New York Mellon, London Branch as agent bank and the paying agents named therein. The fiscal agent, the agent bank and the paying agents for the time being are referred to below respectively as the "**Fiscal Agent**", the "**Agent Bank**" and the "**Paying Agents**" (which expression shall include the Fiscal Agent). The Fiscal Agency Agreement includes the form of the 10 Year Non-Call Securities and the coupons relating to them (the "**Coupons**", which expression includes, where the context so permits, talons for further coupons (the "**Talons**")). Copies of the Fiscal Agency Agreement are available for inspection during normal business hours at the specified offices of the Paying Agents. The Holders of the 10 Year Non-Call Securities and the Holders of the Coupons (each as defined in Condition 1(b) below) (whether or not attached to the relevant 10 Year Non-Call Securities) are deemed to have notice of all the provisions of the Fiscal Agency Agreement applicable to them.

1. **Form, Denomination and Title**

- (a) **Form and denomination:** The 10 Year Non-Call Securities are serially numbered and in bearer form in the denominations of €100,000, each with Coupons attached on issue.
- (b) **Title:** Title to the 10 Year Non-Call Securities and Coupons passes by delivery. The holder of any 10 Year Non-Call Security or Coupon (a "**Holder**") will (except as otherwise required by applicable law or regulatory requirement) be treated as its absolute owner for all purposes (whether or not it is overdue and regardless of any notice of ownership, trust or any interest in it, any writing on it, or its theft or loss) and no person shall be liable for so treating the Holder.

2. **Status and Subordination of the 10 Year Non-Call Securities and Coupons**

- (a) **Status of the 10 Year Non-Call Securities and Coupons:** The 10 Year Non-Call Securities and the Coupons constitute direct, unsecured and subordinated obligations of the Issuer (senior only to Junior Obligations of the Issuer) and shall at all times rank *pari passu* and without any preference among themselves.
- (b) **Subordination of the 10 Year Non-Call Securities:** In the event of an Issuer Winding-up, the rights and claims of the Holders against the Issuer in respect of or arising under the 10 Year Non-Call Securities and the Coupons will rank (i) junior to the claims of all holders of Senior Obligations of the Issuer, (ii) *pari passu* with the claims of holders of all Parity Obligations of the Issuer and (iii) senior to the claims of holders of all Junior Obligations of the Issuer.

Subject to applicable law, no Holder may exercise or claim any right of set-off in respect of any amount owed to it by the Issuer arising under or in connection with the 10 Year Non-Call Securities or the Coupons and each Holder shall, by virtue of being the Holder, be deemed to have waived all such rights of set-off. This Condition 2(b) is an irrevocable stipulation (*derdenbeding*) for the benefit of the creditors of Senior Obligations of the Issuer and each such creditor may rely on and enforce this Condition 2(b) under Section 6:253 of the Dutch Civil Code.

The Issuer does not have any Preferred Shares of the Issuer outstanding and the Issuer's Articles of Association do not provide for the issuance of such shares by the Issuer. For

so long as any of the 10 Year Non-Call Securities remains outstanding, the Guarantor and the Issuer do not intend to issue any Preferred Shares of the Issuer.

3. **Guarantee, Status and Subordination of the Guarantee**

- (a) **Guarantee:** The Guarantor has unconditionally and irrevocably guaranteed the due payment of all sums expressed to be payable by the Issuer under the 10 Year Non-Call Securities and the Coupons on a subordinated basis. Its obligations in that respect (the "**Guarantee**") are set out in the deed of guarantee dated the Issue Date and made by the Guarantor for the benefit of the Holders.
- (b) **Status of the Guarantee:** The payment obligations of the Guarantor under the Guarantee constitute direct, unsecured and subordinated obligations of the Guarantor (senior only to Junior Obligations of the Guarantor) and shall at all times rank *pari passu* and without any preference among themselves.
- (c) **Subordination of the Guarantee:** Subject to mandatory provisions of Spanish applicable law, in the event of the Guarantor being declared in insolvency (*concurso*) under Spanish insolvency law, the rights and claims of Holders against the Guarantor in respect of or arising under the Guarantee will rank (i) junior to the claims of the holders of all Senior Obligations of the Guarantor, (ii) *pari passu* with the claims of the holders of all Parity Obligations of the Guarantor and (iii) senior to the claims of the holders of all Junior Obligations of the Guarantor.

4. **Interest Payments**

(a) **General**

The 10 Year Non-Call Securities bear interest at the Prevailing Interest Rate from (and including) 31 March 2014 (the "**Issue Date**") in accordance with the provisions of this Condition 4.

Subject to Condition 5, interest shall be payable on the 10 Year Non-Call Securities with respect to any Interest Period annually in arrear on each Interest Payment Date in each case as provided in this Condition 4.

(b) **Interest Accrual**

The 10 Year Non-Call Securities will cease to bear interest from (and including) the date of redemption thereof pursuant to Condition 6 unless, upon due presentation, payment of all amounts due in respect of the 10 Year Non-Call Securities is not made, in which event interest shall continue to accrue in respect of unpaid amounts on the 10 Year Non-Call Securities, both before and after judgment, and shall be payable, as provided in these Conditions up to (but excluding) the Relevant Date.

Interest in respect of any 10 Year Non-Call Security shall be calculated per €100,000 in principal amount thereof (the "**Calculation Amount**"). The interest payable on each 10 Year Non-Call Security on any Interest Payment Date shall be calculated by multiplying the Prevailing Interest Rate for the Interest Period ending immediately prior to such Interest Payment Date by the Calculation Amount and rounding the resulting figure to the nearest cent (half a cent being rounded upwards). Interest in respect of any 10 Year Non-Call Security for any Interest Period and where it is necessary to compute an amount of interest in respect of any 10 Year Non-Call Security for a period which is less than a complete year, shall be calculated on the basis of the actual number of days in the relevant period from (and including) the first day of such period to (but excluding) the last day of such period divided by the actual number of days in the period from (and including) the most recent Interest Payment Date (or, if none, the Issue Date) to (but excluding) the next succeeding Interest Payment Date.

(c) **Prevailing Interest Rate**

Unless previously redeemed or repurchased and cancelled in accordance with these Conditions and subject to the further provisions of this Condition 4, the 10 Year Non-Call Securities will bear interest on their principal amount as follows:

- (i) from (and including) the Issue Date to (but excluding) the First Reset Date, at the rate of 5.875 per cent. per annum, payable annually in arrear on each Interest Payment Date, commencing on 31 March 2015; and
- (ii) from (and including) the First Reset Date, at the applicable 10 year Swap Rate in respect of the relevant Reset Period plus:
 - (A) in respect of the period commencing on the First Reset Date to (but excluding) 31 March 2044, 4.301 per cent. per annum;⁷ and
 - (B) from and including 31 March 2044, 5.051 per cent. per annum⁸,all as determined by the Agent Bank payable annually in arrear on each Interest Payment Date, commencing on 31 March 2025, subject to Condition 5,

and where:

"10 year Swap Rate" means, in respect of any Reset Period, the mid-swap rate as displayed on Reuters screen "ISDAFIX2" (the **"Reset Screen Page"**) as at 11:00 a.m. (Central European time) on the relevant Reset Interest Determination Date.

In the event that the relevant 10 year Swap Rate does not appear on the Reset Screen Page on the relevant Reset Interest Determination Date, the 10 year Swap Rate will be the Reset Reference Bank Rate on such Reset Interest Determination Date. **"Reset Reference Bank Rate"** means the percentage rate determined by the Agent Bank on the basis of the 10 year Swap Rate Quotations provided by five leading swap dealers in the interbank market (the **"Reset Reference Banks"**) to the Agent Bank at approximately 11:00 a.m. (Central European time) on the relevant Reset Interest Determination Date. If at least three quotations are provided, the 10 year Swap Rate will be determined by the Agent Bank on the basis of the arithmetic mean of the quotations provided, eliminating the highest quotation (or, in the event of equality one of the highest) and the lowest quotation (or, in the event of equality, one of the lowest).

The **"10 year Swap Rate Quotations"** means, in relation to any Reset Period, the arithmetic mean of the bid and offered rates for the annual fixed leg (calculated on a 30/360 Day Count basis) of a fixed-for-floating euro interest rate swap which (i) has a term of ten years commencing on the relevant Reset Date, (ii) is in an amount that is representative of a single transaction in the relevant market at the relevant time with an acknowledged dealer of good credit in the swap market, and (iii) has a floating leg based on the 6-month EURIBOR rate (calculated on the basis of the actual number of days elapsed and a year of 360 days).

(d) **Publication of Prevailing Interest Rates**

The Issuer shall cause notice of the Prevailing Interest Rate, the amount payable per Calculation Amount determined in accordance with this Condition 4 in respect of each relevant Reset Period commencing on or after the First Reset Date and the relevant dates scheduled for payment to be given to the Fiscal Agent, the Paying Agents, any stock exchange on which the 10 Year Non-Call Securities are for the time being listed or admitted to trading and, in accordance with Condition 14, the Holders of the 10 Year

⁷ Step-up of 25 basis points 10 years after the Issue Date

⁸ Step-up of 75 basis points 30 years after the Issue Date

Non-Call Securities and the Coupons, in each case as soon as practicable after its determination but in any event not later than the fourth Business Day thereafter.

The relevant Prevailing Interest Rate and the dates scheduled for payment so notified may subsequently be amended (or appropriate alternative arrangements made by way of adjustment) without notice in the event of any extension or shortening of the relevant period in accordance with these Conditions.

(e) **Agent Bank and Reset Reference Banks**

With effect from the first Reset Interest Determination Date, the Issuer will maintain an Agent Bank and the number of Reset Reference Banks provided above where the Prevailing Interest Rate is to be calculated by reference to them. The name of the initial Agent Bank is The Bank of New York Mellon, London Branch and its initial specified office is One Canada Square, London E14 5AL, United Kingdom.

The Issuer may from time to time replace the Agent Bank or any Reset Reference Bank with another leading financial institution in London. If the Agent Bank is unable or unwilling to continue to act as the Agent Bank or fails duly to determine the Prevailing Interest Rate in respect of any Reset Period as provided in Condition 4(c), the Issuer shall forthwith appoint another leading financial institution in London to act as such in its place. The Agent Bank may not resign its duties or be removed without a successor having been appointed as aforesaid.

(f) **Determinations of Agent Bank Binding**

All notifications, opinions, determinations, certificates, calculations, quotations and decisions given, expressed, made or obtained for the purposes of this Condition 4 by the Agent Bank shall (in the absence of wilful default, fraud or manifest error) be binding on the Issuer, the Agent Bank the Fiscal Agent, the Paying Agents and all Holders and (in the absence as aforesaid) no liability to the Holders or the Issuer shall attach to the Agent Bank in connection with the exercise or non-exercise by it of any of its powers, duties and discretions.

5. **Optional Interest Deferral**

- (a) **Deferral of Interest Payments:** The Issuer may, subject as provided in Conditions 5(b) and 5(c) below, elect in its sole discretion to defer (in whole or in part) any Interest Payment that is otherwise scheduled to be paid on an Interest Payment Date by giving notice (a "**Deferral Notice**") of such election to the Holders in accordance with Condition 14, the Fiscal Agent and the Paying Agents not more than 14 and not less than 7 Business Days prior to the relevant Interest Payment Date. Any Interest Payment that the Issuer has elected to defer pursuant to this Condition 5(a) and that has not been satisfied is referred to as a "**Deferred Interest Payment**".

If any Interest Payment is deferred pursuant to this Condition 5(a) then such Deferred Interest Payment shall itself bear interest (such further interest together with the Deferred Interest Payment, being "**Arrears of Interest**"), at the relevant Prevailing Interest Rate applicable from time to time, from (and including) the date on which (but for such deferral) the Deferred Interest Payment would otherwise have been due to be made to (but excluding) the date on which such Deferred Interest Payment is paid in accordance with Condition 5(c), in each case such further interest being compounded on each Interest Payment Date.

Non-payment of interest deferred pursuant to this Condition 5(a) shall not constitute a default by the Issuer or the Guarantor under the 10 Year Non-Call Securities or the Guarantee or for any other purpose.

- (b) **Optional Settlement of Arrears of Interest:** Arrears of Interest may be satisfied at the option of the Issuer, in whole or in part, at any given time (the "**Optional Deferred Interest Settlement Date**") following delivery of a notice to such effect given by the Issuer to the Holders in accordance with Condition 14, the Fiscal Agent and the Paying

Agents not more than 14 and no less than 7 Business Days prior to the relevant Optional Deferred Interest Settlement Date informing them of its election so to satisfy such Arrears of Interest (or part thereof) and specifying the relevant Optional Deferred Interest Settlement Date.

- (c) **Mandatory Settlement of Arrears of Interest:** Notwithstanding the provisions of Condition 5(b), the Issuer shall pay any outstanding Arrears of Interest in whole, but not in part, on the first occurring Mandatory Settlement Date following the Interest Payment Date on which any outstanding Arrears of Interest was first deferred.

Notice of the occurrence of any Mandatory Settlement Date shall be given to the Holders in accordance with Condition 14, the Fiscal Agent and the Paying Agents not more than 14 and no less than 7 Business Days prior to the relevant Mandatory Settlement Date.

If a Mandatory Settlement Date does not occur prior to the calendar day which is the fifth anniversary of the Interest Payment Date on which the relevant Deferred Interest Payment was first deferred, it is the intention, though not an obligation, of the Issuer to pay all outstanding Arrears of Interest (in whole but not in part) on the next following Interest Payment Date.

"**Mandatory Settlement Date**" means the earliest of:

- (i) as soon as reasonably practicable (but not later than the fifth business day) following the date on which a Compulsory Arrears of Interest Settlement Event occurs;
- (ii) following any Deferred Interest Payment, on the next scheduled Interest Payment Date on which the Issuer does not elect to defer in whole the interest accrued in respect of the relevant Interest Period; and
- (iii) the date on which the 10 Year Non-Call Securities are redeemed or repaid in accordance with Condition 6 or become due and payable in accordance with Condition 9.

A "**Compulsory Arrears of Interest Settlement Event**" shall have occurred if:

- (i) a Dividend Declaration is made in respect of any Junior Obligations or any Parity Obligations (other than in respect of any such dividend, distribution or payment paid or made (i) in respect of the 2002 Preferred Securities; or (ii) exclusively in Ordinary Shares of the Guarantor); or
- (ii) the Guarantor or any of its subsidiaries has repurchased, redeemed or otherwise acquired any Junior Obligations or any Parity Obligations (other than any repurchase, redemption or acquisition of any 2002 Preferred Securities),

save, in the case of (a) any such Dividend Declaration or such redemption, repurchase or acquisition that is mandatory under the terms of any such Parity Obligations; (b) any Dividend Declaration in respect of any such dividend, distribution or payment by the Issuer to the Guarantor, (c) any Dividend Declaration or repurchase which is required to be validly resolved on, declared, paid or made in respect of, share option, or free share allocation plan in each case reserved for directors, officers and/or employees of the Guarantor or any of its Affiliates or any associated liquidity agreements or any associated hedging transactions; (d) any purchase of Ordinary Shares of the Guarantor by or on behalf of the Guarantor as part of an intra-day transaction that does not result in an increase in the aggregate number of Ordinary Shares of the Guarantor held by or on behalf of the Guarantor as treasury shares at 8:30 a.m. Madrid time on the Interest Payment Date on which any outstanding Arrears of Interest was first deferred; (e) any repurchase or acquisition of Parity Obligations that is made for a consideration less than the aggregate nominal or par value of such Parity Obligations that are purchased or acquired; (f) any repurchase or acquisition of Ordinary Shares of the Guarantor resulting from mandatory obligations or hedging of any convertible securities issued by the Issuer or the Guarantor; or (g) any repurchase or acquisition of Ordinary Shares of the

Guarantor resulting from the settlement of existing equity derivatives after the Interest Payment Date on which any outstanding Arrears of Interest was first deferred.

"**Dividend Declaration**" means the authorisation by resolution of the general meeting of shareholders or the board of directors or other competent corporate body (as the case may be) of the Issuer or the Guarantor (as applicable) of the payment, or the making of, a dividend or other distribution or payment (or, if no such authorisation is required, the payment, or the making of, a dividend or other distribution or payment).

6. **Redemption and Purchase**

- (a) **Final redemption:** Subject to any early redemption described below, the 10 Year Non-Call Securities are undated securities with no specified maturity date. The 10 Year Non-Call Securities may not be redeemed at the option of the Issuer other than in accordance with Condition 6(b), 6(c), 6(d), 6(e), or 6(f).
- (b) **Issuer's Call Option:** The Issuer may, by giving not less than 30 nor more than 60 days' notice to the Fiscal Agent, the Paying Agents and, in accordance with Condition 14, the Holders (which notice shall be irrevocable), redeem the 10 Year Non-Call Securities in whole, but not in part, on the First Reset Date and on any Interest Payment Date thereafter at their principal amount together with any accrued and unpaid interest up to (but excluding) the Redemption Date and any outstanding Arrears of Interest.
- (c) **Redemption for Taxation Reasons:** If, immediately prior to the giving of the notice referred to below, a Tax Event or a Withholding Tax Event has occurred and is continuing, then the Issuer may, subject to having given not less than 30 nor more than 60 days' notice to the Fiscal Agent, the Paying Agents and, in accordance with Condition 14, the Holders (which notice shall be irrevocable) and subject to Condition 6(g), redeem the 10 Year Non-Call Securities in whole, but not in part, in accordance with these Conditions at any time, in each case at (i) their Early Redemption Amount (in the case of a Tax Event if the Redemption Date falls prior to the First Reset Date) or (ii) their principal amount (in the case of (a) a Withholding Tax Event or (b) a Tax Event if the Redemption Date falls on or after the First Reset Date), together, in each case, with any accrued and unpaid interest up to (but excluding) the Redemption Date and any outstanding Arrears of Interest. Upon the expiry of such notice, the Issuer shall redeem the 10 Year Non-Call Securities.
- (d) **Redemption for Accounting Reasons:** If, immediately prior to the giving of the notice referred to below, an Accounting Event has occurred and is continuing, then the Issuer may, subject to having given not less than 30 nor more than 60 days' notice to the Fiscal Agent, the Paying Agent and, in accordance with Condition 14, the Holders (which notice shall be irrevocable) and subject to Condition 6(g), redeem the 10 Year Non-Call Securities in accordance with these Conditions in whole, but not in part, at any time, in each case (i) at their Early Redemption Amount if the Redemption Date falls before the First Reset Date, or (ii) at their principal amount if the Redemption Date falls on or after the First Reset Date, together with any accrued and unpaid interest up to (but excluding) the Redemption Date and any outstanding Arrears of Interest. Upon the expiry of such notice, the Issuer shall redeem the 10 Year Non-Call Securities.
- (e) **Redemption for Rating Reasons:** If, immediately prior to the giving of the notice referred to below, a Capital Event has occurred and is continuing, then the Issuer may, subject to having given not less than 30 nor more than 60 days' notice to the Fiscal Agent, the Paying Agent and, in accordance with Condition 14, the Holders (which notice shall be irrevocable) and subject to Condition 6(g), redeem the 10 Year Non-Call Securities in accordance with these Conditions in whole, but not in part, at any time, in each case (i) at their Early Redemption Amount if the Redemption Date falls before the First Reset Date, or (ii) at their principal amount if the Redemption Date falls on or after the First Reset Date, together with any accrued and unpaid interest up to (but excluding) the Redemption Date and any outstanding Arrears of Interest. Upon the expiry of such notice, the Issuer shall redeem the 10 Year Non-Call Securities.

- (f) **Redemption following a Substantial Purchase Event:** If, immediately prior to the giving of the notice referred to below, a Substantial Purchase Event has occurred, then the Issuer may, subject to having given not less than 30 nor more than 60 days' notice to the Fiscal Agent, the Paying Agents and, in accordance with Condition 14, the Holders (which notice shall be irrevocable) and subject to Condition 6(g), redeem the 10 Year Non-Call Securities in whole, but not in part, in accordance with these Conditions at any time, in each case at their principal amount, together with any accrued and unpaid interest up to (but excluding) the Redemption Date and any outstanding Arrears of Interest. Upon expiry of such notice, the Issuer shall redeem the 10 Year Non-Call Securities.
- (g) **Preconditions to Redemption:** Prior to serving any notice of redemption pursuant to this Condition 6 (other than Condition 6(b)), the Guarantor shall
- (i) deliver to the Fiscal Agent a certificate signed by two directors of the Guarantor stating that the relevant requirement or circumstance giving rise to the right to redeem is satisfied;
 - (ii) in the case of a Tax Event or Withholding Tax Event deliver to the Fiscal Agent an opinion of independent legal or other tax advisers to the effect set out in paragraph (i) above;
 - (iii) in the case of an Accounting Event, deliver to the Fiscal Agent the relevant opinion from the relevant accountancy firm; and
 - (iv) in the case of a Capital Event, deliver to the Fiscal Agent the relevant confirmation from the relevant Rating Agency.
- (h) **Purchase:** Each of the Issuer, the Guarantor and their respective subsidiaries may at any time purchase 10 Year Non-Call Securities in the open market or otherwise at any price (provided that, if they should be cancelled pursuant to this Condition 6(h), they are purchased together with all unmatured Coupons and all unexchanged Talons relating to them). The 10 Year Non-Call Securities so purchased may be held, re-issued or re-sold or, at the option of the relevant purchaser, surrendered to the Fiscal Agent for cancellation, but while held by or on behalf of the Issuer, the Guarantor or any such subsidiary, shall not entitle the holder to vote at any meetings of the Holders of 10 Year Non-Call Securities and shall not be deemed to be outstanding for the purposes of calculating quorums at meetings of the Holders of 10 Year Non-Call Securities or for the purposes of Condition 12.
- (i) **Cancellation:** All 10 Year Non-Call Securities so redeemed and any unmatured Coupons attached to or surrendered with them will be cancelled and may not be re-issued or re-sold.

The Guarantor intends (without thereby assuming any obligation) at any time that it or the Issuer will redeem or repurchase the 10 Year Non-Call Securities only to the extent that the aggregate principal amount of the 10 Year Non-Call Securities to be redeemed or repurchased does not exceed such part of the net proceeds received by the Guarantor or any subsidiary of the Guarantor during the 360-day period prior to the date of such redemption or repurchase from the sale or issuance by the Guarantor or such subsidiary to third party purchasers (other than group entities of the Guarantor) of securities which are assigned by S&P, at the time of sale or issuance, an aggregate "equity credit" (or such similar nomenclature used by S&P from time to time) that is equal to or greater than the "equity credit" assigned to the 10 Year Non-Call Securities to be redeemed or repurchased at the time of their issuance (but taking into account any changes in hybrid capital methodology or another relevant methodology or the interpretation thereof since the issuance of the 10 Year Non-Call Securities), unless:

- (i) *the rating assigned by S&P to the Guarantor is at least "BBB" (or such similar nomenclature then used by S&P) and the Guarantor is of the view that such*

rating would not fall below this level as a result of such redemption or repurchase, or

- (ii) in the case of a repurchase, such repurchase is of less than (a) 10 per cent. of the aggregate principal amount of the 10 Year Non-Call Securities originally issued in any period of 12 consecutive months or (b) 25 per cent. of the aggregate principal amount of the 10 Year Non-Call Securities originally issued in any period of 10 consecutive years, or*
- (iii) the 10 Year Non-Call Securities are redeemed pursuant to a Tax Event, a Capital Event, an Accounting Event or a Withholding Tax Event, or*
- (iv) such redemption or repurchase occurs on or after the Interest Payment Date falling on 31 March 2044.*

7. **Payments**

- (a) **Method of Payment:** Payments of principal and interest will be made against presentation and surrender (or, in the case of a partial payment, endorsement) of 10 Year Non-Call Securities or the appropriate Coupons (as the case may be) at the specified office of any Paying Agent by transfer to a euro account maintained by the payee with a bank in city in which banks have access to the TARGET System. Payments of interest due in respect of any 10 Year Non-Call Security other than on presentation and surrender of matured Coupons shall be made only against presentation and either surrender or endorsement (as appropriate) of the relevant 10 Year Non-Call Security.
- (b) **Payments subject to fiscal laws:** All payments are subject in all cases to any applicable fiscal or other laws and regulations in the place of payment, but without prejudice to the provisions of Condition 8. No commissions or expenses shall be charged to the Holders in respect of such payments.
- (c) **Unmatured Coupons:** Upon the due date for redemption of any 10 Year Non-Call Security, unmatured Coupons relating to such 10 Year Non-Call Security (whether or not attached) shall become void and no payment shall be made in respect of them. Where any 10 Year Non-Call Security is presented for redemption without all unmatured Coupons relating to it, redemption shall be made only against the provision of such indemnity as the Issuer and the Guarantor may require.
- (d) **Exchange of Talons:** On or after the Interest Payment Date for the final Coupon forming part of a Coupon sheet issued in respect of any 10 Year Non-Call Securities, the Talon forming part of such Coupon sheet may be surrendered at the specified office of the Fiscal Agent in exchange for a further Coupon sheet (and another Talon for a further Coupon sheet) (but excluding any Coupons that may have become void pursuant to Condition 10).
- (e) **Payments on business days:** A 10 Year Non-Call Security or Coupon may only be presented for payment on a day which is a business day in the place of presentation (and, in the case of payment by transfer to a euro account, a day that is a Business Day). No further interest or other payment will be made as a consequence of the day on which the relevant 10 Year Non-Call Security or Coupon may be presented for payment under this Condition 7 falling after the due date. In this Condition "**business day**" means a day on which commercial banks and foreign exchange markets settle payments and are open in the relevant city.
- (f) **Paying Agents:** The initial Paying Agents and their initial specified offices are listed below. The Issuer and the Guarantor reserve the right at any time to vary or terminate the appointment of any Paying Agent and appoint additional or other Paying Agents, provided that they will maintain (i) a Fiscal Agent, (ii) a Paying Agent (which may be the Fiscal Agent) having specified offices in London and (iii) a Paying Agent with a specified office in a European Union member state that will not be obliged to withhold or deduct tax pursuant to any law implementing European Council Directive 2003/48/EC

or any other Directive implementing the conclusions of the ECOFIN Council meeting of 26-27 November 2000. Notice of any change in the Paying Agents or their specified offices will promptly be given to the Holders in accordance with Condition 14.

8. Taxation

- (a) **Additional Amounts:** All payments of principal and interest in respect of the 10 Year Non-Call Securities and the Coupons by the Issuer or (as the case may be) the Guarantor under the Guarantee will be made without withholding or deduction for, or on account of, any present or future taxes, duties, assessments or governmental charges (collectively, "**Taxes**") of whatever nature imposed or levied by or on behalf of The Netherlands or the Kingdom of Spain or, in each case, any authority therein or thereof having power to tax (each a "**Taxing Authority**"), unless the withholding or deduction of such Taxes is required by law.

In that event, the Issuer or, as the case may be, the Guarantor will pay such additional amounts ("**Additional Amounts**") as may be necessary in order that the net amounts received by the Holders after such withholding or deduction of Taxes shall equal the respective amounts of principal and interest which would have been received in respect of the 10 Year Non-Call Securities or (as the case may be) Coupons, in the absence of such withholding or deduction of Taxes; except that no Additional Amounts shall be payable with respect to any payment in respect of any 10 Year Non-Call Security or Coupon or (as the case may be) under the Guarantee:

- (i) to, or to a third party on behalf of, a Holder or to the beneficial owner of any 10 Year Non-Call Security or Coupon who is liable for Taxes in respect of such 10 Year Non-Call Security or Coupon by reason of his having some connection with The Netherlands or the Kingdom of Spain other than the mere holding of the 10 Year Non-Call Security or Coupon;
- (ii) presented for payment more than 30 days after the Relevant Date except to the extent that the relevant Holder or the beneficial owner thereof would have been entitled to such Additional Amounts on presenting the same for payment on the thirtieth such day;
- (iii) in relation to any estate, inheritance, gift, sales, transfer or similar Taxes;
- (iv) while the 10 Year Non-Call Securities are represented by Global 10 Year Non-Call Securities and the Global 10 Year Non-Call Securities are deposited with a common depository for Euroclear and/or Clearstream, Luxembourg, to, or to a third party on behalf of, a Holder or to the beneficial owner of any 10 Year Non-Call Security or Coupon if the Issuer or the Guarantor does not receive in a timely manner a duly executed and completed certificate from the Fiscal Agent, pursuant to Law 13/1985 of May 25, as amended ("**Law 13/1985**"), and Royal Decree 1065/2007 of July 27, as amended by Royal Decree 1145/2011 of July 29, and any implementing legislation or regulation;
- (v) while the 10 Year Non-Call Securities are represented by Definitive 10 Year Non-Call Securities, where such withholding or deduction of Taxes is imposed, withheld or deducted by reason of the failure of the Holder or the beneficial owner of any 10 Year Non-Call Security or Coupon to comply with the Issuer's or the Guarantor's request addressed to the Holder or the beneficial owner to provide a valid certificate of tax residence duly issued by the tax authorities of the country of tax residence of the beneficial owner of any 10 Year Non-Call Security or Coupon, which the Holder or the beneficial owner is required to provide by the applicable tax laws and regulations of the relevant Taxing Authority as a precondition to exemption from, or reduction in the rate of deduction or withholding of, Taxes imposed by such relevant Taxing Authority
- (vi) presented for payment in the Kingdom of Spain;

- (vii) where such withholding or deduction is imposed on a payment to an individual and is required to be made pursuant to European Council Directive 2003/48/EC on the taxation of savings income or any other Directive implementing the conclusions of the ECOFIN Council meeting of 26 to 27 November 2000 on the taxation of savings income or any law implementing or complying with, or introduced in order to conform to, such Directive; or
- (viii) presented for payment by or on behalf of a Holder who would have been able to avoid such withholding or deduction by presenting the relevant 10 Year Non-Call Security to another Paying Agent in a Member State of the European Union.

In addition, Additional Amounts will not be payable with respect to (i) any Taxes that are imposed in respect of any combination of the items set forth above and to (ii) any Holder of any 10 Year Non-Call Security who is a fiduciary, a partnership, a limited liability company or other than the sole beneficial owner of that payment, to the extent that payment would be required by the laws of the relevant Taxing Authority to be included in the income, for tax purposes, of a beneficiary or settlor with respect to the fiduciary, a member of that partnership, an interest holder in that limited liability company or a beneficial owner who would not have been entitled to the Additional Amounts had it been the Holder.

- (b) **Tax Credit Payment:** If any Additional Amounts are paid by the Issuer or, as the case may be, the Guarantor under this Condition for the benefit of any Holder and such Holder, in its sole discretion, determines that it has obtained (and has derived full use and benefit from) a credit against, a relief or remissions for, or repayment of, any tax, then, if and to the extent that such Holder, in its sole opinion, determines that (i) such credit, relief, remission or repayment is in respect of or calculated with reference to the Additional Amounts paid pursuant to this Condition; and (ii) its tax affairs for its tax year in respect of which such credit, relief, remission or repayment was obtained have been finally settled, such Holder shall, to the extent that it can do so without prejudice to the retention of the amount of such credit, relief, remission or repayment, pay to the Issuer or, as the case may be, the Guarantor such amount as such Holder shall in its sole opinion, determine to be the amount which will leave such Holder (after such payment) in no worse after tax position than it would have been in had the additional payment in question not been required to be made by the Issuer or, as the case may be, the Guarantor.
- (c) **Tax Credit Clawback:** If any Holder makes any payment to the Issuer or, as the case may be, the Guarantor pursuant to this Condition and such Holder subsequently determines in its sole opinion, that the credit, relief, remission or repayment in respect of which such payment was made was not available or has been withdrawn or that it was unable to use such credit, relief, remission or repayment in full, the Issuer or, as the case may be, the Guarantor shall reimburse such Holder such amount as such Holder determines, in its sole opinion, is necessary to place it in the same after tax position as it would have been in if such credit, relief, remission or repayment had been obtained and fully used and retained by such Holder, such amount not exceeding in any case the amount paid by the Holder to the Issuer or, as the case may be, the Guarantor.
- (d) **Tax Affairs:** Nothing in Conditions 8(b) and (c) above shall interfere with the right of any Holder to arrange its tax or any other affairs in whatever manner it thinks fit, oblige any Holder to claim any credit, relief, remission or repayment in respect of any payment made under this Condition in priority to any credit, relief, remission or repayment available to it nor oblige any Holder to disclose any information relating to its tax or other affairs or any computations in respect thereof.
- (e) **Definitions:** References in these Conditions to (i) "Principal" shall be deemed to include all amounts in the nature of principal payable pursuant to Condition 7 or any amendment or supplement to it; (ii) "interest" shall be deemed to include all Arrears of Interest and all other amounts payable pursuant to Condition 4 or any amendment or supplement to it; and (iii) "principal" and/or "interest" shall be deemed to include any Additional Amounts.

- (f) **Applicable law for Spanish tax purposes:** The Guarantor will apply Additional Provision Two of Law 13/1985 to the 10 Year Non-Call Securities for Spanish tax purposes.

Payments in respect of the 10 Year Non-Call Securities and the Coupons by the Guarantor under the Guarantee will be exempt from Spanish Non-Resident Income Tax to the extent that the Holder or beneficial owner is not acting through a permanent establishment in Spain.

The Guarantor will comply with the reporting obligations set out in Section 3 of Additional Provision Two of Law 13/1985 in respect of Holders or beneficial owners who are taxpayers of the Spanish Individual Income Tax or taxpayers of the Spanish Corporation Tax, as well as taxpayers of the Spanish Non-resident Income Tax who hold the 10 Year Non-Call Securities through a permanent establishment located in Spanish territory.

9. **Enforcement Events and No Events of Default**

There are no events of default in respect of the 10 Year Non-Call Securities.

However, if an Issuer Winding-up occurs, or an order is made or an effective resolution passed for the winding-up, dissolution or liquidation of the Guarantor, or the Guarantor becomes insolvent ("*en estado de insolvencia*") pursuant to article 2 of the Spanish insolvency law, any Holder of a 10 Year Non-Call Security, in respect of such 10 Year Non-Call Security and provided that such Holder does not contravene a previously adopted Extraordinary Resolution (if any) may, by written notice to the Issuer and the Guarantor, declare that such 10 Year Non-Call Security and all interest then accrued but unpaid on such 10 Year Non-Call Security shall be forthwith due and payable, whereupon the same shall become immediately due and payable, together with all interest accrued thereon.

In such case the Holder of a 10 Year Non-Call Security may, at its sole discretion, institute steps in order to obtain a judgment against the Issuer and/or the Guarantor for any amounts due in respect of the 10 Year Non-Call Securities, including the institution of proceedings for the declaration of insolvency ("*declaración de concurso*") under Spanish insolvency law of the Guarantor and/or proving and/or claiming in an Issuer Winding-up or in the winding-up, dissolution, liquidation or insolvency proceeding of the Guarantor for such amount.

Each Holder may, at its discretion and without further notice, institute such proceedings as it may think fit to enforce any term or condition binding on the Issuer or the Guarantor under the 10 Year Non-Call Securities or the Guarantee but in no event shall the Issuer or the Guarantor by the virtue of such proceedings be obliged to pay any sum or sums sooner than the same would otherwise have been payable by it.

No remedy against the Issuer or the Guarantor, other than as referred to in this Condition 9 shall be available to the Holders, whether for the recovery of amounts owing in respect of the 10 Year Non-Call Securities or the Guarantee or in respect of any other breach by the Issuer or the Guarantor of any of their respective other obligations under or in respect of the 10 Year Non-Call Securities or the Guarantee.

10. **Prescription**

Claims in respect of principal and interest or any other amount will become void unless presentation for payment is made as required by Condition 7 within a period of 10 years in the case of principal (or any other amount in the nature of principal) and five years in the case of interest (or any other amount in the nature of interest, including Arrears of Interest) from the appropriate Relevant Date.

11. **Replacement of 10 Year Non-Call Securities and Coupons**

If any 10 Year Non-Call Security or Coupon is lost, stolen, mutilated, defaced or destroyed it may be replaced at the specified office of the Fiscal Agent subject to all applicable laws and stock exchange or other relevant authority requirements, upon payment by the claimant of the

expenses incurred in connection with such replacement and on such terms as to evidence, security, indemnity and otherwise as the Issuer, the Guarantor and the Fiscal Agent may require (provided that the requirement is reasonable in the light of prevailing market practice). Mutilated or defaced 10 Year Non-Call Securities or Coupons must be surrendered before replacements will be issued. In case any such lost, stolen, mutilated, defaced or destroyed Coupon has become or is about to become due and payable, the Issuer in its discretion may, instead of delivering replacements therefor, pay such Coupon when due.

12. **Meetings of Holders of 10 Year Non-Call Securities and Modification**

- (a) **Meetings of Holders of 10 Year Non-Call Securities:** The Fiscal Agency Agreement contains provisions for convening meetings of Holders of 10 Year Non-Call Securities to consider matters affecting their interests, including the sanctioning by Extraordinary Resolution (as defined in the Fiscal Agency Agreement) of a modification of any of these Conditions. Such a meeting may be convened by Holders of 10 Year Non-Call Securities holding not less than one twentieth in principal amount of the 10 Year Non-Call Securities for the time being outstanding. The quorum for any meeting convened to consider an Extraordinary Resolution will be one or more persons holding or representing at least two thirds of the aggregate principal amount of the 10 Year Non-Call Securities for the time being outstanding, or at any adjourned meeting one or more persons being or representing Holders of 10 Year Non-Call Securities whatever the principal amount of the 10 Year Non-Call Securities held or represented. Any Extraordinary Resolution duly passed shall be binding on Holders of 10 Year Non-Call Securities (whether or not they were present at the meeting at which such resolution was passed) and on all Holders of Coupons.

The Fiscal Agency Agreement provides that a resolution in writing signed by or on behalf of the holders of not less than 90 per cent. in principal amount of the 10 Year Non-Call Securities outstanding shall for all purposes be as valid and effective as an Extraordinary Resolution passed at a meeting of Holders of 10 Year Non-Call Securities duly convened and held. Such a resolution in writing may be contained in one document or several documents in the same form, each signed by or on behalf of one or more Holders of 10 Year Non-Call Securities.

- (b) **Modification:** The 10 Year Non-Call Securities, these Conditions, the Deed of Covenant and the Deed of Guarantee may be amended without the consent of the Holders of 10 Year Non-Call Securities to correct a manifest error. No other modification may be made to the 10 Year Non-Call Securities, these Conditions the Deed of Covenant or the Deed of Guarantee except with the sanction of a resolution of the Holders of the 10 Year Non-Call Securities.

In addition, the parties to the Fiscal Agency Agreement may agree to modify any provision thereof, but the Issuer shall not agree, without the consent of the Holders of 10 Year Non-Call Securities, to any such modification unless, in the opinion of the Issuer and the Guarantor, (i) it is of a formal, minor or technical nature; (ii) it is made to correct a manifest error; or (iii) it is not materially prejudicial to the interests of the Holders of 10 Year Non-Call Securities.

13. **Further Issues**

The Issuer may from time to time without the consent of the Holders create and issue further securities either having the same terms and conditions as the 10 Year Non-Call Securities in all respects (or in all respects except for the first payment of interest on them) and so that such further issue shall be consolidated and form a single series with the outstanding securities of any series (including the 10 Year Non-Call Securities) or upon such terms as the Issuer may determine at the time of their issue. References in these Conditions to the 10 Year Non-Call Securities include (unless the context requires otherwise) any other securities issued pursuant to this Condition and forming a single series with the 10 Year Non-Call Securities.

14. **Notices**

Notices to Holders of 10 Year Non-Call Securities will be deemed to be validly given if published in a leading daily newspaper having general circulation in London (which is expected to be the Financial Times) or, if such publication is not practicable, if published in a leading English language daily newspaper having general circulation in Europe. The Issuer shall also ensure that all notices are duly published in a manner which complies with the rules and regulations of any stock exchange or other relevant authority on which the 10 Year Non-Call Securities are for the time being listed and/or admitted to trading. Any such notice shall be deemed to have been validly given on the date of the first such publication or, if published more than once on the first date on which publication is made.

Notwithstanding the above, while all the 10 Year Non-Call Securities are represented by Global 10 Year Non-Call Securities and the Global 10 Year Non-Call Securities are deposited with a common depository for Euroclear and/or Clearstream, Luxembourg, notices to Holders of 10 Year Non-Call Securities may be given by delivery of the relevant notice to Euroclear or Clearstream, Luxembourg in accordance with their respective rules and operating procedures, and such notices shall be deemed to have been given to Holders on the date of delivery to Euroclear and/or Clearstream, Luxembourg. Holders of Coupons will be deemed for all purposes to have notice of the contents of any notice given to the Holders of 10 Year Non-Call Securities in accordance with this Condition.

15. **Contracts (Rights of Third Parties) Act 1999**

No person shall have any right to enforce any term or condition of the 10 Year Non-Call Securities under the Contracts (Rights of Third Parties) Act 1999.

16. **Governing Law**

- (a) **Governing Law:** The Fiscal Agency Agreement, the 10 Year Non-Call Securities, the Coupons and the Guarantee and any non-contractual obligations arising out of or in connection with them are governed by and shall be construed in accordance with English law, other than the provisions of Condition 2(b) which are governed by and construed in accordance with the laws of The Netherlands, and the provisions of Conditions 3(b) and 3(c), and the corresponding provisions of the Guarantee, which are governed by and construed in accordance with the laws of the Kingdom of Spain.
- (b) **Jurisdiction:** The courts of England have exclusive jurisdiction to settle any dispute (a "**Dispute**") arising from or connected with the 10 Year Non-Call Securities or the Coupons (including a dispute relating to the existence, validity or termination of the 10 Year Non-Call Securities or any non-contractual obligations arising out of or in connection with the 10 Year Non-Call Securities or the consequences of their nullity). The Issuer agrees that the courts of England are the most appropriate and convenient courts to settle any Dispute and, accordingly, that it will not argue to the contrary. This Condition is for the benefit of the Holders only. As a result, nothing in this Condition 16 prevents any Holder from taking proceedings relating to a Dispute ("**Proceedings**") in any other courts with jurisdiction. To the extent allowed by law, Holders may take concurrent Proceedings in any number of jurisdictions.
- (c) **Agent for Service of Process:** The Issuer agrees that the documents which start any Proceedings and any other documents required to be served in relation to those Proceedings may be served on it by being delivered to Telefónica UK Limited, 260 Bath Road, Slough, SL1 4DX, United Kingdom, or, if different, its registered office for the time being or at any address of the Issuer in England at which process may be served on it. If such person is not or ceases to be effectively appointed to accept service of process on behalf of the Issuer, the Issuer shall forthwith appoint a further person in England to accept service of process on its behalf in England and notify the name and address of such person to the Fiscal Agent and, failing such appointment within 15 days, any Holder shall be entitled to appoint such a person by written notice addressed to the Issuer and delivered to the Issuer or to the specified office of the Fiscal Agent. Nothing in this

paragraph shall affect the right of any Holder to serve process in any other manner permitted by law. This Condition applies to Proceedings in England.

17. **Definitions**

In these Conditions:

"**2002 Preferred Securities**" means the €2,000,000,000 preferred securities (*participaciones preferentes*) issued by Telefónica Finance USA LLC on 30 December 2002 (of which, as of the date hereof, €58,765,000 were outstanding);

"**2013 Non-Call Securities**" means the September 2013 5 Year Non-Call Securities, the September 2013 8 Year Non-Call Securities and the November 2013 Non-Call Securities;

"**30/360 Day Count**" means, in respect of any period, the number of days in the relevant period, from (and including) the first day in such period to (but excluding) the last day in such period (such number of days being calculated on the basis of a 360 day year consisting of 12 months of 30 days each), divided by 360;

"**6 Year Non-Call Securities**" means the €750,000,000 Undated 6 Year Non-Call Deeply Subordinated Guaranteed Fixed Rate Reset Securities issued by the Issuer concurrently with the 10 Year Non-Call Securities and unconditionally and irrevocably guaranteed on a subordinated basis by the Guarantor;

"**10 year Swap Rate**" has the meaning given to it in Condition 4(c);

"**10 year Swap Rate Quotations**" has the meaning given to it in Condition 4(c);

an "**Accounting Event**" shall be deemed to occur if the Issuer or the Guarantor has received, and notified the Holders in accordance with Condition 14 that it has so received, an opinion of a recognised accountancy firm of international standing, stating that, as a result of a change in the accounting rules or methodology effective after the Issue Date, the 10 Year Non-Call Securities must not or must no longer be recorded as "equity" pursuant to IFRS-EU or any other accounting standards that may replace IFRS-EU for the purposes of the consolidated financial statements of the Guarantor;

"**Additional Amounts**" has the meaning given to it in Condition 8(a);

"**Affiliates**" means an entity that directly, or indirectly through one or more intermediaries, controls, or is controlled by, or is under common control with, the Guarantor;

"**Arrears of Interest**" has the meaning given to it in Condition 5(a);

"**business day**" has the meaning given to it in Condition 7(e);

"**Business Day**" means a day, other than a Saturday, Sunday or public holiday, on which the Target System is operating;

"**Calculation Amount**" has the meaning given to it in Condition 4(b);

a "**Capital Event**" shall be deemed to occur if the Issuer or the Guarantor has received, and notified the Holders in accordance with Condition 14 that it has so received, confirmation from any Rating Agency that, due to (i) any amendment to, clarification of, or change in hybrid capital methodology or a change in the interpretation thereof, in each case occurring or becoming effective after the Issue Date; or (ii) the application of a different hybrid capital methodology or set of criteria by the relevant Rating Agency after the Issue Date (due to changes in the rating previously assigned to the Issuer and/or the Guarantor or to any other reasons), the 10 Year Non-Call Securities will no longer be eligible for the same or a higher amount of "equity credit" (or such other nomenclature that the relevant Rating Agency may then use to describe the degree to which an instrument exhibits the characteristics of an ordinary share) attributed to the 10 Year Non-Call Securities at the Issue Date;

"**Compulsory Arrears of Interest Settlement Event**" has the meaning given to it in Condition 5(c);

"**Condition**" means the terms and conditions of the 10 Year Non-Call Securities;

"**Deferral Notice**" has the meaning given to it in Condition 5(a);

"**Deferred Interest Payment**" has the meaning given to it in Condition 5(a);

"**Early Redemption Amount**" means in respect of a redemption of the 10 Year Non-Call Securities following the occurrence of a Tax Event, an Accounting Event or a Capital Event, 101 per cent. of the principal amount of such 10 Year Non-Call Securities;

"**First Reset Date**" means 31 March 2024;

"**Fitch Ratings**" means Fitch Ratings Limited;

"**Further 10 Year Non-Call Securities**" means any 10 Year Non-Call Securities issued pursuant to Condition 13 and forming a single series with the outstanding 10 Year Non-Call Securities;

"**Guarantor**" means Telefónica, S.A.;

"**Holder**" has the meaning given to it in Condition 1(b);

"**IFRS-EU**" means International Financial Reporting Standards, as adopted by the European Union;

"**Interest Payment**" means, in respect of an interest payment on an Interest Payment Date, the amount of interest payable on the presentation and surrender of the relevant Coupon for the relevant Interest Period in accordance with Condition 4;

"**Interest Payment Date**" means 31 March in each year;

"**Interest Period**" means the period beginning on (and including) the Issue Date and ending on (but excluding) the first Interest Payment Date and each successive period beginning on (and including) an Interest Payment Date and ending on (but excluding) the next succeeding Interest Payment Date;

"**Issue Date**" means 31 March 2014;

"**Issuer**" means Telefónica Europe B.V.;

"**Issuer Winding-up**" means a situation where (i) an order is made or a decree or resolution is passed for the winding-up, liquidation or dissolution of the Issuer, except for the purposes of a solvent merger, reconstruction or amalgamation, or (ii) a trustee (*curator*) is appointed by the competent District Court in The Netherlands in the event of bankruptcy (*faillissement*) affecting the whole or a substantial part of the undertaking or assets of the Issuer and such appointment is not discharged within 30 days;

"**Junior Obligations**" means the Junior Obligations of the Guarantor and the Junior Obligations of the Issuer;

"**Junior Obligations of the Guarantor**" means all obligations of the Guarantor issued or incurred directly or indirectly by it, which rank or are expressed to rank junior to the Guarantee, including Ordinary Shares of the Guarantor;

"**Junior Obligations of the Issuer**" means all obligations of the Issuer, issued or incurred directly or indirectly by it, which rank or are expressed to rank junior to the 10 Year Non-Call Securities, including (i) Ordinary Shares of the Issuer, (ii) Preferred Shares of the Issuer, if any, and, (iii) if there are any Preferred Shares of the Issuer outstanding and any 2013 Non-Call Securities outstanding which by their terms are expressed to rank *pari passu* with Preferred Shares of the Issuer, such 2013 Non-Call Securities;

"**Law 13/1985**" means the Additional Provision Two of Law 13/1985 of the Kingdom of Spain (as amended or replaced from time to time);

"**Mandatory Settlement Date**" has the meaning given to it in Condition 5(c);

"**Moody's**" means Moody's Investors Service Limited;

"**November 2013 Non-Call Securities**" means the £600,000,000 Undated 7 Year Non-Call Deeply Subordinated Guaranteed Fixed Rate Reset Securities (ISIN: XS099326441) issued by the Issuer on 26 November 2013 and unconditionally and irrevocably guaranteed on a subordinated basis by the Guarantor;

"**Ordinary Shares of the Guarantor**" means ordinary shares in the capital of the Guarantor, having at the Issue Date a nominal value of €1.00 each;

"**Ordinary Shares of the Issuer**" means ordinary shares in the capital of the Issuer, having on the Issue Date a nominal amount of €460.00 each;

"**Parity Obligations**" means the Parity Obligations of the Guarantor and the Parity Obligations of the Issuer;

"**Parity Obligations of the Guarantor**" means any and all present or future series of preferred securities (*participaciones preferentes*) issued directly by the Guarantor or indirectly through a wholly-owned subsidiary with the guarantee of the Guarantor in accordance with Law 13/1985, obligations equivalent to preferred securities (*participaciones preferentes*) issued directly by the Guarantor or indirectly through a wholly-owned subsidiary with the guarantee of the Guarantor (whether issued under Law 13/1985 or any other law or regulation of Spain or of any other jurisdiction) (which include the guarantee granted by the Guarantor in connection with the 2002 Preferred Securities) and obligations of the Guarantor, issued directly by it or indirectly through a wholly-owned subsidiary with the guarantee of the Guarantor, which rank or are expressed to rank *pari passu* with the Guarantee (which include the guarantees granted by the Guarantor in connection with the 6 Year Non-Call Securities and the 2013 Non-Call Securities);

"**Parity Obligations of the Issuer**" means any obligations of the Issuer, issued or incurred directly or indirectly by it, which rank, or are expressed to rank, *pari passu* with the 10 Year Non-Call Securities including (i) the 6 Year Non-Call Securities and, (ii) the 2013 Non-Call Securities, except in the event that such 2013 Non-Call Securities are Junior Obligations of the Issuer (as defined above);

"**Preferred Shares of the Issuer**" means any preference shares in the capital of the Issuer (and, if divided into classes, each class thereof);

"**Prevailing Interest Rate**" means the rate of interest payable on the 10 Year Non-Call Securities applicable from time to time pursuant to Condition 4;

"**Proceedings**" has the meaning given to it in Condition 16(b);

"**Rating Agency**" means S&P, Moody's or Fitch Ratings;

"**Redemption Date**" means the date fixed for redemption of the 10 Year Non-Call Securities pursuant to Condition 6;

"**Relevant Date**" means (i) in respect of any payment other than a sum to be paid by the Issuer or the Guarantor in a winding-up or administration of the Issuer or Guarantor, as the case may be, the date on which such payment first becomes due and payable, but if the full amount of moneys payable on such date has not been received by the Fiscal Agent on or prior to such date, the Relevant Date means the date on which such moneys shall have been so received and notice to that effect shall have been given to the Holders of 10 Year Non-Call Securities in accordance with Condition 14 and (ii) in respect of a sum to be paid by the Issuer or the Guarantor in a winding-up or administration of the Issuer or the Guarantor, as the case may be, the date that is one day prior to the date on which an order is made or a resolution is passed for the winding-up, or in the case of an administration, one day prior to the date on which any dividend is distributed;

"Reset Date" means the First Reset Date and each date falling on the tenth anniversary thereafter;

"Reset Interest Determination Date" means, in respect of any Reset Period, the day falling two Business Days prior to the beginning of the relevant Reset Period;

"Reset Period" means each period from and including the First Reset Date to but excluding the next following Reset Date and thereafter from and including each Reset Date to but excluding the next following Reset Date;

"Reset Reference Banks" has the meaning given to it in Condition 4(c);

"Reset Reference Bank Rate" has the meaning given to it in Condition 4(c);

"Reset Screen Page" has the meaning given to it in Condition 4(c);

"S&P" means Standard & Poor's Credit Market Services Europe Limited;

"Senior Obligations of the Guarantor" means all obligations of the Guarantor, including subordinated obligations of the Guarantor according to Spanish insolvency law, other than Parity Obligations of the Guarantor and Junior Obligations of the Guarantor;

"Senior Obligations of the Issuer" means all obligations of the Issuer, including subordinated obligations of the Issuer according to Dutch insolvency law, other than Parity Obligations of the Issuer and Junior Obligations of the Issuer;

"September 2013 5 Year Non-Call Securities" means the €1,125,000,000 Undated 5 Year Non-Call Deeply Subordinated Guaranteed Fixed Rate Reset Securities (ISIN: XS0972570351) issued by the Issuer on 18 September 2013 and unconditionally and irrevocably guaranteed on a subordinated basis by the Guarantor;

"September 2013 8 Year Non-Call Securities" means the €625,000,000 Undated 8 Year Non-Call Deeply Subordinated Guaranteed Fixed Rate Reset Securities (ISIN: XS0972588643) issued by the Issuer on 18 September 2013 and unconditionally and irrevocably guaranteed on a subordinated basis by the Guarantor;

"Subordinated Loan" means the subordinated loan made by the Issuer to the Guarantor dated 31 March 2014, pursuant to which the proceeds of the issue of the 10 Year Non-Call Securities are on-lent to the Guarantor;

a **"Substantial Purchase Event"** shall be deemed to have occurred if at least 80 per cent. of the aggregate principal amount of the 10 Year Non-Call Securities originally issued (which for these purposes shall include any Further 10 Year Non-Call Securities) is purchased by the Issuer, the Guarantor or any subsidiary of the Guarantor (and in each case is cancelled in accordance with Condition 6(i));

a **"Tax Event"** shall be deemed to have occurred if, as a result of a Tax Law Change, in respect of (i) the Issuer's obligation to make any payment under the 10 Year Non-Call Securities (including any Interest Payment) on the next following Interest Payment Date; or (ii) the obligation of the Guarantor to make any payment in favour of the Issuer under the Subordinated Loan on the next following due date for such payment, the Issuer or the Guarantor (as the case may be) would no longer be entitled to claim a deduction in respect of computing its tax liabilities in The Netherlands or in Spain (as the case may be), or such entitlement is materially reduced.

For the avoidance of doubt, a Tax Event shall not occur if payments of interest under the Subordinated Loan by the Guarantor are not deductible in whole or in part for Spanish corporate income tax purposes solely as a result of general tax deductibility limits set forth by Article 20 of the consolidated text of the Spanish Corporate Income Tax Law, approved by the Royal Legislative Decree 4/2004, dated 5 March, as at 24 March 2014;

"Tax Law Change" means a change in or proposed change in, or amendment to, or proposed amendment to, the laws or regulations of The Netherlands or Spain or, in either case, any political subdivision or any authority thereof or therein having power to tax, including, without limitation, any treaty to which The Netherlands or Spain is a party, or any change in the official or generally published interpretation of such laws or regulations, including a decision of any court or tribunal, or any interpretation or pronouncement by any relevant tax authority that provides for a position with respect to such laws or regulations or interpretations thereof that differs from the previously generally accepted position in relation to similar transactions, which change, amendment or interpretation becomes or would become, effective after 24 March 2014;

"Taxing Authority" has the meaning given to it in Condition 8(a); and

a **"Withholding Tax Event"** shall be deemed to occur if as a result of a Tax Law Change, in making any payments in respect of the 10 Year Non-Call Securities or the Guarantee the Issuer or the Guarantor has paid or will or would on the next Interest Payment Date be required to pay Additional Amounts in respect of the 10 Year Non-Call Securities or the Guarantee that cannot be avoided by the Issuer or the Guarantor, as the case may be, taking measures reasonably available to it.

SUMMARY OF PROVISIONS RELATING TO THE SECURITIES IN GLOBAL FORM

The Securities will initially be in the form of Temporary Global Securities which will be deposited on or around the Closing Date with a common depository for Euroclear and Clearstream, Luxembourg.

The Securities are not intended to be held in a manner which would allow Eurosystem eligibility.

Each Temporary Global Security will be exchangeable in whole or in part for interests in a Permanent Global Security not earlier than 40 days after the Closing Date upon certification as to non-U.S. beneficial ownership. No payments will be made under each Temporary Global Security unless exchange for interests in the corresponding Permanent Global Security is improperly withheld or refused. In addition, interest payments in respect of the Securities cannot be collected without such certification of non-U.S. beneficial ownership.

Each Permanent Global Security will become exchangeable in whole, but not in part, for Securities in definitive form ("**Definitive Securities**") in the denomination of EUR 100,000 each at the request of the bearer of the relevant Permanent Global Security if (a) Euroclear or Clearstream, Luxembourg is closed for business for a continuous period of 14 days (other than by reason of legal holidays) or announces an intention permanently to cease business or (b) if principal in respect of any of the relevant Securities is not paid when due and payable.

Whenever a Permanent Global Security is to be exchanged for Definitive Securities, the Issuer shall procure the prompt delivery (free of charge to the bearer) of such Definitive Securities, duly authenticated and with Coupons and Talons attached, in an aggregate principal amount equal to the principal amount of the corresponding Permanent Global Security to the bearer of such Permanent Global Security against the surrender of the relevant Permanent Global Security to or to the order of the Fiscal Agent within 30 days of the bearer requesting such exchange.

If:

- (a) the relevant Temporary Global Security is not duly exchanged, whether in whole or in part, for the corresponding Permanent Global Security by 5.00 p.m. (London time) on the thirtieth day after the time at which the preconditions to such exchange are first satisfied; or
- (b) Definitive Securities have not been delivered by 5.00 p.m. (London time) on the thirtieth day after the bearer has duly requested exchange of a Permanent Global Security for Definitive Securities; or
- (c) the relevant Temporary or Permanent Global Security (or any part of it) has become due and payable in accordance with the Conditions of the relevant Securities or the date for final redemption of the Securities has occurred and, in either case, payment in full of the amount of principal falling due with all accrued interest thereon has not been made to the bearer in accordance with the terms of the relevant Temporary or Permanent Global Security on the due date for payment,

then the relevant Global Security (including the obligation to deliver Definitive Securities) will become void at 5.00 p.m. (London time) on such thirtieth day (in the case of (a) and (b) above) or at 5.00 p.m. (London time) on such due date (in the case of (c) above), and the bearer of such Global Security will have no further rights thereunder (but without prejudice to the rights which the bearer of the Global Security or others may have under a deed of covenant dated 31 March 2014 (the "**Deed of Covenant**") executed by the Issuer). Under the Deed of Covenant, persons shown in the records of Euroclear and/or Clearstream, Luxembourg as being entitled to an interest in the relevant Global Security will acquire directly against the Issuer all those rights to which they would have been entitled if, immediately before such Global Security becomes void, they had been the holders of Definitive Securities in an aggregate principal amount equal to the principal amount of Securities they were shown as holding in the records of Euroclear and/or (as the case may be) Clearstream, Luxembourg.

In addition, each Temporary Global Security and Permanent Global Security will contain provisions which modify the Terms and Conditions of the corresponding Securities as they apply to such Temporary Global Security and Permanent Global Security. The following is a summary of certain of those provisions:

Payments: All payments in respect of each Temporary Global Security and Permanent Global Security will be made against presentation and (in the case of payment of principal in full with all interest accrued thereon) surrender of the relevant Temporary Global Security or (as the case may be) Permanent Global Security to or to the order of any Paying Agent and will be effective to satisfy and discharge the corresponding liabilities of the Issuer in respect of the relevant Securities. On each occasion on which a payment of principal or interest is made in respect of a Temporary Global Security or (as the case may be) a Permanent Global Security, the Issuer shall procure that the payment is entered *pro rata* in the records of Euroclear and Clearstream, Luxembourg.

Payments on business days: In the case of all payments made in respect of a Temporary Global Security or a Permanent Global Security "**business day**" means any day on which the TARGET System is open.

Notices: While all the Securities of a given series are represented by a Permanent Global Security (or by a Permanent Global Security and/or a Temporary Global Security) and such Permanent Global Security is (or such Permanent Global Security and/or Temporary Global Security are) deposited with a common depository for Euroclear and Clearstream, Luxembourg, notices to Holders of such series of Securities may be given by delivery of the relevant notice to Euroclear and Clearstream, Luxembourg and, in any case, such notices shall be deemed to have been given to the Holders in accordance with Condition 14 (*Notices*) of the Terms and Conditions of the 6 Year Non-Call Securities and of the Terms and Conditions of the 10 Year Non-Call Securities, on the date of delivery to Euroclear and Clearstream, Luxembourg.

FORM OF GUARANTEE

The text of the Deed of Guarantee is as follows:

This Deed of Guarantee is made on 31 March 2014

BY

- (1) TELEFÓNICA, S.A. (the "**Guarantor**")

IN FAVOUR OF

- (2) THE HOLDERS of any Security or Securities (as defined below) or the coupons relating to them; and
- (3) THE RELEVANT ACCOUNT HOLDERS (as defined in the Deed of Covenant described below).

WHEREAS

- (A) Telefónica Europe B.V. (the "**Issuer**") proposes to issue €750,000,000 Undated 6 Year Non-Call Deeply Subordinated Guaranteed Fixed Rate Reset Securities and €1,000,000,000 Undated 10 Year Non-Call Deeply Subordinated Guaranteed Fixed Rate Reset Securities (together, the "**Securities**", which expression shall, if the context so admits, include the Global Securities (whether in temporary or permanent form)) in connection with which, the Issuer and Guarantor have become parties to a fiscal agency agreement (the "**Fiscal Agency Agreement**") dated 31 March 2014 between, inter alios, the Issuer, the Guarantor and The Bank of New York Mellon, London Branch in its various capacities as set out therein relating to the Securities, and the Issuer has executed and delivered a deed of covenant (the "**Deed of Covenant**") dated 31 March 2014.
- (B) The Guarantor has duly authorised the giving of a guarantee on a subordinated basis in respect of the Securities and the Deed of Covenant.

THIS DEED WITNESSES as follows:

1. Interpretation
- 1.1 All terms and expressions which have defined meanings in the Conditions (as defined in the Deed of Covenant), the Fiscal Agency Agreement or the Deed of Covenant shall have the same meanings in this Deed of Guarantee except where the context requires otherwise or unless otherwise stated.
- 1.2 Any reference in this Deed of Guarantee to a Clause is, unless otherwise stated, to a clause hereof.
- 1.3 All references in this Deed of Guarantee to an agreement, instrument or other document (including the Conditions, the Fiscal Agency Agreement and the Deed of Covenant) shall be construed as a reference to that agreement, instrument or other document as the same may be amended, supplemented, replaced or novated from time to time.
- 1.4 Any reference in this Deed of Guarantee to any legislation (whether primary legislation or regulations or other subsidiary legislation made pursuant to primary legislation) shall be construed as a reference to such legislation as the same may have been, or may from time to time be, amended or re-enacted.
- 1.5 Clause headings are for ease of reference only.
2. Guarantee and Indemnity
- 2.1 The Guarantor hereby unconditionally and irrevocably guarantees on a subordinated basis:
- 2.1.1 to each Holder the due and punctual payment of all sums expressed to be payable from time to time by the Issuer in respect of any Security as and when the same become due and payable and accordingly undertakes to pay to such Holder, forthwith in the manner

and currency prescribed by the Conditions for payments by the Issuer thereunder, any and every sum or sums which the Issuer is at any time liable to pay in respect of such Security in accordance with the Conditions of the Securities and which the Issuer has failed to pay; and

2.1.2 to each Relevant Account Holder the due and punctual payment of all sums which become payable from time to time by the Issuer to such Relevant Account Holder in respect of the Direct Rights as and when the same become due and payable and accordingly undertakes to pay to such Relevant Account Holder, forthwith in the manner and currency prescribed by the Conditions of the Securities for payments by the Issuer thereunder, any and every sum or sums which the Issuer is at any time liable to pay to such Relevant Account Holder in respect of the Direct Rights in accordance with the Deed of Covenant and which the Issuer has failed to pay.

2.2 The Guarantor undertakes to each Holder and each Relevant Account Holder that, should any amount referred to in Clause 2.1 not be recoverable from the Guarantor thereunder for any reason whatsoever (including, without limitation, by reason of any Security, any provision of any Security, the Deed of Covenant or any provision thereof being or becoming void, unenforceable or otherwise invalid under any applicable law) then, notwithstanding that the same may have been known to such Holder or Relevant Account Holder, the Guarantor will, forthwith upon demand by such Holder or Relevant Account Holder, pay such sum by way of a full indemnity in the manner and currency prescribed by the Securities or (as the case may be) the Deed of Covenant. This indemnity constitutes a separate and independent obligation from the other obligations under this Guarantee and shall give rise to a separate and independent cause of action.

3. Taxes

The Guarantor covenants in favour of each Holder and each Relevant Account Holder that it will duly perform and comply with its obligations expressed to be undertaken by it in Condition 8.

4. Preservation of Rights

4.1 The obligations of the Guarantor herein contained shall be deemed to be undertaken as principal debtor.

4.2 The obligations of the Guarantor herein contained shall be continuing obligations notwithstanding any settlement of account or other matters or things whatsoever and, in particular but without limitation, shall not be considered satisfied by any intermediate payment or satisfaction of all or any of the Issuer's obligations under any Security or the Deed of Covenant and shall continue in full force and effect until all sums due from the Issuer in respect of the Securities and under the Deed of Covenant have been paid, and all other obligations of the Issuer thereunder or in respect thereof have been satisfied, in full.

4.3 Neither the obligations expressed to be assumed by the Guarantor herein contained nor the rights, powers and remedies conferred upon the Holders, the Relevant Account Holders or any of them by this Deed of Guarantee or by law shall be discharged, impaired or otherwise affected by:

4.3.1 the winding up, bankruptcy, moratorium or dissolution of the Issuer or analogous proceeding in any jurisdiction or any change in its status, function, control or ownership; or

4.3.2 any of the obligations of the Issuer under any of the Securities or the Deed of Covenant being or becoming illegal, invalid or unenforceable; or

4.3.3 time or other indulgence being granted or agreed to be granted to the Issuer in respect of its obligations under any of the Securities or the Deed of Covenant; or

4.3.4 any amendment to, or any variation, waiver or release of, any obligation of the Issuer under any of the Securities or the Deed of Covenant; or any other act, event or omission which, but for this Clause 4.3, might operate to discharge, impair or otherwise affect the obligations expressed to be assumed by the Guarantor herein or any of the rights, powers

or remedies conferred upon the Holders, the Relevant Account Holders or any of them by this Deed of Guarantee or by law.

4.4 Any settlement or discharge between the Guarantor and the Holders, the Relevant Account Holders or any of them shall be conditional upon no payment to the Holders, the Relevant Account Holders or any of them by the Issuer or any other person on the Issuer's behalf being avoided or reduced by virtue of any provisions or enactments relating to bankruptcy, insolvency or liquidation for the time being in force and, in the event of any such payment being so avoided or reduced, the Holders and the Relevant Account Holders shall each be entitled to recover the amount by which such payment is so avoided or reduced from the Guarantor subsequently as if such settlement or discharge had not occurred.

4.5 No Holder or Relevant Account Holder shall be obliged before exercising any of the rights, powers or remedies conferred upon it by this Deed of Guarantee or by law:

4.5.1 to make any demand of the Issuer, other than (in the case of a Holder) the presentation of the relevant Security; or

4.5.2 to take any action or obtain judgment in any court against the Issuer; or

4.5.3 to make or file any claim or proof in a winding-up or dissolution of the Issuer and, save as aforesaid, the Guarantor hereby expressly waives, in respect of each Security, presentment, demand and protest and notice of dishonour.

4.6 The Guarantor agrees that so long as any amounts are or may be owed by the Issuer under any of the Securities or the Deed of Covenant or the Issuer is under any actual or contingent obligations thereunder, the Guarantor shall not exercise rights which the Guarantor may at any time have by reason of performance by the Guarantor of its obligations hereunder:

4.6.1 to claim any contribution from any other guarantor of the Issuer's obligations under the Securities or the Deed of Covenant; and/or

4.6.2 to take the benefit, in whole or in part, of any security enjoyed in connection with, any of the Securities or the Deed of Covenant issued by the Issuer, by any Holder or Relevant Account Holder; and/or

4.6.3 to be subrogated to the rights of any Holder or Relevant Account Holder against the Issuer in respect of amounts paid by the Guarantor under this Deed of Guarantee.

5. Conditions, Status and Subordination

5.1 The Guarantor undertakes to comply with and be bound by those provisions of the Conditions which relate to it and which are expressed to relate to it.

5.2 The Guarantor undertakes that its obligations hereunder rank, and will at all times rank, as described in Condition 3(b).

5.3 In the event of the Guarantor being declared in insolvency ("*concurso*") under Spanish insolvency law, the provisions of Condition 3(c) shall apply.

6. Delivery of Deed of Guarantee

A duly executed original of this Guarantee shall be delivered promptly after execution to the Fiscal Agent and such original shall be held to the exclusion of the Guarantor until the date on which complete performance by the Guarantor of the obligations contained in this Guarantee and in the Securities occurs. A certified copy of this Guarantee may be obtained by any Holder or any Relevant Account Holder from the Fiscal Agent at its specified office at the expense of such Holder or Relevant Account Holder. Any Holder or Relevant Account Holder may protect and enforce his rights under this Guarantee (in the courts specified in Clause 11 below) upon the basis described in the Deed of Covenant (in the case of a Relevant Account Holder) and a copy of this Guarantee certified as being a true copy by a duly authorised officer of the Issue and Paying Agent without the need for production in any court of the actual records described in the

Deed of Covenant or this Guarantee. Any such certification shall be binding, except in the case of manifest error or as may be ordered by any court of competent jurisdiction, upon the Guarantor and all Holders and Relevant Account Holders. This Clause shall not limit any right of any Holder or Relevant Account Holder to the production of the originals of such records or documents or this Guarantee in evidence.

7. Deed Poll; Benefit of Guarantee

7.1 This Deed of Guarantee shall take effect as a Deed Poll for the benefit of the Holders and the Relevant Account Holders from time to time.

7.2 The obligations expressed to be assumed by the Guarantor herein shall enure for the benefit of each Holder and Relevant Account Holder, and each Holder and each Relevant Account Holder shall be entitled severally to enforce such obligations against the Guarantor.

7.3 The Guarantor may not assign or transfer all or any of its rights, benefits and obligations hereunder except for the purpose of and followed by a reconstruction, amalgamation, reorganisation, merger or consolidation of the Guarantor on terms approved by an Extraordinary Resolution of the Holders.

8. Provisions Severable

If at any time any provision hereof is or becomes illegal, invalid or unenforceable in any respect under the laws of any jurisdiction, neither the legality, validity or enforceability of the remaining provisions hereof nor the legality, validity or enforceability of such provision under the laws of any other jurisdiction shall in any way be affected or impaired thereby

9. Notices

9.1 All communications to the Guarantor hereunder shall be made in writing (by letter, telex or fax) and shall be sent to the Guarantor at:

Address: Distrito Telefónica
Edificio Central
c/ Ronda de la Comunicación, s/n
28050 Madrid

Fax: + 34 91 727 1397

Attention: Miguel Escrig Meliá

or to such other address or fax number or for the attention of such other person or department as the Guarantor has notified to the Holders in the manner prescribed for the giving of notices in connection with the Securities.

9.2 Every communication sent in accordance with Clause 9.1 shall be effective upon receipt by the Guarantor; and provided, however, that any such notice or communication which would otherwise take effect after 4.00 p.m. on any particular day shall not take effect until 10.00 a.m. on the immediately succeeding business day in the place of the Guarantor.

10. Law and Jurisdiction

10.1 Governing Law: This Deed of Guarantee and all non-contractual obligations arising from or connected with it, are governed by and shall be construed in accordance with English law, except for the provisions of Conditions 3(b) and 3(c) referred to in Clauses 5.2 and 5.3, respectively, which shall be governed by and construed in accordance with Spanish law.

10.2 English courts: The courts of England have exclusive jurisdiction to settle any dispute (a "**Dispute**"), arising from or connected with this Deed of Guarantee (including a dispute regarding the existence, validity or termination of this Deed of Guarantee) or the consequences of its nullity.

- 10.3 Appropriate forum: The Guarantor agrees that the courts of England are the most appropriate and convenient courts to settle any Dispute and, accordingly, that it will not argue to the contrary.
- 10.4 Rights of the Holders and Relevant Account Holders: Clause 10.2 (*English courts*) is for the benefit of the Holders and the Relevant Account Holders only. As a result, nothing in this Clause 10 (*Law and jurisdiction*) prevents the Holders and Relevant Account Holders from taking proceedings relating to a Dispute ("**Proceedings**") in any other courts with jurisdiction. To the extent allowed by law, the Holders and Relevant Account Holders may take concurrent Proceedings in any number of jurisdictions.
- 10.5 Process agent: The Guarantor agrees that the documents which start any Proceedings and any other documents required to be served in relation to those Proceedings may be served on it by being delivered to Telefónica UK Limited, 260 Bath Road, Slough SL1 4DX, United Kingdom or, if different, its registered office for the time being or at any address of the Guarantor in the United Kingdom at which process may be served on it in accordance with Part 34 of the Companies Act 2006. If such person is not or ceases to be effectively appointed to accept service of process on behalf of the Guarantor, the Guarantor shall, on the written demand of any Holder or Relevant Account Holder addressed and delivered to the Guarantor appoint a further person in England to accept service of process on its behalf and, failing such appointment within 15 days, any Holder or Relevant Account Holder shall be entitled to appoint such a person by written notice addressed to the Guarantor and delivered to the Guarantor. Nothing in this paragraph shall affect the right of any Holder or Relevant Account Holder to serve process in any other manner permitted by law. This clause applies to Proceedings in England.

In witness whereof this Deed has been signed as a deed by the Guarantor and is hereby delivered on the date first above written.

SIGNED as a **DEED** and **DELIVERED**)
on behalf of Telefónica, S.A.)
a company incorporated in the Kingdom of Spain)
by:)
[•])
being a person who, in accordance with)
the laws of that territory are acting under)
the authority of the company)

USE OF PROCEEDS

The net proceeds of the issue of the Securities, expected to amount to EUR 1,739,500,000 will be used for general corporate purposes of the Guarantor and its Group, including the preservation of the liquidity cushion and debt refinancing.

DESCRIPTION OF THE ISSUER

Introduction

Telefónica Europe B.V. (the "**Issuer**") was incorporated for an indefinite period in 1996 in The Netherlands as a private company with limited liability (*besloten vennootschap met beperkte aansprakelijkheid*) under the laws of The Netherlands. Its statutory seat is at Amsterdam, The Netherlands, and its business address since 1 October 2013 is at Zuidplein 112, H Tower, 13th floor, 1077XV Amsterdam, The Netherlands. The Issuer's telephone number is +31(0)20 575 3370. Telefónica Europe B.V. is registered with the Chamber of Commerce under number 24269798. The authorised share capital of the Issuer is €46,000 represented by 100 ordinary shares having a nominal value of €460 each. The share capital of the Issuer is fully subscribed and paid up by Telefónica, S.A. as the sole shareholder.

Business

Telefónica Europe B.V. is a wholly-owned subsidiary of the Guarantor and one of its principal purposes is acting as a holding company and raising finance for the Telefónica Group. The Issuer raises funds primarily by issuing negotiable, and non-negotiable, instruments into the capital and money markets.

Directors

The Directors of the Issuer are as follows:

<u>Name</u>	<u>Principal occupation</u>	<u>Principal External Activities</u>
Carlos David Maroto Sobrado	Director	Head of Financing Subsidiaries and Equity at Telefónica, S.A.
Maria Christina van der Sluijs-Plantz	Director	Director of TMF Orange Holding BV
Alfredo Javier Aleix Arguelles	Director	Managing Director of Telfisa Global B.V.
Eduardo José Alvarez Gómez	Director	Head of Financing at Telefónica, S.A.

The business address of each of the directors of the Issuer is Zuidplein 112, H Tower, 13th floor, 1077XV Amsterdam, The Netherlands.

There are no potential conflicts of interest between any duties owed by the directors of the Issuer to the Issuer and their respective private interests and/or other duties.

Auditors

The auditors of the Issuer, Ernst & Young Accountants LLP., at Antonio Vivaldistraat 150, 1083 HP, Amsterdam, The Netherlands, are registered auditors in The Netherlands with The Netherlands Institute of Chartered Accountants and registered with the Chamber of Commerce with registration number 24432944.

DESCRIPTION OF THE GUARANTOR

Introduction

Telefónica, S.A. ("**Telefónica**" or the "**Guarantor**") is a corporation duly organised and existing under the laws of the Kingdom of Spain, incorporated on 19 April 1924. The registered office of the Guarantor is at Gran Vía 28, 28013 Madrid, Spain, telephone number (Spain) +34 91 482 34 33. The Telefónica Group is:

- a diversified telecommunications group which provides a comprehensive range of services through one of the world's largest and most modern telecommunications networks;
- focused on providing telecommunications services; and
- present principally in Europe and Latin America.

Telefónica has been assigned long term credit ratings of BBB (negative outlook), Baa2 (negative outlook), BBB+ (negative outlook), respectively, by S&P, Moody's and Fitch. Telefónica has been assigned short term credit ratings of A2, P2 and F2, respectively, by S&P, Moody's and Fitch. Each of S&P, Moody's and Fitch is established in the European Union and is registered under the CRA Regulation.

The following significant events have occurred since 31 December 2012:

- On 8 February 2013, the bolívar fuerte was devalued from 4.3 bolívares fuertes per U.S. dollar to 6.3 bolívares fuertes per U.S. dollar.

The exchange rate of 6.3 bolívares fuertes per U.S. dollar has been used in the conversion of the financial information of Venezuelan subsidiaries for the whole year 2013. The principal impacts of the devaluation of the bolívar fuerte have been the following:

- The decrease of the Telefónica Group's net assets in Venezuela as a result of the conversion to euro at the new exchange rate with a balancing entry in Group equity of approximately €1,000 million, based on the net assets as at 31 December 2012.
- Increase in the net financial debt resulting from application of the new exchange rate to the net asset value in bolívar fuerte of approximately €873 million, as per the balance as at 31 December 2012.

The income and cash flows from Venezuela will be converted at the new devalued closing exchange rate as of 1 January 2013.

- On 20 February 2013, Telefónica UK Limited ("**Telefónica UK**") was awarded two 10 MHz blocks in the 800 MHz spectrum band in the UK spectrum auction.

The total investment by Telefónica UK in new frequencies amounted to €719 million.

- On 26 March 2013, Telefónica placed 90,067,896 treasury shares (representing 1.979% of its share capital) to qualified and professional investors, at €10.80 per share. These shares were the total treasury shares position of Telefónica as of that date. The terms and conditions of this sale and the final share price were duly notified by the company to the Spanish National Securities and Exchange Commission (the "**CNMV**").
- On 24 April 2013, the Board of Directors of Telefónica approved, upon the prior recommendation from its Nominating, Compensation and Corporate Governance Committee, the appointment as member and Chairman of the Audit and Control Committee of its independent director Mr. Carlos Colomer Casellas, to replace (having completed his legal term) the independent director Mr. Gonzalo Hinojosa Fernández de Angulo, who remains as member of the aforementioned Committee.

Likewise, the Company's Board of Directors resolved to appoint Mr. Gonzalo Hinojosa Fernández de Angulo as member and Chairman of the Regulation Committee, to replace as

chairman the independent director Mr. Pablo Isla Álvarez de Tejera, who remains as member of the aforementioned Committee.

- On 30 April 2013, Telefónica reached an agreement with Corporación Multi Inversiones ("CMI"), for the sale of 40% of Telefónica's stake in its subsidiaries in Guatemala, El Salvador, Nicaragua and Panama. The transaction amounted to 500 million U.S. dollars plus a variable amount of up to 72 million U.S. dollars, according to the future evolution of the transferred assets. On 19 July 2013, Telefónica announced that the conditions to which the transaction was subject had been met and the transaction was completed thereafter.
- On 31 May 2013, Telefónica's Annual General Shareholders' Meeting took place on second call, with an attendance, present or represented, of 54.47 % of the share capital. In such meeting, all the resolutions submitted by the Board of Directors for deliberation and vote were approved by majority of votes.

Also, on 31 May 2013, the Board of Directors of Telefónica, upon the prior recommendation of the Nominating, Compensation and Corporate Governance Committee, adopted the resolutions listed below:

- To re-elect the directors Mr. José María Abril Pérez and Mr. Javier de Paz Mancho, as members of the Executive Commission.
- To appoint the director Mr. Ignacio Moreno Martínez as a member of the Audit and Control Committee; Service Quality and Customer Service Committee; and Regulation Committee.
- To appoint the director Mr. Julio Linares López as a member of the Strategy Committee.
- To accept the resignation of the director Mr. Pablo Isla Álvarez de Tejera as member of the Service Quality and Customer Service Committee and to appoint the Director Mr. Javier de Paz Mancho member of the aforesaid Committee.
- To create an Institutional Affairs Committee, which will be composed of the following Directors: Mr. Javier de Paz Mancho, Mr. Alfonso Ferrari Herrero, Mr. Gonzalo Hinojosa Fernández de Angulo, Mr. Antonio Masanell Lavilla, Mr. Fernando de Almansa Moreno-Barreda and Mr. Julio Linares López, who will assume its presidency.
- To eliminate the International Affairs Committee and the Human Resources, Corporate Reputation and Responsibility Committee.

Finally, the Board of Directors of the Company, as requested by the Nominating, Compensation and Corporate Governance Committee, has resolved to appoint the Director Mr. Alfonso Ferrari Herrero, Coordinating Independent Director, in accordance with article 32 of the Company's Bylaws approved by the Annual General Shareholders' Meeting held on such date.

- On 24 June 2013, Telefónica reached an agreement with Hutchison Whampoa Limited for the total divestment by the Telefónica Group of its shares of Telefónica Ireland, Ltd. The value of the sale totalled €850 million, including an initial cash consideration of €780 million at closing of the transaction, and an additional deferred payment of €70 million based on the completion of agreed financial objectives. The transaction is subject, among other conditions, to the relevant competition approvals.
- On 23 July 2013, Telefónica and its German listed subsidiary Telefónica Deutschland Holding AG (hereinafter, "**Telefónica Deutschland**") entered into an agreement (amended on 26 August 2013) with the Dutch company Koninklijke KPN N.V. (hereinafter, "**KPN**") under which Telefónica Deutschland committed itself to acquire the shares of the German subsidiary of KPN, E-Plus Mobilfunk GmbH & Co. KG (hereinafter, "**E-Plus**") receiving KPN, as consideration, 24.9% of the shares of Telefónica Deutschland and €3,700 million.

Telefónica committed to subsequently acquire from KPN 4.4% of Telefónica Deutschland for a total amount of €1,300 million, and, as a result of the acquisition, KPN's stake in Telefónica Deutschland will be reduced to 20.5%.

Telefónica also committed to subscribe the proportional corresponding share in the capital increase approved by Telefónica Deutschland in the Extraordinary General Meeting held on 11 February 2014, to finance the cash consideration of the transaction.

The closing of this transaction is subject to certain conditions of which only the relevant authorisation from the Competition Authority remains.

- On 24 September 2013, Telefónica and the remaining shareholders of the Italian company Telco, (which holds a capital stake of 22.4% of the voting share capital of Telecom Italia S.p.A. ("**Telecom Italia**")) reached an agreement by virtue of which Telefónica subscribed for and paid out a capital increase in Telco through the contribution of €324 million in cash, receiving in return non-voting shares of Telco. As a result of this capital increase, the interest held by Telefónica in the voting share capital of Telco remained unchanged (i.e. 46.18%), although its interest in the total share capital of Telco has increased to 66%. The current governance structure remained unaffected, including the obligation by Telefónica not to participate in or influence any decisions which could affect the markets in which both Telefónica and Telecom Italia are present. Further details are provided in the Strategic Partnership section.
- On 25 September 2013, the Board of Directors of Telefónica, pursuant to the resolution passed at the Shareholders' Meeting of Telefónica held on 31 May 2013, fixed 6 November 2013 as the date for the dividend distribution charged to unrestricted reserves, of a fixed gross amount of €0.35 for each Company share issued, in circulation, and carrying entitlement to this distribution.
- On 5 November 2013, Telefónica reached an agreement with PPF Group N.V. to sell 65.9% of Telefónica Czech Republic, a.s. ("**Telefónica Czech Republic**") for approximately 306 Czech Crowns per share in cash (approximately €2,467 million at the date of the agreement). The transaction was completed on 28 January 2014, after obtaining the relevant regulatory authorisation.
- On 18 December 2013, the Board of Directors of Telefónica approved, upon the prior recommendation of the Nominating, Compensation and Corporate Governance Committee, the appointment of the Vice-Chairman of the Board of Directors, Mr. Julio Linares López, as a member of the Innovation Board Committee of Telefónica.

The following significant events have occurred since 31 December 2013:

- On 24 January 2014, Exchange Agreement No. 25 came into force, which regulates the sale of foreign currency in the Republic of Venezuela for certain sectors and items. This Agreement does not amend the exchange rate of 6.3 bolívares fuertes per U.S. dollar, which has applied since Exchange Agreement No. 14 was approved on 8 February 2013, except for: (i) cash for travelling abroad and remittances to individuals domiciled abroad; (ii) payment of operations inherent to national civil aviation and the international air transportation public service; (iii) operations inherent to insurance activity; (iv) leasing and service agreements, agreements for the import of intangible assets, payments of rental contracts for networks, and payments corresponding to the telecommunications sector; and (v) foreign investments and payments of royalties, use and exploitation of patents, trademarks and franchises, as well as technology import and technical assistance agreements.

Requests for the liquidation in U.S. dollars of the aforementioned concepts will be settled, at the foreign exchange rate resulting from the allocations conducted through the Complementary System for Administration of Foreign Currency (SICAD). The SICAD allocation as of 15 January 2014 resulted in an exchange rate of 11.36 bolívares fuertes per U.S. dollar. Nonetheless, the aforesaid Agreement stipulates that the liquidation of foreign currency operations requested before the Central Bank of Venezuela before Exchange Agreement No. 25 came into force, will be settled at the exchange rate established in the 8 February 2013 Exchange Agreement, i.e. at a rate of 6.3 bolívares fuerte per U.S. dollar.

The change to the currency exchange system introduced in the aforesaid Agreement will take effect in the Telefónica Group's consolidated financial statements from the moment it comes into force, on 24 January 2014. It is therefore a subsequent event that does not impact the consolidated financial statements, as the previous exchange rate of 6.3 bolívares fuertes per U.S. dollar was in force as at the year ended 31 December 2013 and up to 24 January 2014 for all foreign currency transactions.

The main aspects to be considered in 2014 are as follows. In order to estimate the impacts in euro, the rate used is the exchange rate resulting from the SICAD allocation as of 15 January 2014, amounting to 11.36 bolívares fuertes per U.S. dollar, which will vary throughout 2014.

- The decrease of the Telefónica Group's net assets in Venezuela as a result of the conversion to euro at the new exchange rate with a balancing entry in Group equity of approximately €1,800 million, based on the net assets as at 31 December 2013.
- As part of the decrease mentioned in the preceding paragraph, the value in euro of the net financial assets denominated in bolívar fuerte will decrease by approximately €1,200 million, as per the balance sheet as at 31 December 2013.

On the other hand, it should be noted that Exchange regulations in Venezuela are in constant evolution. Thus, on 20 February 2014, the Government of Venezuela announced a complementary currency system identified as "SICAD 2", in addition to those already in existence, which will revoke the Act of Illicit Exchange ("*Ley de Ilícitos Cambiarios*") and will create an alternative market with bands of exchange rates, which will be regulated by the Central Bank of Venezuela. However, as of the date of authorisation for issue of this Prospectus, the system described in such announcement or the corresponding measures have not yet been formalised.

- On 28 January 2014, after obtaining the relevant regulatory approval, the sale of Telefónica Czech Republic, was completed. Subsequent to the sale, Telefónica holds a 4.9% stake in Telefónica Czech Republic.
- On 26 February 2014, the Board of Directors of Telefónica approved the implementation of a new organisational structure focused on clients and that incorporates the digital offering as the main focus for commercial policies. The structure aims to give greater visibility to local operations, bringing them closer to the corporate decision-making centre, simplifying the global structure and strengthening the transverse areas to make the decision-making process more efficient.

Within this framework, Telefónica has created the role of the Chief Commercial Digital Officer, who will be responsible for fostering revenue growth. On the cost side, the Company has strengthened the role of the Chief Global Resources Officer. Both Officers will report directly to the Chief Operating Officer (COO), as will the local business CEOs for Spain, Brazil, Germany and the United Kingdom, in addition to the Latin American Unit, now without Brazil.

The new model integrates the activities carried out to date by Telefónica Digital Limited, Telefónica Europe Plc ("**Telefónica Europe**") and Telefónica Latin America (Latam) into the Global Corporate Centre, thus simplifying the organisation.

- On 27 February 2014, the Board of Directors of Telefónica has agreed, regarding the 2014 dividend, to determine the amount thereof at €0.75 per share, payable in two tranches:
 - €0.35 per share by means of a "scrip dividend" in the fourth quarter of 2014.
 - €0.40 per share in cash in the second quarter of 2015.
- Regarding the 2013 dividend amounting to €0.75 per share, with a first tranche of €0.35 per share already paid in cash in November 2013, the Company confirms that the second tranche amounting to €0.40 per share will be paid in cash in the second quarter of 2014. The adoption of the corresponding corporate resolutions will be proposed in due course.

Business Overview

2013 highlights

The following table and description summarise the accesses of the Telefónica Group over the years ended 31 December 2013 and 2012:

ACCESSES	2012 December	2013 December	Percentage variation (%) 2012/2013
	<i>Unaudited figures (thousands)</i>		
Final Clients Accesses	310,088.3	316,759.9	2.2%
Fixed telephony accesses ⁽¹⁾⁽²⁾⁽³⁾	40,002.6	39,338.5	(1.7)%
Internet and data accesses	19,402.6	19,102.0	(1.5)%
Narrowband	653.2	510.8	(21.8)%
Broadband ⁽⁴⁾⁽⁵⁾	18,596.2	18,447.8	(0.8)%
Other ⁽⁶⁾	153.1	143.4	(6.3)%
Mobile accesses	247,346.9	254,717.2	3.0%
Prepay	165,821.9	165,557.0	(0.2)%
Contract ⁽²⁾⁽⁸⁾	81,525.0	89,160.3	9.4%
Pay TV	3,336.2	3,602.2	8.0%
Wholesale Accesses	5,731.3	6,358.5	10.9%
Unbundled loops	3,308.8	3,833.4	15.9%
Shared ULL	183.5	130.6	(28.9)%
Full ULL	3,125.3	3,702.9	18.5%
Wholesale ADSL	845.4	866.9	2.5%
Other	1,577.1	1,658.2	5.1%
Total Accesses	315,819.6	323,118.4	2.3%

Note:

- Telefónica Spain mobile accesses include since 2013 the accesses of Tuenti. Figures for the year ended 31 December 2012 have been revised for comparison.

(1) PSTN (including Public Use Telephony) x1; ISDN Basic access x1; ISDN Primary access; 2/6 Access x30. Company's accesses for internal use and total fixed wireless included. Includes VoIP and Naked ADSL.

(2) In the second quarter of 2013, 209 thousand accesses were disconnected due to the disposal of the assets of the fixed business in UK.

(3) ADSL, satellite, optical fiber, cable modem and broadband circuits.

(4) In the second quarter of 2013, 511 thousand accesses were disconnected due to the disposal of the assets of the fixed business in UK.

(5) Retail circuits other than broadband.

(6) The first quarter of 2013 includes the disconnection of 114 thousand inactive accesses in Czech Republic.

Telefónica managed a total of almost 323 million accesses at the end of 2013, up 2.3% year-on-year, driven by contract mobile customers, in particular in the mobile broadband segment, and pay TV accesses. Telefónica Latin America (69% of the total) showed the greatest increase, posting an increase in accesses of +4.2% year-on-year. It is important to note that the variance in accesses is impacted by the sale of the fixed business's residential assets in the UK and the disconnection of some inactive accesses (Czech Republic).

The Telefónica Group's strategy is based on capturing growth in the telecommunications markets and especially on attracting high-value-added customers.

In the mobile segment, contract accesses rose by 9.4% to 89.2 million and now account for 35% of the total mobile customer base (+2 percentage points year-on-year), underlining the focus on the high-value segment.

The Company's mobile broadband accesses stood at 72.8 million in December 2013, maintaining solid growth of 38% year-on-year, and representing 29% of mobile accesses (+7 percentage points year-on-year). Underpinning this growth was the strong performance of smartphones, which achieved a

penetration of 27% in terms of mobile Internet tariffs over the customer base (+8 percentage points year-on-year), with net additions of 20.7 million (+35% year-on-year).

Telefónica's customer base includes the consumer and business segments, and therefore is less affected by customer concentration risk.

Segment Outlook

Telefónica Latin America

ACCESSES	2012 December	2013 December	Percentage variation (%) 2012/2013
	<i>Unaudited figures (thousands)</i>		
Final Clients Accesses	211,908.0	221,046.7	4.3%
Fixed telephony accesses ⁽¹⁾	24,153.3	24,526.3	1.5%
Internet and data accesses	8,732.5	9,239.7	5.8%
Narrowband	209.1	125.5	(40.0)%
Broadband ⁽²⁾	8,415.3	9,011.7	7.1%
Other ⁽³⁾	108.0	102.6	(5.0)%
Mobile accesses	176,595.4	184,507.0	4.5%
Prepay	137,141.5	138,076.0	0.7%
Contract	39,453.9	46,431.0	17.7%
Pay TV	2,426.8	2,773.6	14.3%
Wholesale Accesses	47.0	41.5	(11.7)%
Total Accesses Telefónica Latam	211,955.1	221,088.2	4.3%
Terra Accesses	604.7	412.5	(31.8)%
Total Accesses in Latin America	212,559.8	221,500.7	4.2%

⁽¹⁾ PSTN (including public use telephony) x1; ISDN basis access x1; ISDN primary access; 2/6 access x30. Includes the Group's accesses for internal use and total fixed wireless accesses.

⁽²⁾ Includes ADSL, fiber optic, cable modem and broadband circuits.

⁽³⁾ Remaining retail circuits other than broadband

Evolution of competitive position:

Telefónica Latin América	2012 December	2013 December
<i>Mobile Market Share (1)</i>		
Brazil	29.1%	28.6%
Argentina	29.7%	31.4%
Chile	38.8%	38.7%
Peru	60.0%	59.7%
Colombia	21.6%	24.0%
Venezuela	32.9%	32.0%
Mexico	19.2%	18.5%
Central America	29.7%	31.8%
Ecuador	29.3%	32.6%
Uruguay	37.4%	35.8%

⁽¹⁾ Company estimation

Telefónica Latin América	2012 December	2013 December
<i>Share of ADSL (1)</i>		
Brazil	18.8%	16.3%
Argentina	30.9%	30.5%
Chile	41.2%	40.2%
Peru	90.1%	86.9%
Colombia	18.1%	18.7%

⁽¹⁾ Company estimation

Main 2013 trends in the mobile business

- Estimated total market penetration in Latin America at the end of December 2013 was 118% (+2.9 percentage points year-on-year).
- Mobile accesses reached 184.5 million at year end (+4.5% year-on-year growth), with notable growth in accesses in the contract segment (+17.7%) and despite the impact of the application a more restrictive criteria in the calculation of the number of customers for the prepay segment (+0.7%). Contract accesses represented 25% of total mobile accesses and totalled 46.4 million as at 31 December 2013.
- The continued growth in mobile broadband accesses is noteworthy, reaching 43.6 million at year end (increasing year-on-year 60%) leveraged on the strong demand for smartphones, whose access base grew 75% year-on-year and increased its weight by 9 percentage points over the entire mobile access base.
- Net additions stood at 7.9 million for the year, boosted by the 60% year-on-year growth in contract accesses, with 7.0 million new accesses in 2013 (+64% year-on-year).
- Traffic grew by 9% year-on-year, with year-on-year growth reported in all the countries in the region.
- ARPU growth year-on-year was 5.7%, despite the reduction of mobile termination rates. Thus, outgoing ARPU posted year-on-year growth of 8.4%, driven by non-SMS data and the growth in voice traffic.

Key 2013 trends in the fixed line business

- Total accesses reached 36.6 million as of 31 December 2013, growing year-on-year by 3%.
- Traditional business accesses stood at 24.5 million, up 1.5% year-on-year, reflecting the acceleration in the capture of new accesses, with net additions of 373 thousand in the year ended 31 December 2013.
- Broadband accesses amounted to 9.0 million (year-on-year growth of 7.1%) with net additions of 596 thousand in the year. Thus, broadband accesses represented 37% of traditional business accesses, increasing 2 percentage points year-on-year.
- Pay TV accesses stood at 2.8 million, with year-on-year growth of 14.3%, with net additions of 347 thousand in the year ended 31 December 2013, despite the commercial repositioning of MMDS (multichannel multipoint distribution service) in Brazil, which resulted in a reduction of 71 thousand clients.

Brazil

	2012 December	2013 December	Percentage variation (%) 2012/2013
<i>Unaudited figures (thousands)</i>			
BRAZIL			
Final Clients Accesses.....	91,345.4	92,730.0	1.5%
Fixed telephony accesses ⁽¹⁾	10,642.7	10,747.8	1.0%
Internet and data accesses.....	3,964.3	4,102.0	3.5%
Narrowband.....	137.9	92.1	(33.2)%
Broadband ⁽²⁾	3,748.4	3,936.7	5.0%
Other ⁽³⁾	78.1	73.2	(6.2)%
Mobile accesses.....	76,137.3	77,240.2	1.4%
Prepay.....	57,335.1	53,551.9	(6.6)%
Contract.....	18,802.2	23,688.3	26.0%
Pay TV.....	601.2	640.1	6.5%
Wholesale Accesses.....	24.4	18.8	(22.8)%
Total Accesses.....	91,369.8	92,748.9	1.5%

⁽¹⁾ PSTN (including public use telephony) x1; ISDN basis access x1; ISDN primary access; 2/6 access x30. Includes the Group's accesses for internal use and total fixed wireless accesses.

⁽²⁾ Includes ADSL, fiber optic, cable modem and broadband circuits.

⁽³⁾ Remaining retail circuits other than broadband

	2012 December	2013 December	Percentage variation (%) 2012/2013 (local currency)
<i>Unaudited figures</i>			
BRAZIL			
Traffic (Million minutes) ⁽¹⁾	113,955	115,698	1.5%
ARPU (EUR).....	8.9	8.0	2.3%

⁽¹⁾ From the third quarter of 2013, duplicated traffic was deleted following the integration of fixed and mobile companies.

In 2013, Telefónica Brasil S.A. ("**Telefónica Brasil**") strengthened its competitive positioning in the market; reinforcing its leadership in high value segments of the mobile market through ongoing service innovation and differential coverage and network quality and in the fixed market through a renewed commercial offer and deployment of the fiber network.

In the fixed business, in addition to the fiber network in Sao Paulo, Telefónica Brasil also continued to develop fixed wireless technology, which enables fixed services to be offered in areas where the copper network has not been installed. With the aim of strengthening its portfolio and broadband services, Telefónica Brasil has also relaunched "Vivo Internet Box", which provides mobile Internet associated with a WiFi modem with a capacity of up to 40 GB.

Innovative services continue to be launched, such as the new mobile generation network deployment of both 3G and 4G, which was launched in the second quarter and now covers 73 cities and the launch of "Multivivo", a product which allows data and/or voice to be shared between several devices and that already had 1.4 million users as at the year ended 31 December 2013.

Argentina

	2012 December	2013 December	Percentage variation 2012/2013
<i>Unaudited figures (thousands)</i>			
ARGENTINA			
Final Clients Accesses.....	24,121.9	26,636.7	10.4%
Fixed telephony accesses ⁽¹⁾	4,762.4	4,833.5	1.5%
Fixed wireless.....	234.6	342.7	46.0%
Internet and data accesses.....	1,755.5	1,848.5	5.3%
Narrowband.....	19.3	12.9	(32.8)%
Broadband ⁽²⁾	1,736.3	1,835.5	5.7%
Mobile accesses.....	17,604.0	19,954.7	13.4%
Prepay.....	11,000.0	12,916.6	17.4%
Contract.....	6,604.0	7,038.1	6.6%
Wholesale Accesses.....	14.1	14.0	(0.4)%
Total Accesses.....	24,136.0	26,650.7	10.4%

(1) PSTN (including public use telephony) x1; ISDN basis access x1; ISDN primary access; 2/6 access x30. Includes the Group's accesses for internal use and total fixed wireless accesses.

(2) Includes ADSL, fiber optic, cable modem and broadband circuits.

CUMULATIVE SELECTED OPERATING MOBILE BUSINESS DATA	2012 December	2013 December	Percentage variation (%) 2012/2013 (local currency)
<i>Unaudited figures</i>			
ARGENTINA			
Traffic (Million minutes).....	21,201	22,540	6.3%
ARPU (EUR).....	11.0	9.4	5.9%

In 2013 Telefónica Argentina, S.A. ("**Telefónica Argentina**") consolidated its market leadership thanks to its competitive position and ongoing focus on quality and innovation in its products and services.

Telefónica Argentina launched Quam, a secondary brand to Movistar for mobile telephony services, reflecting its commitment to innovation by being the first telecommunications company to launch an offering of this type in the region. This new offering gives Telefónica access to fresh market segments with a simple proposal that combines various minute, SMS and data bundles and is aimed at ensuring that the youngest customers in the prepay segment are always connected.

Venezuela and Central America

The following tables present combined figures of Venezuela and Central America for the year ended 31 December 2013, and the figures for the year ended 31 December 2012 have been revised for comparison:

	2012 December	2013 December	Percentage variation (%) 2012/2013
<i>Unaudited figures (thousands)</i>			
VENEZUELA AND CENTRAL AMERICA			
Final Clients Accesses.....	21,686.3	23,491.6	8.3%
Fixed telephony accesses	1,500.7	1,426.7	(4.9)%
Fixed wireless ⁽²⁾	1,340.5	1,168.7	(12.8)%
Internet and data accesses	41.0	12.4	(69.8)%
Narrowband.....	29.7	1.7	(94.3)%
Broadband ⁽³⁾	4.9	4.7	(3.9)%
Other ⁽⁴⁾	6.4	6.0	(6.4)%
Mobile accesses.....	19,929.3	21,666.8	8.7%
Prepay	18,060.2	19,489.8	7.9%
Contract	1,869.1	2,177.0	16.5%
PayTV.....	215.3	385.6	79.1%
Total Accesses ⁽¹⁾	21,686.3	23,491.6	8.3%

(1) Includes Guatemala, Panama, El Salvador, Nicaragua and Costa Rica.

(2) Fixed wireless accesses exclude since the first quarter of 2013, 58 thousand accesses included as fixed telephony accesses.

(3) Includes ADSL, optical fiber, cable modem and broadband circuits.

(4) Retail circuits other than broadband.

	2012 December	2013 December	Percentage variation (%) 2012/2013 (local currency)
<i>Unaudited figures</i>			
CUMULATIVE SELECTED OPERATING MOBILE BUSINESS DATA			
VENEZUELA AND CENTRAL AMERICA			
Traffic (Million minutes).....	27,536	32,304	17.3%
ARPU (EUR)	13.8	11.6	19.4%

During 2013, Telefónica Venezolana, C.A. ("**Telefónica Venezolana**") continued strengthening its unique position thanks to its integrated services offering and the ongoing improvements in network quality and coverage, showing a positive trend both in operational and financial terms throughout the year ended 31 December 2013.

Commercial activity in 2013 was focused on incentivising the consumption of data plans and launching new offerings adapted to customer needs depending on voice, SMS and data demand.

Underlining its commitment to innovation and maintaining a greater access to technology and comfort to its customers, the Telefónica Venezolana began a nationwide rollout of WiFi infrastructure in the fourth quarter of 2013. The goal is to install 1,000 hotspots by 2016, with a view to placing Telefónica Venezolana as the telecommunications company with the largest WiFi network in the country.

Chile

	2012 December	2013 December	Percentage variation (%) 2012/2013
<i>Unaudited figures (thousands)</i>			
CHILE			
Final Clients Accesses.....	13,142.1	13,625.2	3.7%
Fixed telephony accesses ⁽¹⁾	1,737.9	1,654.2	(4.8)%
Internet and data accesses.....	940.1	977.5	4.0%
Narrowband.....	5.5	5.2	(5.5)%
Broadband ⁽²⁾	932.0	969.9	4.1%
Other ⁽³⁾	2.5	2.4	(6.5)%
Mobile accesses.....	10,040.1	10,490.3	4.5%
Prepay.....	7,385.0	7,806.5	5.7%
Contract.....	2,655.1	2,683.8	1.1%
Pay TV.....	424.0	503.2	18.7%
Wholesale Accesses.....	4.9	5.0	2.6%
Total Accesses.....	13,147.0	13,630.2	3.7%

(1) PSTN (including public use telephony) x1; ISDN basis access x1; ISDN primary access; 2/6 access x30. Includes the Group's accesses for internal use and total fixed wireless accesses.

(2) Includes ADSL, fiber optic, cable modem and broadband circuits.

(3) Remaining retail circuits (broadband)

CUMULATIVE SELECTED OPERATING MOBILE BUSINESS DATA	2012 December	2013 December	Percentage variation (%) 2012/2013 (local currency)
<i>Unaudited figures</i>			
CHILE			
Traffic (Million minutes).....	13,064	13,339	2.1%
ARPU (EUR).....	12.0	10.9	(4.6)%

Telefónica Chile, S.A. ("**Telefónica Chile**") strengthened its leadership position in Chile in 2013 thanks to its innovative services and the ongoing improvement in the quality of its fixed and mobile network.

On 15 November 2013, Telefónica Chile announced the launch of nationwide LTE services, further expanding telecommunications in the country.

In another noteworthy development Telefónica Chile was also granted one of the three blocks of radioelectric spectrum for LTE auctioned in the 700 Mhz band. This will enable a more efficient rollout of the network for the delivery of 4G services, further strengthening Telefónica Chile's position.

Mexico

	2012 December	2013 December	Percentage variation (%) 2012/2013
<i>Unaudited figures (thousands)</i>			
MEXICO			
Mobile accesses.....	19,168.0	20,332.8	6.1%
Prepay.....	17,668.3	18,863.2	6.8%
Contract.....	1,499.7	1,469.7	(2.0)%
Fixed wireless.....	1,158.9	1,558.9	34.5%
Total Accesses.....	20,326.9	21,891.7	7.7%

2013 was a key year for the Mexican telecommunications market following the approval in June 2013 of the new Telecommunications Law that is expected to be implemented in the first half of 2014, initiating a process of structural transformation in the sector.

Telefónica Móviles México, S.A. de C.V. ("**Telefónica México**") launched the "Movistar Ilimitado" plan in April 2013 (plan in the prepaid segment with off-net minute bundles, SMS, data capacity from 50 MB and unlimited on-net calls for top-ups of more than 100 pesos) and the launch of the "Prepago Doble" plan in October 2013, which offers double the balance topped up for all top-ups. Furthermore, in December 2013, the Company initiated the launch of "Plan GigaMove", a new range of data contract plans aimed at high value customers. Depending on the plan chosen, the customer receives up to 3 GB of browsing, 1,500 SMS to any company in Mexico, Spotify Premium, Twitter, Whatsapp, Facebook and unlimited mail. Telefónica México also signed a new deal with the distributor MAZ Tiempo following the agreements made in September 2013 with the mobile virtual network operators Coppel, S.A. de C.V. and Virgin Mobile. An agreement was also reached in January 2013 with NII Holdings, Inc. whereby Telefónica México is to provide Nextel de México, S.A. de C.V. with nationwide voice and data coverage services on its 3G mobile network.

Peru

	2012 December	2013 December	Percentage variation (%) 2012/2013
<i>Unaudited figures (thousands)</i>			
PERU			
Final Clients Accesses.....	20,299.5	20,897.6	2.9%
Fixed telephony accesses ⁽¹⁾	2,883.4	2,801.5	(2.8)%
Fixed wireless.....	580.3	313.5	(46.0)%
Internet and data accesses.....	1,317.6	1,437.1	9.1%
Narrowband.....	8.2	5.0	(38.7)%
Broadband ⁽²⁾	1,288.3	1,411.1	9.5%
Other ⁽³⁾	21.0	21.0	-
Mobile accesses.....	15,196.9	15,762.0	3.7%
Prepay.....	11,555.3	11,258.7	(2.6)%
Contract.....	3,641.6	4,503.3	23.7%
Pay TV.....	901.6	897.1	(0.5)%
Wholesale Accesses.....	0.4	0.4	(8.7)%
Total Accesses.....	20,299.9	20,898.0	2.9%

(1) PSTN (including Public Use Telephony) x1; ISDN Basic access x1, ISDN Primary access, 2/6 Access x30. Includes the Group's accesses for internal use and total fixed wireless accesses..

(2) Includes ADSL, optical fiber, cable modem and broadband circuits.

(3) Retail circuits other than broadband.

During 2013, Telefónica Móviles Perú, S.A.C. ("**Telefónica Perú**") continued to consolidate its integrated services offering, focusing on improvements in service quality and on simplifying plans and tariffs. This resulted in a doubling of the speed of fixed broadband while Telefónica Perú also fostered the migration of customers to pay TV bundles with HD channels. In the mobile business, the restructuring of the tariff portfolio in favour of voice and data plans continued to drive smartphone adoption.

Telefónica Perú continued to expand telecommunications in the country, with the grant in the fourth quarter of 2013 of one of the two blocks of radioelectric spectrum for LTE auctioned on 22 July 2013 in the AWS band (2x20 MHz). A 20-year concession contract has been signed for €120 million. Telefónica Perú is aiming to introduce the 4G network to 234 district capitals (around 50% of the population) over the next five years. In keeping with this plan, Telefónica Perú launched commercial 4G services in seven districts of Lima at the end of November 2013.

Colombia

	2012 December	2013 December	Percentage variation (%) 2012/2013
<i>Unaudited figures (thousands)</i>			
COLOMBIA			
Final Clients Accesses	14,122.8	14,778.7	4.6%
Fixed telephony accesses ⁽¹⁾	1,420.4	1,447.1	1.9%
Internet and data accesses	714.0	862.2	20.8%
Narrowband.....	8.5	8.5	(0.0)%
Broadband ⁽²⁾	705.4	853.7	21.0%
Mobile accesses	11,703.6	12,121.7	3.6%
Prepay.....	8,675.2	8,818.5	1.7%
Contract.....	3,028.4	3,303.2	9.1%
Pay TV.....	284.8	347.6	22.1%
Wholesale Accesses	3.3	3.3	0.0%
Total Accesses.....	14,126.1	14,782.0	4.6%

(1) PSTN (including Public Use Telephony) x1; ISDN Basic access x1, ISDN Primary access, 2/6 Access x30. Includes the Group's accesses for internal use and total fixed wireless accesses.

(2) Includes ADSL, optical fiber, cable modem and broadband circuits.

In 2013 Telefónica Colombia maintained its commercial position since June 2012 following the merger between Telefónica Móviles Colombia, S.A. and Colombia Telecomunicaciones S.A. that strengthened Telefónica Colombia's position in the country's telecommunications sector.

The structural changes implemented by the Colombian regulator ("CRC") in the first semester of 2013 continued to boost the telecommunications market through the application of asymmetric mobile termination rates between the dominant operator and other telecommunications companies (including Telefónica Colombia). In order to adapt to the new regulatory regime and to progress with its commercial repositioning, Telefónica Colombia focused on higher-value customers in 2013 while strengthening the integrated marketing of services.

Telefónica Colombia also secured 30 MHz of spectrum in the AWS band (2x15 MHz) for the provision of LTE services at the auction on 26 June 2013 at a total cost of €109 million. In December 2013 it launched LTE services commercially, in five important cities in the country.

Telefónica Colombia managed a total of 14.8 million accesses at the end of December 2013, for year-on-year growth of 5%.

Telefónica Europe

ACCESSES	2012 December	2013 December	Percentage variation (%) 2012/2013
<i>Unaudited figures (thousands)</i>			
Final Clients Accesses	97,575.5	95,300.7	(2.3)%
Fixed telephony accesses ⁽¹⁾⁽²⁾	15,849.3	14,812.2	(6.5)%
Internet and data accesses	10,065.4	9,449.7	(6.1)%
Narrowband.....	444.1	385.3	(13.2)%
Broadband ⁽³⁾	9,576.2	9,023.6	(5.8)%
Other ⁽⁴⁾	45.1	40.8	(9.4)%
Mobile accesses.....	70,751.5	70,210.2	(0.8)%
Prepay.....	28,680.4	27,480.9	(4.2)%
Contract ⁽⁵⁾	42,071.1	42,729.2	1.6%
Pay TV.....	909.3	828.6	(8.9)%
Wholesale Accesses	5,684.3	6,317.0	11.1%
Total Accesses.....	103,259.8	101,617.7	(1.6)%

Note: Mobile accesses of Telefónica España include since 2013 the accesses of Tuenti. Figures for the year ended 31 December 2012 have been revised for comparison.

- (1) Basic Fix Line (including Public Use Telephony) x1, RDSI primary access, Digital Accesses 2/6x30. Includes internal use, VOIP and Naked ADSL.
- (2) During the second quarter of 2013, 209 thousand accesses were derecognised due to the asset sale of the Fix Business in UK.
- (3) During the second quarter of 2013, 511 thousand accesses were derecognised due to the asset sale of the Fix Business in UK.
- (4) Other non-broadband retail circuits.
- (5) During the first quarter of 2013, 114 thousand inactive accesses were derecognised in the Czech Republic.

The below table shows the evolution of Telefónica's estimated mobile market share:

Telefónica Europe	2012 December	2013 December
<i>Mobile Market Share (1)</i>		
Spain	36.2%	33.9%
United Kingdom.....	26.6%	26.5%
Germany.....	16.7%	16.9%
Czech Republic	38.6%	38.7%
Ireland	33.0%	31.4%
Slovakia	21.1%	23.7%

(1) Company estimation

Telefónica Europe	2012 December	2013 December
<i>ADSL Market Share (1)</i>		
Spain	48.8%	47.4%

(1) Company estimation

During 2013, Telefónica Europe's portfolio was restructured through the sale of operations in the Czech Republic, which completed in January 2014 after obtaining regulatory approval, and Ireland, pending regulatory approval, and with the announcement of the acquisition of E-Plus by Telefónica Deutschland.

Telefónica Europe included, at the end of 2013, the operations in Spain, United Kingdom, Germany, Czech Republic, Slovakia and Ireland.

Over 2013 Telefónica Europe has updated its commercial offering, with the launch of new tariffs, focused on the capture and growth of data both in the fixed (fiber) and mobile (4G) businesses. In this respect, the strengthening of "Movistar Fusión" in Spain, the commitment to streamline packages and to improve distribution channels in the United Kingdom, and introducing the "O2 Blue All-in" tariffs in Germany, all improved growth in mobile data.

The new "O2 Refresh" tariff was launched in April 2013 and aims to eliminate subsidies and improve the mix of distribution channels and offer customers more flexibility "to change telephones with the same frequency that telephones change". The "O2 Blue All-in" tariffs in Germany are tariffs focused on mobile data.

The greater uptake of 4G services in the United Kingdom and Germany, and the acceleration in the roll out of fiber optic and Pay TV in Spain will be the main pillars of expected growth in 2014.

Total accesses stood at 101.6 million at the end of December 2013 (-1.6% year-on-year) affected by asset disposals in Telefónica UK's fixed consumer business on 1 May 2013 (720 thousand accesses) and the disconnection of 114 thousand accesses of inactive mobile contract customers in the first quarter of 2013 in the Czech Republic.

Main 2013 trends in accesses in the mobile business include the following:

- Mobile accesses totalled 70.2 million for the year ended 31 December 2013, a decline of 0.8% year-on-year, with the contract segment continuing to increase its weight over the reduced total (61% of the base; +1 percentage points vs. 2012).
- Growth in mobile contract customers with a net gain in 2013 of 772 thousand accesses (excluding the disconnection of inactive customers in the Czech Republic). Total net mobile losses in 2013, excluding those disconnections in the Czech Republic, stood at 427 thousand accesses due to the loss of prepay customers.

- Mobile broadband accesses continued to increase and totalled 29.2 million at the end of 2013 (+14.6% year-on-year growth) driven by the growing demand for data and the strong rise in the adoption of smartphones (42% penetration in terms of mobile Internet data tariffs over total mobile customer base, at year-end; +7 percentage points, year-on-year).

Main 2013 trends in accesses in fixed business

- Retail fixed broadband accesses stood at 9.0 million (-5.8% year-on-year) for the year ended 31 December 2013 primarily impacted by the sale of the fixed business's residential assets in the UK (-511 thousand accesses). However, in 2013 an improvement was seen in net adds for the fixed broadband segment especially in the last part of the year, driven by growth in fiber optic in Spain.
- Fixed telephony accesses fell by 6.5%, year-on-year, to 14.8 million for the year ended 31 December 2013 affected by competitive pressures in the market, and by asset disposals in Telefónica UK's fixed consumer business in the second quarter (-209 thousand accesses).

Spain

ACCESSES BY COUNTRY	2012 December	2013 December	Percentage variation (%) 2012/2013
	<i>Unaudited figures (thousands)</i>		
TELEFÓNICA SPAIN			
Final Clients Accesses.....	38,821.7	36,663.6	(5.6)%
Fixed telephony accesses ⁽¹⁾	11,723.0	11,089.8	(5.4)%
Naked ADSL.....	25.0	22.8	(9.1)%
Internet and data accesses.....	5,779.3	5,899.0	2.1%
Narrowband.....	54.0	38.5	(28.7)%
Broadband ⁽²⁾	5,709.3	5,846.8	2.4%
Other ⁽³⁾	16.0	13.7	(14.2)%
Mobile accesses.....	20,608.7	19,002.1	(7.8)%
Prepay.....	5,180.5	4,262.7	(17.7)%
Contract.....	15,428.2	14,739.3	(4.5)%
Pay TV.....	710.7	672.7	(5.4)%
Wholesale Accesses.....	4,396.0	4,990.1	13.5%
WLR ⁽⁴⁾	481.2	525.8	9.3%
Unbundled loops.....	3,262.0	3,787.1	16.1%
Shared ULL.....	183.5	130.6	(28.9)%
Full ULL ⁽⁵⁾	3,078.5	3,656.5	18.8%
Wholesale ADSL.....	652.3	676.8	3.8%
Other ⁽⁶⁾	0.5	0.4	(23.9)%
Total Accesses.....	43,217.8	41,653.6	(3.6)%

Note:

- Mobile accesses of Telefónica España include since 2013 accesses of Tuenti. Figures for the year ended 31 December 2012 have been revised for comparison.

(1) Basic Fix Line (including Public Use Telephony) x1, RDSI primary access, Digital Accesses 2/6x30. Includes internal use, VOIP and Naked ADSL.

(2) ADSL, satellite, fiber optic and broadband circuits.

(3) Leases of circuits

(4) Wholesale line rental.

(5) Includes naked shared loops.

(6) Wholesale circuits

CUMULATIVE SELECTED OPERATING MOBILE BUSINESS DATA	2012 December	2013 December	Percentage variation (%) 2012/2013 (local currency)
	<i>Unaudited figures</i>		
TELEFÓNICA SPAIN			
Traffic (Million minutes).....	36,382	34,428	(5.4)%
ARPU (EUR)	20.6	17.7	(14.3)%
Prepay	8.8	7.3	(17.8)%
Contract	24.7	21.0	(15.0)%
Data ARPU (EUR).....	6.5	6.8	4.4%
% non-SMS over data revenues.....	<u>85.2%</u>	<u>92.1%</u>	<u>7.0 pp</u>

Telefónica España's 2013 results indicate the gradual recovery of the business. Revenue stabilised the pace of year-on-year decline over the year and profitability remained steady.

Through 2013, commercial activity continued, especially in fiber and, towards the end of 2013, in pay TV.

The portability figures in the mobile contract segment showed a positive trend towards the end of 2013.

At the end of 2013, "Movistar Fusión" reached 2.9 million customers, and more than one million additional mobile lines, which accounted in the consumer segment for 52% of fixed broadband and 45% of mobile contract customers). There was also a steady improvement in the percentage of new customers and/or customers taking new services.

Fiber customers reach 594 thousand as at 31 December 2013; almost double that in December 2012 (17% of passed homes, amounting to 3.5 million homes).

United Kingdom

ACCESSES BY COUNTRY	2012 December	2013 December	Percentage variation (%) 2012/2013
	<i>Unaudited figures (thousands)</i>		
TELEFÓNICA UK			
Final Clients Accesses.....	23,801.7	23,872.0	0.3%
Fixed telephony accesses ⁽¹⁾⁽²⁾	377.4	208.2	(44.8)%
Internet and data accesses	560.1	14.8	(97.4)%
Broadband ⁽³⁾	560.1	14.8	(97.4)%
Mobile accesses	22,864.2	23,649.0	3.4%
Prepay	10,962.9	10,764.7	(1.8)%
Contract.....	<u>11,901.3</u>	<u>12,884.3</u>	<u>8.3%</u>
Wholesale Accesses	40.5	31.6	(22.1)%
Total Accesses.....	<u>23,842.2</u>	<u>23,903.6</u>	<u>0.3%</u>

⁽¹⁾ Basic Fix Line (including Public Use Telephony) x1, RDSI primary access, Digital Accesses 2/6x30. Includes internal use, VOIP and Naked ADSL

⁽²⁾ In the second quarter of 2013, 209 thousand accesses disconnected after sale of fixed assets in UK

⁽³⁾ In the second quarter of 2013, 511 thousand accesses disconnected after sale of fixed assets in UK.

CUMULATIVE SELECTED OPERATING MOBILE BUSINESS DATA	2012	2013	Percentage variation (%)
	December	December	2012/2013 (local currency)
	<i>Unaudited figures</i>		
TELEFÓNICA UK			
Traffic (Million minutes).....	48,250	48,479	0.5%
ARPU (EUR)	22.5	19.6	(8.8)%
Prepay	9.6	7.7	(16.0)%
Contract	35.0	29.9	(10.4)%
Data ARPU (EUR).....	11.4	10.4	(4.5)%
% non-SMS over data revenues.....	46.8%	50.0%	3.2 p.p.

In 2013, Telefónica UK's results maintained a solid momentum driven by the introduction of new tariffs. The new "O2 Refresh" tariff launched on 16 April 2013 aims to eliminate subsidies and improve the mix of distribution channels and offer customers more flexibility "to change telephones with the same frequency that telephones change".

Telefónica UK continued working on the deployment of its LTE network, reaching 38% outdoor coverage at the end of 2013. The first 4G customers show increased data consumption (up to 2 times higher average data consumption than 3G customers).

Total accesses reached 23.9 million at the end of December 2013 (+0.3% year-on-year) despite the impact from the disposal of the fixed assets (720 thousand accesses: 209 thousand in fixed telephony accesses and 511 thousand in fixed broadband accesses). Total mobile customers grew 3.4% year-on-year to 23.6 million at the end of December 2013 driven by the consistent mobile contract customer base growth. The contract mix increased 2 percentage points year-on-year to account for 54% of the mobile base. Contract net additions totalled 983 thousand in 2013 driven by solid gross additions, despite the highly competitive environment. Contract churn improved by 0.1 percentage points to 1.0% due to the management of its customer base. Smartphone penetration (as a percentage of mobile data tariffs over total mobile customers) grew 4 percentage points year-on-year and reached 49% by the end of December 2013.

Germany

ACCESSES BY COUNTRY	2012	2013	Percentage variation (%)
	December	December	2012/2013
	<i>Unaudited figures (thousands)</i>		
TELEFÓNICA GERMANY			
Final Clients Accesses.....	24,284.9	24,042.0	(1.0)%
Fixed telephony accesses ⁽¹⁾	2,249.0	2,124.9	(5.5)%
Internet and data accesses	2,678.9	2,516.1	(6.1)%
Narrowband.....	302.6	271.7	(10.2)%
Broadband.....	2,376.3	2,244.3	(5.6)%
Mobile accesses	19,299.9	19,401.0	0.5%
Prepay	9,191.3	9,114.9	(0.8)%
Contract.....	10,108.5	10,286.1	1.8%
Pay TV ⁽²⁾	57.2	–	n.s.
Wholesale Accesses	1,087.9	1,125.0	3.4%
Total Accesses.....	25,372.8	25,166.9	(0.8)%

Note:

⁽¹⁾ Basic Fix Line (including Public Use Telephony) x1, RDSI primary access, Digital Accesses 2/6x30. Includes internal use, VOIP and naked ADSL.

⁽²⁾ In the fourth quarter of 2013, all TV accesses were disconnected.

CUMULATIVE SELECTED OPERATING MOBILE BUSINESS DATA	2012	2013	Percentage variation (%)
	December	December	2012/2013 (local currency)
<i>Unaudited figures</i>			
TELEFÓNICA GERMANY			
Traffic (Million minutes).....	29,519	30,152	2.1%
ARPU (EUR)	13.8	12.7	(7.9)%
Prepay	5.5	5.1	(6.8)%
Contract	21.5	19.4	(9.8)%
Data ARPU (EUR).....	6.2	6.2	0.7%
% non-SMS over data revenues.....	56.7%	66.5%	9.8 p.p.

During 2013, the German mobile market remained steady, with differentiated value propositions across segments, channels and regions and increasing commercial spend.

In 2013 Telefónica Europe's portfolio was restructured and has announced the acquisition of E-Plus by Telefónica Deutschland to form the leading operator in the European market.

The "O2 Blue All-in" tariffs are improving the value of Telefónica's customer base, where the weighting of customers who opt for higher value offers has increased. "O2 Blue All-in" tariffs are mobile data centric tariffs. At the same time, the sale of handsets with LTE technology increased during the year.

As a consequence, the mobile contract customer base grew 1.8% year-on-year, driving mobile accesses to 19.4 million (+0.5% year-on-year). Meanwhile, the contract mix improved 1 percentage point year-on-year to 53%. Smartphone penetration reached 31% at the end of 2013 (+5 percentage points year-on-year), with an encouraging rate of adoption of LTE-enabled handsets. Total net additions amounted 101 thousand in 2013. Mobile contract net adds amounted to 178 thousand in the year. Mobile contract churn reached 1.6% in 2013 (+0.1 p.p. year-on-year). In retail broadband fixed Internet accesses amounted to 2.2 million at the end of December (down 6% year-on-year), despite the broad acceptance of the new "O2 DSL All-in" portfolio and the increasing customer demand for speed.

Czech Republic and Slovakia

ACCESSES BY COUNTRY	2012	2013	Percentage variation (%)
	December	December	2012/2013
<i>Unaudited figures (thousands)</i>			
TELEFÓNICA CZECH REPUBLIC			
Final Clients Accesses.....	7,740.3	7,631.8	(1.4)%
Fixed telephony accesses ⁽¹⁾	1,499.9	1,389.3	(7.4)%
Naked ADSL.....	285.9	324.9	13.7%
VoIP	76.7	86.4	12.7%
Internet and data accesses	1,016.1	985.0	(3.1)%
Narrowband.....	87.6	75.1	(14.3)%
Broadband.....	899.4	882.9	(1.8)%
Other	29.1	27.1	(6.8)%
Mobile accesses	5,082.9	5,101.5	0.4%
Prepay	1,891.1	1,866.1	(1.3)%
Contract ⁽²⁾	3,191.7	3,235.4	1.4%
Pay TV.....	141.4	156.0	10.3%
Wholesale Accesses	159.9	170.4	6.6%
Total Accesses.....	7,900.1	7,802.2	(1.2)%

Note:

(1) Basic Fix Line (including Public Use Telephony) x1, RDSI primary access, Digital Accesses 2/6x30. Includes internal use, VOIP and Naked ADSL.

(2) First quarter of 2013 includes the disconnection of 114 thousand inactive accesses.

ACCESSES BY COUNTRY	2012 December	2013 December	Percentage variation (%) 2012/2013
	<i>Unaudited figures (thousands)</i>		
TELEFÓNICA SLOVAKIA			
Mobile accesses	1,354.2	1,539.5	13.7%
Prepay	694.9	765.6	10.2%
Contract.....	659.3	773.9	17.4%
Total Accesses.....	1,354.2	1,539.5	13.7%

In 2013, Telefónica Czech Republic launched the "Free" and "Vario" tariffs, a new tariff portfolio, which includes unlimited on net calls and SMS and a higher data focus. Furthermore, these tariffs completely eliminate handset subsidy.

Throughout 2013, Telefónica Europe's portfolio was restructured through the sale of operations in the Czech Republic, which was closed in January 2014 after obtaining regulatory approval.

Telefónica Czech Republic and Telefónica Slovakia, s.r.o. ("**Telefónica Slovakia**") participated in auctions of 4G spectrum in the last quarter of 2013, acquiring the frequencies needed to launch its next generation LTE network. As a result, Telefónica Czech Republic acquired 2 blocks in the 800 MHz bandwidth and subsequently acquired 3 blocks in the 1800 MHz bandwidth and 4 blocks in the 2600 MHz bandwidth. The total amount paid for these frequencies was €108 million. Telefónica Slovakia acquired frequencies in the 800 MHz and 1800 MHz bandwidths, in order to permit the company to construct a high-speed and quality LTE network, for €40 million.

Accesses in the Czech Republic declined 1.2% year-on-year in 2013 due to the declines in fixed telephony accesses. The mobile customer base stood at 5.1 million accesses at the end of 2013, up 0.4% year-on-year, driven by the rise in contract customers (1.4% despite the disconnection of 114 thousand inactive contract mobile customers in the first quarter of 2013 in Czech Republic), which now represent 63% of the total (+1 percentage points year-on-year). In Slovakia, the growth in accesses continued, especially in the contract segment due to the success of the tariffs focused on high value customers.

Smartphone penetration grew 11 p.p. year-on-year, to reach 25% at the end of 2013.

The highlights of operating performance in the fixed telephony businesses are as follows:

- Retail broadband accesses amounted to 883 thousand, year-on-year decrease of 1.8% (net annual loss of 16.6 thousand accesses). VDSL continued its positive trend, and 362 thousand clients have already subscribed to this service, representing 39% of the xDSL customer base.
- Pay TV accesses stood at 156 thousand at the end of 2013, a year-on-year increase of +10.3%, evidencing the success of the new O2 TV proposal leveraged on the new IPTV platform.

Telefónica's services and products

Mobile business

Telefónica offers a wide variety of mobile and related services and products to personal and business customers. Although they vary from country to country, Telefónica's principal services and products are as follows:

- *Mobile voice services:* Telefónica's principal service in all of its markets is mobile voice telephony.
- *Value added services:* Customers in most of the markets have access to a range of enhanced mobile calling features, including voice mail, call hold, call waiting, call forwarding and three-way calling.
- *Mobile data and Internet services:* Current data services offered include Short Messaging Services, or SMS, and Multimedia Messaging Services, or MMS, which allow customers to send messages with images, photographs, sound recordings and video recordings. Customers may also

receive selected information, such as news, sports scores and stock quotes. Telefónica also provides mobile broadband connectivity and Internet access. Through mobile Internet access, customers are able to send and receive e-mail, browse the Internet, download games, purchase goods and services in m-commerce transactions and use Telefónica's other data and software services.

- *Wholesale services:* Telefónica has signed network usage agreements with several MVNOs in different countries.
- *Corporate services:* Telefónica provides business solutions, including mobile infrastructure in offices, private networking and portals for corporate customers that provide flexible online billing.
- *Roaming:* Roaming agreements allow Telefónica customers to use their mobile handsets when they are outside their service territories, including on an international basis.
- *Fixed wireless.* Telefónica provides fixed voice telephony services through mobile networks in Brazil, Venezuela, Argentina, Peru, Mexico, Ecuador, El Salvador, Guatemala and Nicaragua.
- *Trunking and paging:* Telefónica provides digital mobile services for closed user groups of clients and paging services in Spain and most of its operations in Latin America.

Fixed line telephony business

The principal services Telefónica offers in its fixed businesses in Europe and Latin America are:

- **Traditional fixed telecommunication services:** Telefónica's principal traditional fixed telecommunication services include PSTN lines; ISDN accesses; public telephone services; local, domestic and international long-distance and fixed-to-mobile communications services; corporate communications services; supplementary value added services (including call waiting, call forwarding, voice and text messaging, advanced voicemail services and conference-call facilities); video telephony; business oriented value-added services; intelligent network services; leasing and sale of handset equipment; and telephony information services.
- **Internet and broadband multimedia services:** the principal Internet and broadband multimedia services include Internet service provider service; portal and network services; retail and wholesale broadband access through ADSL, naked ADSL (broadband connection without the monthly fixed line fee); narrowband switched access to Internet for universal service, and other technologies. Telefónica also offers high-speed Internet services through fiber to the home (FTTH) in certain markets (primarily Spain, Brazil and Chile) and VDSL-based services (primarily Spain, Czech Republic and Germany). Telefónica also offers VoIP services in some markets.
- **Data and business-solutions services:** the data and business-solutions services principally include leased lines; virtual private network, or VPN, services; fiber optics services; the provision of hosting and application, or ASP, service, including web hosting, managed hosting, content delivery and application, and security services; outsourcing and consultancy services, including network management, or CGP; and desktop services and system integration and professional services.
- **Wholesale services for telecommunication operators:** the wholesale services for telecommunication operators principally include domestic interconnection services; international wholesale services; leased lines for other operators' network deployment; and local loop leasing under the unbundled local loop regulation framework). It also includes bit stream services, bit stream naked, wholesale line rental accesses and leased ducts for other operators' fiber deployment.

Digital services

The main highlights in services developed by Telefónica Digital in 2013 are:

- *Video/TV services:* IPTV services (Internet protocol), over-the-top network television services, and cable and satellite TV. In certain markets, advanced pay TV services are offered, such as high-definition TV (HDTV), Multiroom (allowing clients to watch different TV channels in different rooms) and Digital Video Recording (DVR).
- *M2M:* M2M includes both M2M connectivity services and end-to-end products in different countries including in-house developments, as the "smart" M2M solution, which enables "smart" meter communications services.
- *e-Health services or telecare:* these services allow tele-assistance through connectivity services to customers with chronic health issues, and other eHealth services.
- *Financial services and other payment services:* these services allow customers to make transfers, payments and mobile recharges among other transactions through prepay accounts or bank accounts.
- *Security services:* such as the "Latch" applications, which allows consumers to remotely switch their digital services on and off.
- *Cloud computing services:* these include the Instant Servers services, Telefónica's new global public cloud service for corporate clients. This entails high-performance virtual servers that are optimised for mobile and corporate applications (both fixed and mobile).

Sales and Marketing

Telefónica's sales and marketing strategy is aimed toward reinforcing its market position, generating brand awareness, promoting customer growth and achieving customer satisfaction. Telefónica uses a variety of marketing initiatives and programmes, including those that focus on customer value, with in-depth market segmentation; programmes to promote customer loyalty; pricing initiatives aimed toward stimulating usage, including segmented packages and innovative tariff options; and initiatives that are responsive to the latest market trends, including those aimed toward increasing demand for its mobile Internet and mobile broadband offerings. In connection with these and Telefónica's other sales and marketing initiatives, it markets its products through a broad range of channels, including television, radio, billboards, telemarketing, direct mail and Internet advertising. Telefónica also sponsors a variety of local cultural and sporting events in order to enhance its brand recognition.

Competition

The telecommunications industry is competitive and consumers generally have a choice of mobile and fixed line operators from which to select services. Telefónica is a global telecommunications services provider and faces significant competition in most of the markets in which it operates. In Europe, its largest competitor is Vodafone Group Plc and in Latin America, its largest competitor is América Móvil S.A.B. de C.V.. Newer competitors, including handset manufacturers, MVNOs, Internet companies and software providers, are also entering the market and offering integrated communications services.

Telefónica competes in its markets on the basis of the price of its services; the quality and range of features; the added value Telefónica endeavours to offer with its service; additional services associated with those main services; the reliability of its network infrastructure and its technological attributes; and the desirability of its offerings, including bundled offerings of one type of service with another and, in the case of the mobile industry, in most of the markets offerings that include simple and data-centric solutions, moving away from subsidies in some markets and enhancing its offer with the launch of new high speed mobile services in key markets.

To compete effectively with its competitors, Telefónica needs to successfully market its products and services and to anticipate and respond to various competitive factors affecting the relevant markets, such as the introduction of new products and services, different pricing strategies and changes in consumer preferences. See "*Risk Factors – Risks Relating to the Group's Industry – The Group operates in highly*

competitive markets and the industry in which it operates is subject to continuous technological changes, which requires the Group to continuously adapt to such changes and to upgrade its existing networks."

Strategic Partnerships

China United Network Communications Group Co., Ltd. (China Unicom)

Since 2005, Telefónica has had a stake in China Unicom and its predecessor company. On 6 September 2009 Telefónica entered into a strategic alliance agreement with China Unicom, which provides, among other areas for cooperation, joint procurement of infrastructure and client equipment, common development of mobile service platforms, joint provisions of service to multinational customers, roaming, research and development, sharing of best practices and technical, operational and management know-how, joint development of strategic initiatives in the area of network evolution, joint participation in international alliances and exchanges of senior management. In furtherance of this strategic alliance Telefónica entered into a subscription agreement with China Unicom, pursuant to which it increased its voting interest in the share capital of China Unicom to 8.06% and China Unicom obtained 0.87% voting interest in its share capital in October 2009.

Pursuant to the strategic alliance agreement mentioned above, China Unicom has agreed to use its best endeavours to maintain a listing of all the issued ordinary shares of China Unicom on the Hong Kong Stock Exchange. For so long as the strategic alliance agreement with Telefónica is in effect, China Unicom has committed to not (i) offer, issue or sell any significant number of its ordinary shares (including treasury shares), or any securities convertible into or other rights to subscribe for or purchase a significant number of China Unicom's ordinary shares (including treasury shares), to any current major competitor of Telefónica or (ii) make any significant investment, directly or indirectly, in any current competitor of Telefónica. Telefónica made similar commitments to China Unicom.

The strategic alliance agreement between Telefónica and China Unicom was automatically renewed on 6 September 2012 and is subject to automatic annual renewal, subject to either party's right to terminate on six months' notice. Also, the strategic alliance agreement may be terminated by China Unicom if Telefónica's shareholding in China Unicom drops below 5% of its issued share capital as a result of Telefónica, directly or indirectly, selling, contracting to sell or otherwise disposing of shares in China Unicom or if China Unicom's shareholding in Telefónica drops below 0.5% of Telefónica's issued share capital. In addition, the strategic alliance agreement is subject to termination in the event that either party is in default and automatically terminates on a change of control of China Unicom.

On 28 January 2011, China Unicom completed its acquisition of 21,827,499 Telefónica shares.

On 10 June 2012, Telefónica through its 100% owned subsidiary, Telefónica Internacional, S.A.U., and China Unicom through a 100% owned subsidiary, signed an agreement for the acquisition by this last company of 1,073,777,121 shares of China Unicom -Hong Kong- Limited, owned by Telefónica, equivalent to 4.56% of the issued share capital of China Unicom.

On 21 July 2012, the aforementioned agreement was complemented by a Supplemental Agreement which determined the acquisition of the shares at a price of HK\$10.02 per share, for a total amount of HK\$10,759,246,752.42 (approximately €1,142 million). The transaction was completed on 30 July 2012 after obtaining the relevant regulatory authorisations.

As of the date of this Prospectus, Telefónica's shareholding in China Unicom amounts 5.01% of its capital stock. Furthermore, Mr. César Alierta, chairman of Telefónica is a member of the Board of Directors of China Unicom while Mr. Chang Xiaobing, chairman of China Unicom, is a member of the Board of Directors of Telefónica.

Telecom Italia

- Through a series of transactions from 2007 to 2009, Telefónica acquired an indirect holding of 10.49% in the voting shares of Telecom Italia (7.21% of the dividend rights) through its holdings in Telco.
- On 24 September 2013, Telefónica and the remaining shareholders of Telco, (which holds a capital stake of 22.4% of the voting share capital of Telecom Italia) reached an Agreement by virtue of which:

- Telefónica subscribed for, and paid out a capital increase in, Telco, through the contribution of €324 million in cash, receiving in return non-voting shares of Telco. As a result of this capital increase, the interest held by Telefónica in the voting share capital of Telco remained unchanged (46.18%), although its interest in the total share capital of Telco has increased to 66%. The current governance structure at Telco remained unaffected, including the obligation by Telefónica of abstaining from participating or influencing in any decisions which could affect the markets in which both, Telefónica and Telecom Italia are present.
- Subject to receiving any required anti-trust and telecommunications approvals (including in Brazil and Argentina), Telefónica will subscribe for and pay out a second capital increase in Telco, through the contribution of €117 million in cash and will receive in return non-voting shares of Telco. As a result of this second capital increase, the interest of Telefónica in the voting share capital of Telco will remain unchanged (46.18%), although its interest in the total share capital will be then increased to 70%.
- Starting from 1 January 2014, subject to receiving any required anti-trust and telecommunications approvals (including in Brazil and Argentina), Telefónica may convert all or a portion of its non-voting shares in Telco into voting shares in Telco, representing no more than 64.9% of the voting share capital of Telco.
- The Italian shareholders of Telco have granted Telefónica a call option to acquire all of their shares in Telco, whose exercise is subject to receiving any required anti-trust and telecommunications approvals (including in Brazil and Argentina). The call option may be exercised by Telefónica starting from 1 January 2014 while the Shareholders Agreement remains in effect, except (i) between 1 June 2014 and 30 June 2014 and between 15 January 2015 and 15 February 2015, and (ii) during certain periods, if the Italian shareholders of Telco request the demerger of Telco.

As at the date of this Prospectus the approvals that are necessary for the implementation of the transactions contemplated in the Agreement dated 24 September 2013, and subscribed between Telefónica and the remaining shareholders of Telco, have not been obtained.

- On 4 December 2013, the Brazilian Antitrust Regulator, Conselho Administrativo de Defesa Econômica (CADE) announced, the two following decisions:
 1. To approve, with the restrictions mentioned below, the acquisition by Telefónica of the entire participation held by Portugal Telecom, SGPS S.A., and PT Móveis - Serviços de Telecomunicações, SGPS, S.A., (the "**PT Companies**") in Brasilcel N.V., which controlled the Brazilian mobile company, Vivo Participações S.A.

This transaction was approved by ANATEL (the Brazilian Telecommunications Regulation Authority) and the closing (which did not require CADE's prior approval at the time), occurred immediately after ANATEL's approval, on 27 September 2010.

The above mentioned decision has been granted by CADE conditional on:
 - (a) The entry of a new shareholder in Vivo, sharing with Telefónica the control of Vivo in conditions identical to those that were applicable to the PT Companies when they had a participation in Brasilcel N.V., or
 - (b) That Telefónica ceases to have any direct or indirect financial interest in TIM Participações S.A.
 2. To impose on Telefónica a fine of 15 million Brazilian Reais, for having allegedly breached the spirit and the goal of the agreement signed between Telefónica and CADE (as a condition to the approval of Telefónica's original acquisition of an interest in Telecom Italia in 2007), due to the subscription of non-voting shares of Telco on a recent capital increases. This decision also requires Telefónica to divest such non-voting shares of Telco S.p.A.

The timing for the accomplishment of the conditions and obligations imposed by CADE on both decisions was classified by CADE as confidential and reserved information.

- On 13 December 2013, Telefónica announced, in relation to the two decisions adopted by CADE on during its 4 December 2013 session, that the company considers that the remedies imposed were unreasonable, and therefore, is further analysing the possibility of initiating appropriate legal actions.

In line with such course of action, and to reinforce Telefónica's strong commitment with the previous obligations undertaken by Telefónica to remain separate from Telecom Italia's Brazilian businesses Telefónica, highlighted in the aforementioned announcement that Mr. César Alierta Izuel and Mr. Julio Linares López have decided to resign, with immediate effect, from their positions as Directors of Telecom Italia; and Mr. Julio Linares has decided to resign, with immediate effect, from his position in the slate submitted by Telco for the potential re-election of the Board of Directors of Telecom Italia in the Shareholders Meeting of the aforementioned company, called for 20 December 2013.

For the same reasons, Telefónica indicated that, without prejudice to any of the rights recognised in the Telco Shareholder's Agreement, it has decided for the time being not to avail of its right to appoint two Directors in the Board of Directors of Telecom Italia.

Legal Proceedings

Telefónica and its group companies are party to several legal proceedings which are currently in progress in the courts of law and the arbitration bodies of the various countries in which it is present.

Telefónica highlights the following unresolved legal proceedings or those underway in 2013:

Contentious proceedings in connection with the merger between Terra Networks, S.A. and Telefónica

On 26 September 2006, Telefónica was notified of the claim filed by former shareholders of Terra Networks, S.A. (Campoaguas, S.L., Panabeni, S.L. and others) alleging breach of contract in respect of the terms and conditions set forth in the Prospectus of the Initial Public Offering of shares of Terra Networks, S.A. dated 29 October 1999. The court rejected this claim and ordered the plaintiffs to pay court costs by a ruling issued on 21 September 2009. The plaintiffs appealed this ruling on 4 December 2009 and Telefónica was notified of such appeal on 16 June 2010. Telefónica opposed to the appeal on 5 January 2011. On 23 April 2013, Telefónica was notified a ruling of the Madrid Regional Court dismissing in its entirety the appeal filed by the plaintiffs against the first instance ruling handed down in 2009, confirming the rulings of the decision under appeal and ordering appellants to pay court costs. The ruling became firm on 29 May 2013, with no further appeals possible.

Cancellation of the UMTS licence granted to Quam GMBH in Germany

In December 2004, the German Telecommunications Market Regulator revoked the UMTS licence granted in 2000 to Quam GmbH ("**Quam**"), in which Telefónica has a stake. After obtaining a suspension of the revocation order, on 16 January 2006, Quam filed a suit against the order with the German courts. This claim sought two objectives: 1) to overturn the revocation order issued by the German Telecommunications Market Regulator, and 2) if this failed, to be reimbursed for the total or partial payment of the original amount paid for the licence, €8,400 million.

This claim was rejected by the Cologne Administrative Court. Quam appealed the decision before the Supreme Administrative Court of North Rhine-Westphalia, which also rejected its appeal.

Finally, Quam filed a new claim in third instance before the Federal Supreme Court for Administrative Cases, which was not admitted for processing.

Quam appealed this decision on 14 August 2009. On 17 August 2011, after the oral hearing, the Federal Administrative Court rejected Quam's appeal at third instance.

In October 2011, Quam filed a constitutional complaint before the German Federal Constitutional Court (Karlsruhe).

Appeal against the European Commission ruling of 4 July 2007 against Telefónica Spain's broadband pricing policy

On 9 July 2007, Telefónica was notified of the decision issued by the European Commission (the "EC") imposing on Telefónica and Telefónica de España, S.A.U. ("**Telefónica de España**") a fine of approximately €152 million for breach of the former Article 82 of the Treaty Establishing the European Community for not charging equitable prices to whole and retail broadband access services. The court ruled in favour of the EC accusing Telefónica of applying a margin squeeze between the prices it charged competitors to provide regional and national wholesale broadband services and its retail broadband prices using ADSL technology between September 2001 and December 2006.

On 10 September 2007, Telefónica and Telefónica de España filed an appeal to overturn the decision before the General Court of the European Union. The Kingdom of Spain, as an interested party, also lodged an appeal to overturn the decision. Meanwhile, France Telecom and the Spanish Association of Bank Users (AUSBANC) filed requests to intervene, which the General Court admitted.

In October 2007, Telefónica presented a guarantee for an indefinite period of time to secure the principal and interest.

A hearing was held on 23 May 2011, at which Telefónica presented its case. On 29 March 2012, the General Court ruled rejecting the appeal by Telefónica and Telefónica de España, confirming the sanction imposed by the EC. On 13 June 2012, an appeal against this ruling was lodged before the European Court of Justice.

On 26 September 2013, the Attorney General presented its conclusions to the court stating a possible breach of the principle of non-discrimination with respect to the sanction and a defective application of the principle of full jurisdiction by the General Court, requesting the return of the lawsuit to the court of first instance.

Appeal against the decision by Agência Nacional de Telecomunicações (ANATEL) regarding the inclusion of interconnection and network usage revenues in the Fundo de Universalização de Serviços de Telecomunicações ("FUST")

Vivo Group operators, together with other cellular operators, appealed ANATEL's decision of 16 December 2005, to include interconnection and network usage revenues and expenses in the calculation of the amounts payable into the Fund for Universal Access to Telecommunications Services – a fund which pays for the obligations to provide universal service - with retroactive application from 2000. On 13 March 2006, the Brasilia Regional Federal Court granted a precautionary measure which stopped the application of ANATEL's decision. On 6 March 2007, a ruling in favour of the wireless operators was issued, stating that it was not appropriate to include the revenues received by transfer from other operators in the taxable income for the FUST's calculation and rejecting the retroactive application of ANATEL's decision. ANATEL filed an appeal to overturn this decision with Brasilia Regional Federal Court no. 1. This appeal is pending resolution.

At the same time, Telefónica Brazil and Telefónica Empresas, S.A., together with other wireline operators through ABRAFIX (Associação Brasileira de Concessionárias de Serviço Telefônico Fixo Comutado) appealed ANATEL's decision of 16 December 2005, also obtaining the precautionary measures requested. On 21 June 2007, Federal Regional Court no. 1 ruled that it was not appropriate to include the interconnection and network usage revenues and expense in the FUST's taxable income and rejected the retroactive application of ANATEL's decision. ANATEL filed an appeal to overturn this ruling on 29 April 2008 before Brasilia Federal Regional Court no. 1.

No further action has been taken since then. The amount of the claim is quantified at 1% of the interconnection revenues.

Public civil procedure by the São Paulo government against Telefónica Brazil for alleged reiterated malfunctioning in services provided by Telefónica Brazil and request of compensation for damages to the customers affected

This proceeding was filed by the Public Ministry of the State of São Paulo for alleged reiterated malfunctioning in the services provided by Telefónica Brazil, seeking compensation for damages to the customers affected. A general claim is filed by the Public Ministry of the State of São Paulo, for 1,000

million Brazilian reais (approximately €370 million), calculated on the company's revenue base over the last five years.

In April 2010, a ruling in first instance against the Telefónica Group was issued, there will not be a precision of its effects until there is a final ruling, and the total amount of persons affected and party in the procedure is known. At that moment, the amount of the indemnity will be established, ranging between 1,000 million and 60 million Brazilian reais (approximately, between €370 million and €22 million), depending on the number of parties. On 5 May 2010, Telefónica Brazil filed an appeal before the São Paulo Court of Justice, suspending the effect of the ruling. No further action has been taken since then.

Appeal against the ruling by the European Commission dated 23 January 2013 to sanction Telefónica for the infringement of Article 101 of the Treaty on the functioning of the European Union

On 19 January 2011, the EC initiated formal proceedings to investigate whether Telefónica and Portugal Telecom SGPS, S.A. ("**Portugal Telecom**") had infringed on European Union anti-trust laws with respect to a clause contained in the sale and purchase agreement of Portugal Telecom's ownership interest in Brasilcel, N.V., a joint venture in which both were venturers and owner of Brazilian company Vivo.

On 23 January 2013, the EC passed a ruling on the formal proceedings. The ruling imposed a fine on Telefónica of €67 million, as the EC ruled that Telefónica and Portugal Telecom committed an infraction as stipulated in Article 101 of the Treaty on the Functioning of the European Union for having entered into the agreement set forth in Clause Nine of the sale and purchase agreement of Portugal Telecom's ownership interest of Brasilcel, N.V.

On 9 April 2013, Telefónica filed an appeal for annulment of this ruling with the European Union General Court. On 6 August 2013, the General Court notified Telefónica of the response issued by the European Commission, in which the EC reaffirmed the main arguments of its ruling and, specially, that Clause Nine is a competition restriction. On 30 September 2013, Telefónica filed its reply. On 18 December 2013, the European Commission filed its appeal.

Tax proceedings

Tax Inspections and tax relating lawsuits

In December 2012, the National Court of Justice issued a ruling on the tax inspection for the years 2001 to 2004, accepting the tax losses incurred by the Group in relation to the transfer of certain interests in Tele Sudeste Celular Participações S.A., Telefónica Móviles México, S.A. de C.V., and Lycos, Inc. as tax deductible and rejecting the other allegations. The Company filed an appeal with the Supreme Court on 28 December 2012.

Also in 2012, the tax inspections for all taxes for the years 2005 to 2007 were completed, with the Company signing consent forms for an income tax payment of €135 million and non-consent forms for the items which the Company contests. The tax assessment for which a non-consent form was signed did not require payment of any tax because it only proposed a reduction in unused tax loss carry forwards. An appeal was filed with the Large Taxpayers Central Office of the Spanish State Tax Agency (*la Delegación Central de Grandes Contribuyentes*) requesting this tax assessment be reversed, although no decision on the appeal has been issued as of the date of this Prospectus.

In July 2013, new inspections of various companies in the 24/90 Tax Group, of which Telefónica is the parent, were initiated. The taxes and periods subject to review are corporate income tax for the years 2008 to 2011, VAT, tax withholdings and payments on account in respect of personal income tax, tax on investment income, property tax and non-resident income tax for the second half of 2009 and the years 2010 and 2011. It is not expected that these inspections in progress will result in the need to recognise any additional liabilities in the Telefónica Group's consolidated financial statements.

Telefónica Brasil has a number of appeals underway regarding the ICMS (similar to VAT levied on telecommunications services). There is a dispute with the Brazilian tax authority over which services should be subject to settlement of this tax, the most significant being the demands of the collection of the ICMS on complementary or auxiliary services to base telecommunications service, such as value added services or the lease of modems. As at the date of this Prospectus, all the related procedures are being

contested in all instances (administrative and judicial). The aggregate amount of these assessments, updated to take into account interests, fines and other items, is approximately €2,038 million. No provisions have been set aside for these matters, as the risk of them giving rise to liabilities is not probable. Telefónica Brasil has obtained independent expert reports supporting its position, i.e. that the aforesaid services are not subject to ICMS.

Regarding the Group's main tax litigation in Peru, on 20 March 2013, notification was received of a first instance court decision upholding Telefónica Peru's arguments in three of the five objections filed by the authorities and appealed against in higher courts. Both the tax authorities and the company have appealed against the decision in the court of second instance.

The assessment originally raised by the tax authorities amounted to €124 million comprising the tax charge, excluding interest and penalties. At the date of authorisation for issue of this Prospectus, €80 million had been paid out (€42 million of which was for penalty and interest paid in 2013). The Company has also obtained suspensive measures in the amount of €340 million within the process of appeals to the Ordinary Court. The Group and its legal advisors believe they have legal grounds to defend the Company's interests in the appeal that is currently underway.

At the 2013 year end, based on the final outcome of these assessments, and on the lawsuits, and inspections in progress it has not been deemed necessary to recognise additional liabilities in the Telefónica Group's consolidated financial statements.

Major Shareholders

At 31 December 2013 the outstanding share capital of Telefónica was 4,551,024,586 shares, each with a nominal value of €1.00 per share. All outstanding shares have the same rights.

To the extent that shares are represented by account entries, Telefónica does not keep a shareholder registry therefore it is not possible to ascertain the precise shareholding structure. Based on the information available to Telefónica there is no individual or corporation that directly or indirectly through one or more intermediaries exercises or may exercise any type of control over the company. Nevertheless, certain shareholders have holdings which are considered material.

According to information provided to Telefónica or to the CNMV, beneficial owners of 3% or more of the company's voting stock were as follows:

Name of Beneficial Owner	Number of Shares	Percent
Banco Bilbao Vizcaya Argentaria, S.A. ⁽¹⁾	313,707,133	6.893%
Caja de Ahorros y Pensiones de Barcelona ("la caixa") ⁽²⁾	246,977,147	5.427%
Blackrock, Inc. ⁽³⁾	177,257,649	3.895%

⁽¹⁾ Based on the information provided by Banco Bilbao Vizcaya Argentaria, S.A. as at 31 December 2013 for the 2013 Annual Report on Corporate Governance.

⁽²⁾ Based on information provided by Caja de Ahorros y Pensiones de Barcelona, "la Caixa" as at 31 December 2013 for the 2013 Annual Report on Corporate Governance. The 5.411% indirect shareholding in Telefónica is owned by CaixaBank, S.A.

⁽³⁾ According to notification sent to the CNMV, dated 4 February 2010.

At 31 December 2013, 184,990,503 of Telefónica's shares were held in the form of ADSs by 800 holders of record, including Cede & Co., the nominee of the Depository Trust Company. The number of ADSs outstanding was 216,751,480 at 31 December 2012.

Management of Telefónica

During 2013, the Board of Directors met 14 times. As of the date of this Prospectus, the Board of Directors had met three times during 2014 and as of such date, the directors, their respective positions on the Board and the year they were appointed to such positions were as follows:

Name	Date of Birth	Age	First Appointed	Current Term Ends
Chairman				
Mr. César Alierta Izuel ⁽¹⁾	05/05/1945	68	1997	2017
Vice-chairmen				
Mr. Isidro Fainé Casas ⁽¹⁾⁽²⁾	10/07/1942	71	1994	2016
Mr. José María Abril Pérez ⁽¹⁾⁽³⁾⁽⁷⁾	19/03/1952	62	2007	2018
Mr. Julio Linares López ⁽⁵⁾⁽⁷⁾⁽⁸⁾	26/12/1945	68	2005	2016
Members (vocales)				
Mr. José María Álvarez - Pallete López ⁽¹⁾	12/12/1963	50	2006	2017
Mr. José Fernando de Almansa Moreno - Barreda ⁽⁵⁾⁽⁶⁾⁽⁸⁾	04/10/1948	65	2003	2018
Ms. Eva Castillo Sanz ⁽⁶⁾⁽⁸⁾⁽¹⁰⁾	23/11/1962	51	2008	2018
Mr. Carlos Colomer Casellas ⁽¹⁾⁽⁴⁾⁽⁷⁾⁽⁹⁾⁽¹⁰⁾	05/04/1944	69	2001	2016
Mr. Peter Erskine ⁽¹⁾⁽⁷⁾⁽⁸⁾⁽⁹⁾	10/11/1951	62	2006	2016
Mr. Santiago Fernández Valbuena	22/04/1958	55	2012	2018
Mr. Alfonso Ferrari Herrero ⁽¹⁾⁽⁴⁾⁽⁵⁾⁽⁶⁾⁽⁸⁾⁽⁹⁾⁽¹⁰⁾	28/02/1942	72	2001	2016
Mr. Luiz Fernando Furlán	29/07/1946	67	2008	2018
Mr. Gonzalo Hinojosa Fernández de Angulo ⁽¹⁾⁽⁴⁾⁽⁵⁾⁽⁶⁾⁽⁸⁾⁽⁹⁾⁽¹⁰⁾	10/07/1945	68	2002	2017
Mr. Pablo Isla Álvarez de Tejera ⁽⁶⁾⁽⁹⁾	22/01/1964	50	2002	2017
Mr. Antonio Massanell Lavilla ⁽²⁾⁽⁴⁾⁽⁵⁾⁽⁷⁾⁽¹⁰⁾	24/09/1954	59	1995	2016
Mr. Ignacio Moreno Martínez ⁽³⁾⁽⁴⁾⁽⁶⁾⁽¹⁰⁾	30/07/1957	56	2011	2017
Mr. Francisco Javier de Paz Mancho ⁽¹⁾⁽⁵⁾⁽⁶⁾⁽¹⁰⁾	24/07/1958	55	2007	2018
Mr. Chang Xiaobing ⁽¹¹⁾	27/03/1957	56	2011	2016

- (1) Member of the Executive Commission of the Board of Directors.
(2) Nominated by Caja de Ahorros y Pensiones de Barcelona ("La Caixa").
(3) Nominated by Banco Bilbao Vizcaya Argentaria, S.A. ("BBVA").
(4) Member of the Audit and Control Committee of the Board of Directors.
(5) Member of the Institutional Affairs Committee.
(6) Member of the Regulation Committee.
(7) Member of the Innovation Committee.
(8) Member of the Strategy Committee.
(9) Member of the Nominating, Compensation and Corporate Governance Committee.
(10) Member of the Service Quality and Customer Service Committee.
(11) Nominated by China Unicom (Hong Kong) Limited.

The principal activities inside and outside the Group of each of the directors of Telefónica are as follows:

Name	Principal activities inside the Group	Principal Activities outside the Group
César Alierta Izuel	Executive Chairman of Telefónica, S.A.	Director of China Unicom (Hong Kong) Limited Director of International Consolidated Airlines Group (AIG)
Isidro Fainé Casas	Vice Chairman of Telefónica, S.A.	Chairman of Caja de Ahorros y Pensiones de Barcelona ("la Caixa") Chairman of CaixaBank, S.A. Chairman of Criteria Caixaholding, S.A. Vice Chairman 1º of Abertis Infraestructuras, S.A. Chairman of Confederación Española de Cajas de Ahorros Vice Chairman 1º of Repsol, S.A. Director of Banco Português de Investimento, SA (BPI) Vice Chairman of Sociedad General de Aguas de Barcelona, S.A. (AGBAR) Vice-Chairman of European Savings Bank Group (ESG) and World Savings Bank Institute (WSBI) Non-executive Director of the Bank of East Asia
Ignacio Moreno Martínez	Director of Telefónica, S.A.	Chief Executive Officer of N+1 Private Equity Non-executive president of Metrovacesa, S.A.
Julio Linares López	Vice Chairman of Telefónica, S.A.	
José María Abril Pérez	Vice Chairman of Telefónica, S.A.	
Fernando de Almansa Moreno Barreda	Director of Telefónica, S.A.	Substitute Director of Grupo Financiero BBVA Bancomer, S.A. de C.V.
	Director of Telefónica Brasil, S.A. Director of Telefónica Móviles México, S.A.	Substitute Director of BBVA Bancomer, S.A.

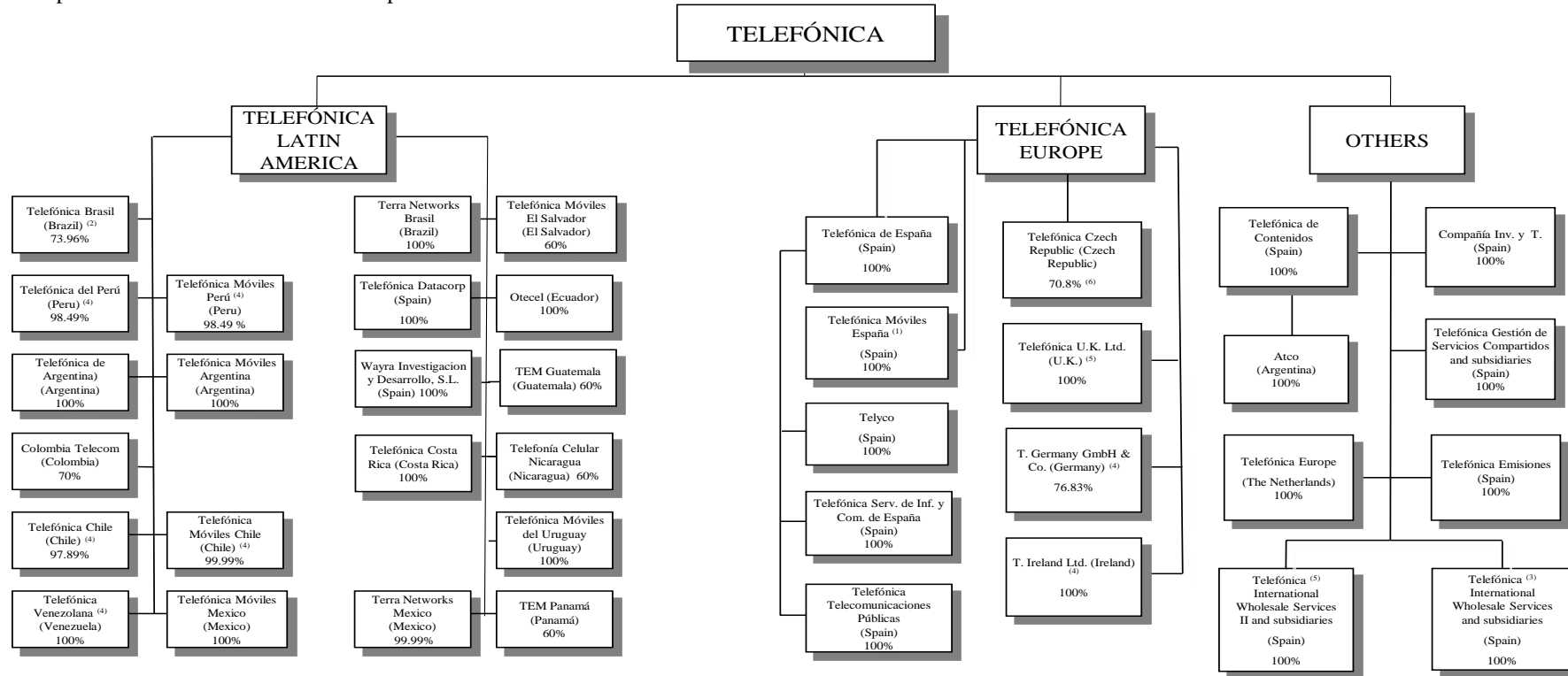
Name	Principal activities inside the Group	Principal Activities outside the Group
	de C.V.	
José María Álvarez Pallete López	COO (Chief Operating Officer) of Telefónica, S.A.	
Santiago Fernández Valbuena	Director of Telefónica, S.A. Chief Strategy Officer (CSO) Vice Chairman of Telefónica Brasil, S.A.	Director of Ferrovial, S.A.
Eva Castillo Sanz	Director of Telefónica, S.A. Chairman of Supervisory Board of Telefónica Deutschland Holding A.G.	Director of Bankia, S.A.
Carlos Colomer Casellas	Director of Telefónica, S.A.	Chairman of Inversiones Mobiliarias Urquiola, S.A., SICAV Chairman of Ahorro Bursátil, S.A. SICAV Director of MDF Family Partners Chairman of Haugron Holdings S.L. Director of Abertis Infraestructuras, S.A.
Peter Erskine	Director of Telefónica, S.A.	Chairman of the Advisory Board of the Henley Management Centre Chairman of Ladbrokes, Plc
Alfonso Ferrari Herrero	Director of Telefónica, S.A. Substitute Director of Telefónica Chile, S.A. Director of Telefónica del Perú, S.A.A.	
Luiz Fernando Furlán	Director of Telefónica, S.A. Director of Telefónica Brasil, S.A.	Chairman of Amazonas Sustainability Foundation Member of the Board of Directors of BRF, S.A. Director of AGCO Corporation Member of the Consultative Board of Abertis Infraestructuras S.A. Member of the Advisory/Consultative Board of Panasonic (Japan), McLarty & Associates (USA) and Wal-Mart Stores Inc. (USA)
Gonzalo Hinojosa Fernández de Angulo	Director of Telefónica, S.A. Director of Telefónica del Perú, S.A.A.	
Pablo Isla Alvarez de Tejera	Director of Telefónica, S.A.	Chairman and CEO of Inditex, S.A.
Antonio Massanell Lavilla	Director of Telefónica, S.A.	General Manager of CaixaBank, S.A. Director of Sociedad de Gestión de Activos Inmobiliarios procedentes de la Reestructuración Bancaria (SAREB). Chairman of Barcelona Digital Centre Tecnologic (formerly Fundación Barcelona Digital) Non-executive Director of CECA BANK Director of Bousorama S.A. Director of Mediterranea Beach & Golf Community, S.A
Francisco Javier de Paz Mancho	Director of Telefónica, S.A. Director of Telefónica de Argentina, S.A. Director of Telefónica Brasil, S.A.	Member of the Executive Committee of the Chambers Board (Consejo Superior de Cámaras)
Chang Xiaobing	Director of Telefónica, S.A.	Chairman of China United Network Communications Group Company Limited Chairman of China United Network Communications Limited Executive Director, Chairman and Chief Executive Officer of China Unicom (Hong Kong) Limited Chairman of China United Network Communications Corporation Limited

Conflicts of Interest

As of the date of this Prospectus, there were no current or potential conflicts of interest in relation to members of the Board of Directors between any duties owed to Telefónica and their private interests and other duties.

Organisational Structure

The following chart shows the organisational structure of the principal subsidiaries of the Telefónica Group at 31 December 2013, including their jurisdictions of incorporation and Telefónica's ownership interest:



- (1) Ownership in Telefónica Móviles España, S.A.U. is held directly by Telefónica, S.A.
- (2) 91.76% representing voting interest.
- (3) Ownership in Telefónica International Wholesale Services, S.L. is held 92.51% by Telefónica, S.A. and 7.49% by Telefónica Datacorp, S.A.U.
- (4) Companies held indirectly.
- (5) Ownership in TIWS II is held directly by Telefónica, S.A.
- (6) 72.1% including treasury shares.

TAXATION

The following is a general description of certain tax considerations relating to the Securities. It does not purport to be a complete analysis of all tax considerations relating to the Securities whether in those countries or elsewhere. Prospective purchasers of Securities should consult their own tax advisors as to the consequences under the tax laws of the country of which they are resident for tax purposes and the tax laws of The Netherlands and the Kingdom and Spain of acquiring, holding and disposing of Securities and receiving payments of interest, principal and/or other amounts under the Securities. This summary is based upon the law as in effect on the date of this Prospectus and is subject to any change in law that may take effect after such date.

Also investors should note that the appointment by an investor in Securities, or any person through which an investor holds Securities, of a custodian, collection agent or similar person in relation to such Securities in any jurisdiction may have tax implications. Investors should consult their own tax advisors in relation to the tax consequences for them of any such appointment

Dutch Tax

For the purpose of the paragraph "Taxes on Income and Capital Gains" below it is assumed that:

- (i) a holder of Securities, being an individual or a non-resident entity, does not have nor will have a substantial interest (aanmerkelijk belang), or - in the case of such holder being an entity - a deemed substantial interest, in the Issuer and that no connected person (verbonden persoon) to the holder has or will have a substantial interest in the Issuer;
- (ii) a holder of Securities is not a pension fund or otherwise not a taxpayer or exempt for tax purposes; and
- (iii) a holder of Securities which is an entity is not a resident of Aruba, Curaçao or Sint Maarten.

Generally speaking, an individual has a substantial interest in a company if (a) such individual, either alone or together with his partner, directly or indirectly has, or is deemed to have or (b) certain relatives of such individual or his partner directly or indirectly have or are deemed to have (i) the ownership of, a right to acquire the ownership of, or certain rights over, shares representing 5 per cent or more of either the total issued and outstanding capital of such company or the issued and outstanding capital of any class of shares of such company, or (ii) the ownership of, or certain rights over, profit participating certificates (winstbewijzen) that relate to 5 per cent or more of either the annual profit or the liquidation proceeds of such company

Generally speaking, a non-resident entity has a substantial interest in a company if such entity, directly or indirectly has (i) the ownership of, a right to acquire the ownership of, or certain rights over, shares representing 5 per cent or more of either the total issued and outstanding capital of such company or the issued and outstanding capital of any class of shares of such company, or (ii) the ownership of, or certain rights over, profit participating certificates (winstbewijzen) that relate to 5 per cent or more of either the annual profit or the liquidation proceeds of such company. An entity has a deemed substantial interest in a company if such entity has disposed of or is deemed to have disposed of all or part of a substantial interest on a non-recognition basis.

For the purpose of this summary, the term "entity" means a corporation as well as any other person that is taxable as a corporation for Dutch corporate tax purposes.

Where this summary refers to a holder of Securities, an individual holding Securities or an entity holding Securities, such reference is restricted to an individual or entity holding legal title to as well as an economic interest in the Securities or otherwise being regarded as owning Securities for Dutch tax purposes. It is noted that for purposes of Dutch income, corporate, gift and inheritance tax, assets legally owned by a third party such as a trustee, foundation or similar entity, may be treated as assets owned by the (deemed) settlor, grantor or similar originator or the beneficiaries in proportion to their interest in such arrangement.

Where the summary refers to "The Netherlands" or "Dutch" it refers only to the European part of the Kingdom of The Netherlands.

Investors should consult their professional advisers on the tax consequences of their acquiring, holding and disposing of Securities.

1. WITHHOLDING TAX

All payments made by the Issuer of interest and principal under the Securities can be made free of withholding or deduction of any taxes of whatever nature imposed, levied, withheld or assessed by The Netherlands or any political subdivision or taxing authority thereof or therein.

2. TAXES ON INCOME AND CAPITAL GAINS

Residents

Resident entities

An entity holding Securities which is, or is deemed to be, resident in The Netherlands for corporate tax purposes and which is not tax exempt, will generally be subject to corporate tax in respect of income or a capital gain derived from the Securities at the prevailing statutory rates.

Resident individuals

An individual holding Securities who is, is deemed to be, or has elected to be treated as, resident in The Netherlands for income tax purposes will be subject to income tax in respect of income or a capital gain derived from the Securities at rates up to 52 per cent if:

- (i) the income or capital gain is attributable to an enterprise from which the holder derives profits (other than as a shareholder); or
- (ii) the income or capital gain qualifies as income from miscellaneous activities (*belastbaar resultaat uit overige werkzaamheden*) as defined in the Income Tax Act (*Wet inkomstenbelasting 2001*), including, without limitation, activities that exceed normal, active asset management (*normaal, actief vermogensbeheer*).

If neither condition (i) nor (ii) applies, an individual holding Securities will be subject to income tax on the basis of a deemed return, regardless of any actual income or capital gain derived from the Securities. The deemed return amounts 4% of the fair market value of the individual's net assets exceeding a certain threshold as at the beginning of the relevant fiscal year (including the Securities). Subject to application of certain allowances, the deemed return will be taxed at a rate of 30 per cent.

Non-residents

A holder which is not, is not deemed to be, and - in case the holder is an individual - has not elected to be treated as, resident in The Netherlands for the relevant tax purposes will not be subject to taxation on income or a capital gain derived from the Securities unless:

- (i) the income or capital gain is attributable to an enterprise or part thereof which is either effectively managed in The Netherlands or carried on through a permanent establishment (*vaste inrichting*) or a permanent representative (*vaste vertegenwoordiger*) in The Netherlands and the holder of Securities derives profits from such enterprise (other than by way of securities); or
- (ii) the holder is an individual and the income or capital gain qualifies as income from miscellaneous activities (*belastbaar resultaat uit overige werkzaamheden*) in The Netherlands as defined in the Income Tax Act (*Wet inkomstenbelasting 2001*), including, without limitation, activities that exceed normal, active asset management (*normaal, actief vermogensbeheer*).

3. GIFT AND INHERITANCE TAXES

Dutch gift or inheritance taxes will not be levied on the occasion of the transfer of Securities by way of gift by, or on the death of, a holder of Securities, unless:

- (i) such holder is, or is deemed to be, resident in The Netherlands for the purpose of the relevant provisions; or

- (ii) the transfer is construed as an inheritance or gift made by, or on behalf of, a person who, at the time of the gift or death, is or is deemed to be resident in The Netherlands for the purpose of the relevant provisions.

4. **VALUE ADDED TAX**

There is no Dutch value added tax payable by a holder of Securities in respect of payments in consideration for the issue of the Securities or in respect of the payment of interest or principal under the Securities, or the transfer of Securities.

5. **OTHER TAXES AND DUTIES**

There is no Dutch registration tax, stamp duty or any other similar tax or duty payable in The Netherlands by a holder of Securities in respect of or in connection with the execution, delivery and/or enforcement by legal proceedings (including any foreign judgement in the courts of The Netherlands) of the Securities or the performance of the Issuer's obligations under the Securities.

6. **RESIDENCE**

A holder of Securities will not be and will not be deemed to be resident in The Netherlands for tax purposes and, subject to the exceptions set out above, will not otherwise become subject to Dutch taxation, by reason only of acquiring, holding or disposing of Securities or the execution, performance, delivery and/or enforcement of Securities.

Spanish Tax

Applicable law for Spanish tax purposes

The Guarantor believes that Additional Provision Two of Law 13/1985 of May 25 shall apply to the Securities according to its Section 6, provided that the Securities are issued by a company which is (i) tax resident in the European Union, (ii) whose voting rights are completely held directly by a Spanish listed entity whose shares are regularly traded on an organised market and (iii) regardless of whether its corporate purpose is wider than the exclusive activity of issue of preferred shares and debt instruments (in this regard, this criterion has been confirmed by the Spanish General Tax Directorate in its binding ruling dated 26 December 2013 (no. V3670-13), which overrides the binding ruling dated 11 November 2013 (no. V3313-13), where it points out that the requirements of exclusive corporate purpose and exclusive activity contained in Sections 1 and 5 of Additional Provision Two of Law 13/1985 of May 25 are not applicable to issuers that are subsidiaries of non-financial entities).

The Guarantor will comply with the reporting obligations set out in Section 3 of Additional Provision Two of Law 13/1985 in respect of Holders who are taxpayers of the Spanish Individual Income Tax or taxpayers of the Spanish Corporation Tax, as well as taxpayers of the Spanish Non-resident Income Tax ("**NRIT**") who hold the Securities through a permanent establishment located in the Spanish territory.

Payments made by the Guarantor

In the opinion of the Guarantor, any payments of principal and interest that do not remunerate the use of funds in Spain made by the Guarantor under the Guarantee should not be subject to taxation in Spain.

However, payments of interest made under the Guarantee to the beneficial owners of the income arising from the Securities (each of them, a "**Holder**", and collectively the "**Holders**") may be subject to Spanish taxation and, hence, to Spanish withholding tax at the then applicable rate (as at the date of this Prospectus, 21%) to the extent it remunerates the use of funds in Spain. According to Spanish tax legislation, "interest" includes payment of coupons and income deriving from the transfer, redemption or reimbursement of the Securities, on the basis of the positive difference between the amounts obtained in the transfer, redemption or reimbursement of the Securities and their tax basis.

For Non-Spanish tax resident Holders not acting with respect to the Securities through a permanent establishment in Spain, such income should be exempt from Spanish tax in accordance with Additional Provision Two of Law 13/1985 of May 25 and, therefore, no Spanish withholding may be due.

The application of the abovementioned exemption from Spanish withholding tax is conditional:

- (i) while the Securities are represented by Global Securities and the Global Securities are deposited with a common depository for Euroclear and/or Clearstream, Luxembourg, upon the submission by the Fiscal Agent, in a timely manner, to the Guarantor with a certificate containing certain information relating to the Securities in accordance with section 44 of the Royal Decree 1065/2007 as amended by Royal Decree 1145/2011, as detailed under the Fiscal Agency Agreement, or
- (ii) while the Securities are represented by Definitive Securities, upon the submission by the Holder to the Guarantor prior to the corresponding payment of interest under the Guarantee of a valid certificate of tax residence, duly issued by the tax authorities of the country of tax residence of the Holder, each certificate generally being valid for a period of one year beginning on the date of the issuance.

The Issuer, the Guarantor and the Fiscal Agent have arranged certain procedures to facilitate the collection of information concerning the Securities so that before the close of business on the Business Day (as defined in the Conditions of the relevant Securities) immediately preceding the date on which any payment of interest, principal or of any amounts in respect of the early redemption of the Securities (each, a "**Payment Date**") is due, the Guarantor must receive from the Fiscal Agent a certificate containing certain information relating to the Securities as prescribed under section 44 paragraph 5 of the Royal Decree 1065/2007. If, despite these procedures, the relevant information is not received by the Guarantor on each Payment Date, the Guarantor will withhold tax at the then-applicable rate (currently 21%) from any payment of interest in respect of the relevant Security. Neither the Issuer nor the Guarantor will pay any additional amounts with respect to any such withholding.

Notwithstanding the above, if, before the tenth calendar day of the month following the month in which the relevant income is paid, the Fiscal Agent provides the required information, the Guarantor will reimburse the amounts withheld.

If Additional Provision Two of Law 13/1985 of May 25 was not deemed applicable to the Securities, the relevant Additional Amounts will be payable according to Condition 8(a) (*Taxation – Additional Amounts*) of the Terms and Conditions of the 6 Year Non-Call Securities and of the Terms and Conditions of the 10 Year Non-Call Securities, respectively.

Holders not acting with respect to the Securities through a permanent establishment in Spain and entitled to exemption from NRIT, but the payment to whom was not exempt from Spanish withholding tax due to the failure to deliver by the Holder or the Fiscal Agent (as the case may be) of a valid certificate of tax residence of the Holder or certain information relating to the Securities (as the case may be) in a timely manner may apply directly to the Spanish tax authorities for any refund to which they may be entitled. Holders are advised to consult their own tax advisors regarding their eligibility to claim a refund from the Spanish tax authorities and the procedures to be followed in such circumstances.

Furthermore, Non-Spanish tax resident Holders not acting with respect to the Securities through a permanent establishment in Spain may take the position that payments of interest received from the Guarantor under the Guarantee should be characterised as an indemnity under Spanish law and, hence, should have been made free of withholding or deduction on account of any Spanish tax. In such a case, these Holders should apply directly to the Spanish tax authorities for any refund to which they may be entitled.

In connection with Spanish tax resident Holders and Non-Spanish tax resident Holders acting with respect to the Securities through a permanent establishment in Spain, income deriving from the Securities and the Guarantee is subject to tax in Spain. Payments made under the Guarantee which correspond to payments of interest under the Securities may be subject to withholding on account of Spanish taxes.

EU Savings Tax Directive

Under EC Council Directive 2003/48/EC on the taxation of savings income, each Member State is required to provide to the tax authorities of another Member State details of payments of interest or other similar income paid by a person within its jurisdiction to, or collected by such a person for, an individual resident or certain limited types of entity established in that other Member State; however, for a transitional period, Austria and Luxembourg may instead apply a withholding system in relation to such payments, deducting tax at a rate of 35%. The transitional period is to terminate at the end of the first full

fiscal year following agreement by certain non-EU countries to the exchange of information relating to such payments. Luxembourg has announced that it will no longer apply the withholding tax system as from 1 January 2015 and will provide details of payments of interest (or similar income) as from this date.

A number of non-EU countries, and certain dependent or associated territories of certain Member States, have adopted similar measures (either provision of information or transitional withholding) in relation to payments made by a person within its jurisdiction to, or collected by such a person for, an individual resident or certain limited types of entity established in a Member State. In addition, the Member States have entered into provision of information or transitional withholding arrangements with certain of those dependent or associated territories in relation to payments made by a person in a Member State to, or collected by such a person for, an individual resident or certain limited types of entity established in one of those territories.

The European Commission has proposed certain amendments to the Directive, which may, if implemented, amend or broaden the scope of the requirements described above. Investors who are in any doubt as to their position should consult their professional advisors.

The proposed financial transactions tax ("FTT")

The European Commission recently published a proposal for a Directive for a common financial transaction tax in Belgium, Germany, Estonia, Greece, Spain, France, Italy, Austria, Portugal, Slovenia and Slovakia (the "**participating Member States**"). The tax could enter into force towards the middle of 2014.

The proposed FTT has very broad scope and it would apply to a wide range of financial transactions.

Under current proposals the FTT could apply in certain circumstances to persons both within and outside of the participating Member States. Generally, it would apply to certain dealings in the Securities where at least one party is a financial institution, and at least one party is established in a participating Member State.

In relation to many secondary market transactions in bonds, the FTT would be charged at a minimum rate of 0.1% on each financial institution which is party to the transaction.

A person transacting with a financial institution which fails to account for FTT would be jointly and severally liable for that tax.

The FTT proposal remains subject to negotiation between the participating Member States and is the subject of legal challenge. It may therefore be altered prior to any implementation. Additional Member States may decide to participate. Prospective holders of the Securities are strongly advised to seek their own professional advice in relation to the FTT.

SUBSCRIPTION AND SALE

Banco Bilbao Vizcaya Argentaria, S.A., Banco Santander, S.A., Barclays Bank PLC, CaixaBank, S.A., Goldman Sachs International, Mizuho International plc and The Royal Bank of Scotland plc (the "**Joint Bookrunners**") have, in a subscription agreement dated 25 March 2014 (the "**Subscription Agreement**") and made between the Issuer, the Guarantor and the Joint Bookrunners upon the terms and subject to the conditions contained therein, jointly and severally agreed to subscribe for the Securities. The Joint Bookrunners are entitled in certain circumstances to be released and discharged from their obligations under the Subscription Agreement prior to the closing of the issue of the Securities.

United Kingdom

Each Joint Bookrunner has further represented, warranted and undertaken that:

- (a) it has only communicated or caused to be communicated and will only communicate or cause to be communicated an invitation or inducement to engage in investment activity (within the meaning of Section 21 of the FSMA) received by it in connection with the issue or sale of the Securities in circumstances in which Section 21(1) of the FSMA does not apply to the Issuer or the Guarantor; and
- (b) it has complied and will comply with all applicable provisions of the FSMA with respect to anything done by it in relation to the Securities in, from or otherwise involving the United Kingdom.

United States of America

The Securities have not been and will not be registered under the Securities Act and may not be offered or sold within the United States or to, or for the account or benefit of, U.S. persons except in certain transactions exempt from the registration requirements of the Securities Act. Terms used in this paragraph have the meanings given to them by Regulation S.

The Securities are subject to U.S. tax law requirements and may not be offered, sold or delivered within the United States or its possessions or to a United States person, except in certain transactions permitted by U.S. tax regulations. Terms used in this paragraph have the meanings given to them by the United States Internal Revenue Code and regulations thereunder.

Each Joint Bookrunner has agreed that, except as permitted by the Subscription Agreement, it will not offer, sell or deliver the Securities, (a) as part of their distribution at any time or (b) otherwise, until 40 days after the later of the commencement of the offering and the issue date of the Securities, within the United States or to, or for the account or benefit of, U.S. persons, and that it will have sent to each dealer to which it sells Securities during the distribution compliance period a confirmation or other notice setting forth the restrictions on offers and sales of the Securities within the United States or to, or for the account or benefit of, U.S. persons.

In addition, until 40 days after commencement of the offering, an offer or sale of Securities within the United States by a dealer (whether or not participating in the offering) may violate the registration requirements of the Securities Act.

The Netherlands

Each Joint Bookrunner has represented and agreed that the Securities are not, and may not be, offered to the public in The Netherlands other than to persons or entities which are qualified investors as defined in the Dutch Financial Supervision Act (*Wet op het financieel toezicht*).

The Kingdom of Spain

Neither the Securities nor this Prospectus have been approved or registered in the administrative registries of the Spanish Securities Markets Commission (*Comisión Nacional del Mercado de Valores*). Accordingly, the Securities may not be offered, sold or distributed, nor may any subsequent resale of the Securities be carried out in Spain, except in circumstances which do not constitute a public offer of securities in Spain within the meaning of Article 30-bis of the Spanish Securities Market Law

(Ley 24/1988, de 28 de julio, del Mercado de Valores), Royal Decree 1310/2005 of 4 November (Real Decreto 1310/2005 de 4 de noviembre), and supplemental rules enacted thereunder.

General

Each Joint Bookrunner has represented, warranted and agreed that, to the best of its knowledge and belief, it has complied and will comply with all applicable laws and regulations in each country or jurisdiction in which it purchases, offers, sells or delivers Securities or possesses, distributes or publishes this Prospectus or any other offering material relating to the Securities. Persons into whose hands this Prospectus comes are required by the Issuer, the Guarantor and the Joint Bookrunners to comply with all applicable laws and regulations in each country or jurisdiction in which they purchase, offer, sell or deliver Securities or possess, distribute or publish this Prospectus or any other offering material relating to the Securities, in all cases at their own expense.

GENERAL INFORMATION

Authorisation

1. The creation and issue of the Securities has been authorised by a resolution of the Board of Managing Directors of the Issuer dated 14 March 2014. The giving of the Guarantee of the Securities has been authorised by a resolution of the Delegated Committee of the Board of Directors of the Guarantor dated 14 March 2014, by a resolution of the Board of Directors of the Guarantor dated 31 May 2013, and by a resolution of the shareholders acting through the General Shareholders' Meeting of the Guarantor dated 31 May 2013.

Legal and Arbitration Proceedings

2. Save as described in "Risk Factors - Telefónica and Telefónica Group companies are party to lawsuits, tax claims, antitrust and other legal proceedings" on page 15 of this Prospectus, and under "Description of the Guarantor - Legal Proceedings" on pages 107 – 109 of this Prospectus, there are no governmental, legal or arbitration proceedings, (including any such proceedings which are pending or threatened, of which the Issuer or the Guarantor is aware), which may have, or have had during the 12 months prior to the date of this Prospectus, a significant effect on the financial position or profitability of the Issuer or the Guarantor and its subsidiaries.

Significant/Material Change

3. Since 31 December 2013 there has been no material adverse change in the prospects, and no significant change in the financial or trading position, of the Issuer or its subsidiary save for: i) on 7 February 2014, the Issuer made an early repayment for €801 million of its syndicated loan (Tranche D1) dated 2 March 2012 (originally scheduled to mature on 14 December 2015). Since 31 December 2013 there has been no material adverse change in the prospects, and no significant change in the financial or trading position, of the Guarantor and the Group, save for: i) on 31 January 2014, Telefónica Emisiones, S.A.U. ("Telefónica Emisiones") redeemed £296 million (equivalent to €355 million) of its notes, issued on 28 December 2006, the notes were guaranteed by the Guarantor; ii) on 3 February 2014, Telefónica Emisiones redeemed €2,000 million of its notes, issued on 3 February 2009, the notes were guaranteed by the Guarantor; iii) on 7 February 2014, Telefónica Emisiones redeemed €1,500 million of its notes, issued on 7 February 2007, the notes were guaranteed by the Guarantor; iv) on 7 February 2014, the Guarantor made an early repayment for €923 million of its syndicated loan (Tranche D2) dated 2 March 2012 (originally scheduled to mature on 14 December 2015); v) on 10 February 2014, O2 Telefónica Deutschland Finanzierungs, GmbH issued seven-year notes in an aggregate principal amount of €500 million maturing on 10 February 2021, and with an annual interest rate of 2.375%, these notes are guaranteed by Telefónica Deutschland; vi) on 18 February 2014, the Guarantor signed a €3,000 million syndicated revolving credit facility maturing on 18 February 2019. This agreement entered into effect on 25 February 2014 cancelling the €3,000 million syndicated credit facility signed on 28 July 2010 (originally scheduled to mature in 2015); and vii) on 12 March 2014, Telefónica Emisiones launched an issuance of two-year floating rate notes in aggregate principal amount of €200 million. These notes are guaranteed by the Guarantor. The settlement and closing date is scheduled for execution on 26 March 2014.

Auditors

4. The consolidated financial statements of the Guarantor have been audited without qualification for the years ended 31 December 2013 and 2012 by Ernst & Young, S.L. with its registered address at Plaza Pablo Ruiz Picasso, 1, 28020, Madrid, Spain, registered in the ROAC under number S0530.

The unconsolidated financial statements of the Issuer have been audited without qualification for the years ended 31 December 2013 and 2012 by Ernst & Young Accountants LLP with its registered address at Antonio Vivaldistraat 150, 1083 HP, Amsterdam, The Netherlands, registered in The Netherlands in the Chamber of Commerce, Rotterdam with registration number 24432944.

Documents on Display

5. Copies of the following documents may be inspected during normal business hours at the offices of the Fiscal Agent and at the registered/head office of the Issuer and the Guarantor for 12 months from the date of this Prospectus:
 - (a) the articles of association of the Issuer (together with English translations thereof);
 - (b) the constitutional documents of the Guarantor (together with English translations thereof);
 - (c) drafts (subject to modification) of the Fiscal Agency Agreement, the Deed of Covenant and the Deed of Guarantee;
 - (d) the audited unconsolidated financial statements of the Issuer for the years ended 31 December 2013 and 2012; and
 - (e) the audited consolidated financial statements of the Guarantor for the years ended 31 December 2013 and 2012.

Each of the translations into English of the Issuer's articles of association and the constitutive documents of the Guarantor is a direct and accurate translation of the corresponding document. In the event of any discrepancy between the English language version and the original language version, the original language version shall prevail.

Yield

6. From (and including) the Issue Date to (but excluding) the First Reset Date, the yield on the 6 Year Non-Call Securities will be 5.000% per annum. From (and including) the Issue Date to (but excluding) the First Reset Date, the yield on the 10 Year Non-Call Securities will be 5.875% per annum. In each case, the yield is calculated at the Issue Date on the basis of the Issue Price. It is not an indication of future yield.

Legend Concerning US Persons

7. The Securities and any Coupons and Talons appertaining thereto will bear a legend to the following effect: "Any United States person who holds this obligation will be subject to limitations under the United States income tax laws, including the limitations provided in Sections 165(j) and 1287(a) of the Internal Revenue Code."

Listing

8. It is expected that the listing of the Securities on the Official List of the FCA and the admission of the Securities to trading on the Regulated Market of the London Stock Exchange will take place on or about 31 March 2014, subject to the issue of each Temporary Global Security.

Fees

9. The estimated costs and expenses in relation to admission to trading are £8,000.

ISIN and Common Code

10. The Securities have been accepted for clearance through Euroclear and Clearstream, Luxembourg. The ISIN of the 6 Year Non-Call Securities is XS1050460739 and the common code is 105046073. The ISIN of the 10 Year Non-Call Securities is XS1050461034 and the common code is 105046103.

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