



Telefónica Europe B.V.

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

**EUR 850,000,000 Undated 5 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 850,000,000 Undated 5 Year Non-Call Deeply Subordinated Guaranteed Fixed Rate Reset 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 Securities (the "**Conditions**"), the Securities will bear interest on their principal amount (i) at a fixed rate of 4.200% per annum from (and including) the Issue Date to (but excluding) the First Reset Date (as defined in the Conditions) payable annually in arrear on 4 December in each year, with the first Interest Payment Date on 4 December 2015; and (ii) from (and including) the First Reset Date (as defined in the Conditions), at the applicable 5 year Swap Rate in respect of the Reset Period, plus: (A) in respect of the period commencing on the First Reset Date to (but excluding) 4 December 2024, 3.806 per cent. per annum; (B) in respect of the period commencing on 4 December 2024 to (but excluding) 4 December 2039, 4.056 per cent. per annum; and (C) from and including 4 December 2039, 4.806 per cent. per annum, all as determined by the Agent Bank, payable annually in arrear on 4 December in each year (each, an Interest Payment Date as defined in the Conditions), commencing on 4 December 2020.

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 Securities — Optional Interest Deferral*". 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). The Issuer may pay outstanding Arrears of Interest, in whole or in part, at any time in accordance with the Conditions. 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 Deferred Interest Payment was first deferred, all as more particularly described in "*Terms and Conditions of the Securities — Optional Interest Deferral — Mandatory Settlement of Arrears of Interest*".

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) or upon any Interest Payment Date (as defined in the Conditions) thereafter, at their principal amount together with any accrued and unpaid interest up to (but excluding) the Redemption Date (as defined in the Conditions) 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 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 Securities — Redemption and Purchase*".

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 Securities — Status and Subordination of the Securities and Coupons*". 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) 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 Securities - Guarantee, Status and Subordination of the Guarantee*".

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 Securities - Taxation*".

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, as amended (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 and 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 the Temporary Global Security will be exchangeable for interests in the permanent global security (the "**Permanent Global Security**") and together with the Temporary Global Security, the "**Global Securities**") in the circumstances set out in the Temporary Global Security. The Permanent Global Security will be exchangeable for definitive Securities (the "**Definitive Securities**") in the circumstances set out in the 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

**Barclays
J.P. Morgan**

**BNP PARIBAS
Société Générale Corporate & Investment Banking
UniCredit Bank**

28 November 2014

CONTENTS

	Page
IMPORTANT NOTICES.....	1
RISK FACTORS.....	6
OVERVIEW OF THE SECURITIES.....	28
INFORMATION INCORPORATED BY REFERENCE.....	34
TERMS AND CONDITIONS OF THE SECURITIES.....	36
SUMMARY OF PROVISIONS RELATING TO THE SECURITIES IN GLOBAL FORM.....	53
FORM OF GUARANTEE.....	55
USE OF PROCEEDS.....	60
DESCRIPTION OF THE ISSUER.....	61
DESCRIPTION OF THE GUARANTOR.....	62
TAXATION.....	96
SUBSCRIPTION AND SALE.....	101
GENERAL INFORMATION.....	103

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.
- **"IPTV"** (Internet Protocol Television): distribution system for TV or video using DSL connection through IP
- **"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 prepay 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.
- **"Bundles"** refers to offering several commercial products, such as Fixed Telephony, Broad Band, TV and Mobile products, selling them as one combined product.
- **"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.
- **"CapEx"** means capital expenditure in tangible and intangible assets.
- **"CDMA"** means Code Division Multiple Access, which is a channel access method used by radio communication technology.
- **"Churn"** is the percentage of average customers disconnected over a period of time.
- **"Cloud computing"** refers to a platform to share resources, software and information over a network (typically the Internet) to computers and other devices.
- **"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.
- "**FTR (Fixed Termination Rate)**" means an established rate for the fixed network associated to call termination in a competitor's network.
- "**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 additions**" 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 an enhanced 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 (an organisation that provides service for accessing, using or participating on the Internet).
- "**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 additions**" 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**" refers to the delivery of audio, video and other media services over the Internet, without a multiple system operator being involved in the distribution of the content.
- "**P2P SMS**" refers to SMS messages exchanged between two mobile subscribers.

- "**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 minutes of traffic used by Telefónica's customers over a given period, both outbound and inbound.
- "**UMTS**" means Universal Mobile Telecommunications System.
- "**VDSL**" or "**VHDSL**": means Very high bit-rate Digital Subscriber Line.
- "**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 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 in which recovery may be delayed or weakened resulting from imbalances that still require adjustment. According to the European Economic and Financial Affairs Council, the European economy is expected to grow 1.2% in 2014, mainly as a consequence of weak private consumption growth in certain economies. In this region, the Telefónica

Group generated 23.7% of its revenues in Spain, 13.6% in the UK and 9.2% in Germany in the first nine months of 2014.

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, given the negative impact that a higher than expected depreciation in their currencies could have on cash flows from both countries. Although the economic outlook for the entire region suggests that growth rates will remain between 1%-2% in the short term, in the medium term these could increase up to 3% being supported by solid domestic demand fundamentals (*source*: IMF). 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". As at 30 September 2014, Telefónica Latin America and Telefónica Brazil represented 28.7% and 22.1% of the Telefónica Group's revenues respectively. On this point, approximately 12.7% 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. It is also significant that, despite clear improvements in Brazil, the uncertainty surrounding the political situation, fiscal policy stimuli and a relatively high inflation rate could result in a rating downgrade that, depending on the extent of such downgrade, could result in strong exchange-rate volatility due to an outflow of investments, especially in relation to fixed-income.

The following are highlighted among the factors included in the concept of "country risk":

- 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 both fiscal and external deficits 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) regular and selective 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, despite its recent stability, continues to be under the threat of 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 margin 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 Defence 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 30 September 2014, 74% of the Group's net debt (in nominal terms) had its interest rates fixed over a year, while 24% 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 30 September 2014: (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 €55 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 €43 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 €30 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 30 September 2014, including derivative instruments in place.

At 30 September 2014, 21.2% of Telefónica Group's operating income before depreciation and amortisation (OIBDA) was concentrated in Brazil, 28.9% in Latin America and 10.4% in the UK. 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 30 September 2014, gross financial debt scheduled to mature in 2014 amounted to €2,953 million (which includes the net position of derivative financial instruments and certain current payables), and gross financial debt scheduled to mature in 2015 amounted to €5,012 million. Despite having covered gross debt maturities of 2014 and 2015 by available cash and lines of credit at 30 September 2014, 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.

In 2013 the Group issued bonds mainly (i) in euro totalling €3,250 million with an average coupon of 3.69%; (ii) in dollars totalling \$2,000 million with an average coupon of 3.709%; and (iii) in Swiss Francs

totalling CHF225 million with an annual coupon of 2.595%. The Group also issued hybrid instruments in euro totalling €1,750 million with an average coupon of 6.902%, and in pounds sterling totalling £600 million with an annual coupon of 6.75%. In 2014 the Group issued bonds mainly in the European market with a maturity of eight years totalling €1,250 million with an annual coupon of 2.242%, and bonds with a fifteen year maturity totalling €800 million with an annual coupon of 2.932%. In addition, the Group issued hybrid instruments in 2014 totalling €1,750 million with an average coupon of 5.50%.

Although the Group maintains liquidity coverage for more than 2 years, 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, 8% of which, at 30 September 2014, initially mature prior to 30 September 2015.

In addition, the impact of the sovereign debt crisis and the rating downgrades in certain Eurozone 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.

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, regulated wholesale services over 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 authorities 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 amendments by the EU Parliament to the Commission's draft on the "Digital Single Market" (the "DSM") package of measures are currently being discussed by the European Council. The DSM includes 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.

Germany's global system for mobile communications (GSM) licences, in the 900 MHz/1800 MHz bands, expire at the end of 2016. In this regard, on 20 October 2014, the German regulator started a public consultation on draft decisions about the order for, and choice of, spectrum allocation proceedings and on the auction conditions of these bands, together with the allocation of spectrum in the 1500 MHz and 700 MHz bands. The German regulator has announced that it intends to publish respective final decisions of the President's Chamber in the fourth quarter of 2014 and to commence the spectrum allocation procedure at the end of 2014. The resolution of this spectrum procedure is envisaged in the second quarter of 2015.

In parallel, on 4 July 2014, the German regulator announced that the new merged entity resulting from the acquisition of E-Plus Mobilfunk GmbH Co KG ("**E-Plus**") by Telefónica Deutschland Holding AG ("**Telefónica Deutschland**") is obliged to return frequencies of 900MHz and 1800MHz until 31 December 2015. As at the date of this Prospectus, this merged entity does not have an assignment beyond the year 2016. The German regulator also announced that it will examine, in the context of an overall consideration of the market taking into account the future frequency equipment in the ranges of 900MHz and 1800MHz, if any action is required in relation to the merger-related frequency spectrum, particularly in the area of 2GHz (frequency distribution analysis).

On 4 August 2014, Telefónica Deutschland filed a claim against this decision of the German regulator, which is pending resolution. In addition to this, the merged entity is obliged to offer 2x10 MHz at each spectrum of 2,600 MHz, as well as 2,100 MHz spectrum to a new mobile network operator or to the operator with whom Telefónica Deutschland has signed the network access agreement within the framework of the conditions imposed by the European Commission (Drillisch Group). This offer however is only to remain open for a specified period of time. This and other actions may be fulfilled subsequently to the closing of the acquisition of E-Plus by Telefónica Deutschland. On 29 August 2014, the European Commission gave final clearance to the acquisition of E-Plus.

In Spain, on 1 January 2015 the frequencies in the 800 MHz spectrum auctioned prior to such date and which are part of the "Digital Dividend" (spectrum allocation process from television operators to electronic communications services), shall be delivered to the relevant mobile operators.

For its part, in the UK a significant increase in the annual licence fees charged for the use of the spectrum in 900 and 1800 MHz band has been proposed by the regulator (Ofcom), and a decision is under discussion, the outcome of which remains uncertain. In addition, on 5 November 2014, the UK Government published a consultation document entitled "Tackling partial not-spots in mobile coverage", in which it has been suggested that the UK Government might seek to amend spectrum licences to impose a duty to require either national roaming, the provision of wholesale services to MVNOs, or a coverage obligation. This consultation is under discussion.

In Europe, the main allocation criteria for the 700 MHz band of "Digital Dividend II" (the second spectrum allocation process from television operators to electronic communications services) will be defined in the coming years. This could involve facing new cash outflow ahead of schedule (it is expected that the spectrum will be available between 2018 and 2021).

In Latin America, spectrum auctions are expected to 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:

- Ecuador: The government has shown its agreement to provide operators with additional spectrum.
- Venezuela: The auction in the AWS (Advanced Wireless Services) band (1710-2170 MHz frequencies) and in the 2.5 GHz band has continued after a period in which it was suspended and it is expected to be resolved during the final quarter of 2014.
- With regard to Argentina, on 4 July 2014 the Secretary of Communication opened the auction of high speed wireless licenses for AWS and 700MHz bands through Resolution 38/2014. The period to present offers expired on 18 September 2014. Telefónica de Argentina applied correctly, fulfilling all the procedural requirements and was accepted as a "Pre-qualified Offeror" by Resolution 65/2014. The auction took place on 31 October 2014 and Telefónica de Argentina was awarded in the Tenth Block (1710-1720/2110-2120 and 703-713/758-768 MHz frequencies), assuming a commitment to provide services in those frequencies for 18 months.

- Peru: Peru's government announced plans to auction the 700 MHz spectrum band that it is expected to take place in the first quarter of 2015 (possibly 3 blocks of 2x15 MHz).
- Costa Rica: Costa Rica's government announced plans to auction spectrum in 1800 MHz and AWS bands during 2015.
- Mexico: It is expected that the government of Mexico will publish its spectrum plan defining the spectrum bands to be auctioned at the end of 2015.

With regard to El Salvador, the auction of one block in the 1900 MHz band and another in the AWS band has been suspended.

On the other hand, in Colombia, the ICT Ministry issued a Resolution on 27 March 2014 to renew 850 MHz/1900 MHz licences for 10 additional years. The issue of the reversion of assets will be discussed during the liquidation of the concession contract, taking into consideration the terms of the contract and the Constitutional Court's review of Law 422 of 1998, which established the reversion only of the radio-electric frequencies. 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, in light of the constitutional reform resulting from the "Pact for Mexico" political initiative, it is expected that a publicly owned wholesale network, which will offer wholesale services in the 700 MHz band, will be created. As at the date of this Prospectus, the funding and marketing model of this project have not yet been determined.

With regard to the acquisition of spectrums in Brazil, on 30 September 2014, Telefónica obtained a block of 2x10 MHz in the 700 MHz band amounting to 1,927,964,770 Brazilian Reals (approximately €619 million) for the provision 4G mobile services.

Telefónica Móviles Chile, S.A. was awarded a spectrum on the 700 MHz (2x10 MHz) band in March 2014. A third party provider has opposed this allocation of spectrum on the basis that it would exceed the limit spectrum of 60 MHz established by a judgment of the Supreme Court of 27 January 2009. This cap was established for the AWS competition held in 2009, but not for subsequent competitions (2600 MHz and 700 MHz). As at the date of this Prospectus, this has not been resolved, however this is not expected to affect the award for 2014 due to the demand being experienced in relation to the 2600 MHz spectrum, which is complementary to the band awarded to Telefónica Móviles Chile, S.A.

On 27 March 2014, Telefónica executed a renewal contract in Panama, paying \$108 million, granting the use of spectrum for 20 additional years from February 5, 2016 to February 4, 2036. 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 (radio frequencies in the 1.9/2.1GHz band used for the provision of 3G mobile services) in order to relocate the blocks of radiofrequencies. 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.

During 2012, in Brazil, Telefónica was awarded a block of the "X" band (radiofrequencies 2500 MHz (20+20 MHz), used for the provision 4G mobile services, and includes the 450 MHz band in certain states). In the spectrum auction, Telefónica Brazil had to compensate the former licensees 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 has been legally contested. In Venezuela, the concession agreement between Telefónica Venezuela 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 consolidated investment in spectrum acquisitions and renewals in the first half of 2014 amounted to €189 million, mainly allocated in Colombia and Central America.

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 on 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" were reduced on 1 July 2014 (in the wholesale market, the price of data by 67%, the price of call by 50%, and the price of texts: 0%; and in the retail market, the price of data by 55%, the price of outgoing voice call by 21%, the price of incoming voice call by 28%; and the price of outgoing texts by 25%), 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 also took 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 (the European Parliament has brought forward the "end of roaming" to 15 December 2015 – "Roaming Like at Home") as well as international charges.

The decreases in wholesale mobile network termination rates (MTR) in Europe are also noteworthy. In the UK, wholesale mobile network termination rates have been reduced to 0.845 ppm (pence/minute) from 1 April 2014 (representing a 0.3% reduction compared to the previous rates). In a consultation document published in June 2014, Ofcom has proposed a further reduction to 0.545 ppm, from 1 April 2015. The consultation period ended on 13 August 2014.

In Germany, on 3 September 2014, the German regulator ("**BNetzA**") adopted a proposal to reduce MTRs. The new prices will gradually decrease to 0.0172 euro/minute from 1 December 2014, and in a second step, from 0.0172 euro/minute to 0.0166 euro/minute from 1 December 2015 until the end of November 2016. The European Commission has requested that the German regulator withdraw or amend its latest decision on mobile termination rates, in force as at the date of this Prospectus. 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.

In Spain, the National Regulatory Competition Authority (*Comisión Nacional de Mercados y Competencia*) has adopted a final decision on the third round analysis of the wholesale market for fixed call termination. From 1 November 2014, a symmetric fixed termination rate (FTR) of 0.0817 euro cents/minute will apply, based on pure bottom up long run incremental costs (BU-LRIC), meaning that billing must be entirely conducted on a "per second" basis, without a peak/off-peak differentiation. The decision therefore eliminates the asymmetry in FTRs that existed since 2006 when alternative network operators were allowed to charge up to 30% above Telefónica's per minute local FTR. It also brings forth an important reduction in average termination prices for Telefónica (-80%) in comparison to the former applicable tariffs.

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 Federal Institute of Telecommunications (*El Instituto Federal de Telecomunicaciones*) ("**IFT**") has declared "America Movil Group" a preponderant operator in the telecommunications market and, as a result, on 26 March 2014, it introduced, among other, special regulations on asymmetric interconnection rates. In that sense, the Federal Telecommunications and Broadcasting law, effective from 13 August 2014, imposed several obligations on the preponderant operator, which are quite exhaustive and, in principle, potentially significantly beneficial to Telefónica's competitive position, particularly as regard to the measures imposed on preponderant operators (to the extent they nominally retain such qualification). Independently of the above, Telefónica México filed an administrative appeal against the 2011 resolutions of the Federal Telecommunications Commission of México (Cofetel) 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. Recently, IFT determined the mobile termination rates for 2012 and Telefónica Mexico filed an injunction against this rate. Once these appeals have been concluded, the rates applied may be further reduced retroactively. As of the date of this Prospectus, IFT has not approved the termination rates for 2013 or 2014 for Telefónica México.

In Brazil, at the end of 2012, the National Telecommunications Agency (*Agência Nacional de Telecomunicações*) ("ANATEL") launched the "*Plano Geral de Metas de Competição*" ("PGMC") regarding fixed-mobile rate adjustment reductions until 2015 and amending the previous reduction conditions (75% of the 2013 rate in 2014 and 50% of the 2013 rate in 2015). In order to complement reductions and approach the cost of the services according to a financial cost model, on 7 July 2014 ANATEL published reference values for MTR taking effect from 2016 to 2019. Such reductions are approximately 44% per year. Furthermore, there are several legislative initiatives that aim to abolish the basic fee of fixed-telephony service. "Price protection" practices (reimbursement of differences in prices of a product to customers if this falls within a relative short period of time) may also have a negative impact in Telefónica Brasil, in both economic and image terms.

In Chile, a new tariff decree has been issued to set fixed-line termination charges for the 2014-2019 period. The new tariff entered into effect on 8 May 2014 and applies a reduction of 37% in prices against those charged for the period prior to such tariff. A tariff decree has been issued 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 75.41% with respect to the previous rates. After a review by the general comptroller (*Contraloría General*) an additional 2.8% reduction was approved on 27 May 2014. 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. Under this Act, in January 2014, an Organic Fair Price Law was issued, which caps the revenue of related enterprises at 30% of their operating costs. In relation to MTRs with the national operator of reference (*Compañía Anónima Nacional Teléfonos de Venezuela*) ("CANTV"), these have been reduced by 6% compared to the previous rates.

In Peru, the previously applicable for mobile termination rate was reduced by 31.43% 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, (contracting capacity template regardless of traffic actually carried), the reduction will be 10.9% for 2014 and 12.3% for 2015. In relation to fix networks (for extended local networks) the reduction will be 50% for 2014 and 100% for 2015. Additionally, the Colombian regulator has adopted a proposal for consultation on new MTRs, using a pure LRIC cost model which implies a reduction of 85% in 2016.

Regulation of universal services:

Further to its formal obligation to review the scope of the Universal Service (the set of basic electronic communication services whose provision is guaranteed to any user requesting it, regardless of its location, with a specified quality at an affordable price), the European Commission is expected to undertake a public consultation in the months following the date of this Prospectus, which may include both the potential inclusion of broadband in its scope and a possible reduction of some of the current universal service obligations. 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 last *Plano Geral de Metas de Universalização* ("PGMU") was published in Brazil on 30 June 2011 and applies to the 2011 - 2015 period. This sets goals for public phones, low cost fixed-lines and coverage density in rural and poor areas with 2.5GHz/450 MHz technology or older technologies. Also according to the new PGMU, the backhaul used to meet the commitments of universalisation was characterised as a reversible asset.

PGMU is currently under a public consultation process to review the goals of universalisation. The Agency's proposal focuses on reducing the distance between public telephones and backhaul's expansion.

Regulation of fiber networks:

It is expected that in the first half of 2015 the Spanish National Regulatory Competition Authority (*Comisión Nacional de los Mercados y la Competencia*) will set regulatory obligations for broadband market regulation in Spain. New regulation will apply to NGN (Next Generation Networks) for, at least,

three years. This could increase Telefónica's regulatory obligations in Spain and the ability of other operators to compete in such market.

Regulations on privacy:

In Europe, a new Data Protection Regulation is in the European legislative process which, at the date of this Prospectus, is not expected to end before the fourth quarter of 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.

In Brazil, triggered by the approval of Civil Rights Framework for Internet Governance, which provides certain generic rules about data protection, it is believed that in the near future new regulations addressing data protection will be launched. These could lead to a greater number of obligations for operators in relation to the collection of personal data of telecom services users, and further restrictions on the treatment of such 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, national regulators are seeking to 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 DSM Regulation proposed by the European Commission which, among other things, deals with the principle of network neutrality. The regulation of network neutrality could impact directly on possible future business models of Telefónica and may affect the network management or differentiation of characteristics and quality of Internet access service.

Telefónica has presence in countries where net neutrality has already been ruled, such as Chile, Colombia, Peru and more recently Brazil, but this remains a live issue and with varying degree of development in the other countries. In Germany, the Economy Minister withdrew a draft law which it published on 20 June 2013, to regulate net neutrality, especially with regard to blocking and discrimination of content and Internet services. It plans to submit a new draft after the EU has settled on a position on net neutrality within the DSM approach, which might occur at the end of 2014 or in early 2015. In addition, one German region (Bundesland of Thuringia) has passed a new law (which applies only in such region) with the aim that broadcasting and tele media may not be blocked, limited or treated differently from other data traffic.

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 assistance and services 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.

The 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, in a timely manner, to constant technological changes, changes in consumer preferences that are taking place in the industry, as well as economic, political and social situations.

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 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 30 September 2014, the Telefónica Group depends on 7 handset suppliers and 9 network infrastructure suppliers, which together accounted for 80% of the awarded contracts. 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, 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 with a negative impact of €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 Securities.

Under Spanish Law 10/2014 and Royal Decree 1065/2007, 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 issuer (that is, the Guarantor with respect to any payments of interest under the Guarantee) 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 issuer (that is, the Guarantor with respect to any payments of interest under the Guarantee), before the close of business on the Business Day (as defined in the Terms and Conditions of the 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 (as at the date of this Prospectus, 21 per cent.) from any payment of interest in respect of

the 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 (that is, the Guarantor with respect to any payments of interest under the Guarantee). 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*").

U.S. Foreign Account Tax Compliance Withholding

The U.S. "Foreign Account Tax Compliance Act" (or "**FATCA**") imposes a new reporting regime and, potentially, a 30% withholding tax with respect to (i) certain payments from sources within the United States, (ii) "foreign passthru payments" made to certain non-U.S. financial institutions that do not comply with this new reporting regime, and (iii) payments to certain investors that do not provide identification information with respect to interests issued by a participating non-U.S. financial institution. Whilst the Securities are in global form and held within the clearing systems, in all but the most remote circumstances, it is not expected that FATCA will affect the amount of any payments received by the clearing systems. However, FATCA may affect payments made to custodians or intermediaries in the subsequent payment chain leading to the ultimate investor if any such custodian or intermediary generally is unable to receive payments free of FATCA withholding. It also may affect payments to any ultimate investor that is a financial institution that is not entitled to receive payments free of withholding under FATCA, or an ultimate investor that fails to provide its broker (or other custodian or intermediary from which it receives payments) with any information, forms, other documentation or consents that may be necessary for the payments to be made free of FATCA withholding. Investors should choose the custodians or intermediaries with care (to ensure each is compliant with FATCA or other laws or agreements related to FATCA) and provide each custodian or intermediary with any information, forms, other documentation or consents that may be necessary for such custodian or intermediary to make a payment free of FATCA withholding. The Issuer or the Guarantor, as the case may be, has no responsibility for any amount thereafter transmitted through the clearing systems and custodians or intermediaries. Furthermore, if an amount in respect of U.S. withholding tax were to be deducted or withheld from any payments on the Securities, the Issuer would not, pursuant to the conditions of the Securities, be required to pay additional amounts as a result of the deduction or withholding of such tax

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 Securities and Coupons*) of the Conditions of the Securities. By virtue of such subordination, payments to a Holder of Securities will, in the event of an Issuer Winding-up (as described in the 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 (as defined below), 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 Securities.

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 the 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 Securities).

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 Securities). The 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 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 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 Securities. 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 Securities. 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 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 Securities.

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 the Securities contain provisions for calling meetings of Holders of the Securities to consider matters affecting their interests generally. These provisions permit defined majorities to bind all Holders of the Securities including Holders of Securities 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 the 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 the 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 the 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 Council of the European Union formally adopted a Council Directive amending the Directive on 24 March 2014 (the "**Amending Directive**"). The Amending Directive broadens the scope of the requirements described in the first paragraph above. Member States have until 1 January 2016 to adopt the national legislation necessary to comply with the Amending Directive and are required to apply these new requirements from 1 January 2017. The changes made under the Amending Directive include extending the scope of the Directive to payments made to, or collected for, certain other entities and legal arrangements. They also broaden the definition of "interest payment" to cover income that is equivalent to interest.

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.

Investors who are in any doubt as to their position should consult their professional advisers.

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 SECURITIES

This overview must be read as an introduction to this Prospectus and any decision to invest in the 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 Securities" below have the same meanings in this overview.

Issuer:	Telefónica Europe B.V.
Guarantor:	Telefónica, S.A.
Description of Securities:	€850,000,000 Undated 5 Year Non-Call Deeply Subordinated Guaranteed Fixed Rate Reset Securities (the " Securities "), to be issued by the Issuer on 4 December 2014 (the " Issue Date ").
Joint Bookrunners:	Barclays Bank PLC, BNP Paribas, J.P. Morgan Securities plc, Société Générale and UniCredit Bank AG.
Fiscal Agent:	The Bank of New York Mellon, London Branch.
Issue Price:	100% of the principal amount of the Securities.
Issue Date:	4 December 2014.
Maturity Date:	Undated.
Interest:	<p>The 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 4.200 per cent. per annum, payable annually in arrear on each Interest Payment Date, commencing on 4 December 2015; and(ii) from (and including) the First Reset Date, at the applicable 5 year Swap Rate in respect of the Reset Period plus:<ul style="list-style-type: none">(A) in respect of the period commencing on the First Reset Date to (but excluding) 4 December 2024, 3.806 per cent. per annum;(B) in respect of the period commencing on 4 December 2024 to (but excluding) 4 December 2039, 4.056 per cent. per annum¹; and(C) from and including 4 December 2039, 4.806 per cent. per annum², <p>all as determined by the Agent Bank, payable annually in arrear on each Interest Payment Date, commencing on 4 December 2020, 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 Securities.</p>

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

² Additional step-up of 75 basis points 25 years after the Issue Date

Interest Payment Dates:	Interest payments in respect of the Securities will be payable annually in arrear on 4 December in each year, commencing on 4 December 2015.
Status of the Securities:	The 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 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 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 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 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 Securities, as more particularly described in " <i>Terms and Conditions of the Securities – Optional Interest Deferral</i> ". Non-payment of interest so deferred shall not constitute a default by the Issuer or Guarantor under the 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:	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 Optional Deferred Interest Settlement Date informing them of its election so to satisfy such Arrears of Interest (or part thereof) and specifying the Optional Deferred Interest Settlement Date. See Condition 5(b) (<i>Optional Settlement of Arrears of Interest</i>) of the Terms and Conditions of the 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 Deferred Interest Payment 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 Interest Period; and
- (iii) the date on which the 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 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 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,

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

Events of Default

There are no events of default in respect of the 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 Security, in respect of such 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 Security and all interest then accrued but unpaid on such 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 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 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 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 Securities.

Form:

The 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 Securities will be issued in the denomination of €100,000.

Governing Law:

The Fiscal Agency Agreement, the 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 Securities and Coupons – Subordination of the Securities*) relating to the subordination of the 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 Securities.

Replacement Intention: The Guarantor intends (without thereby assuming any obligation) at any time that it or the Issuer will redeem or repurchase the Securities only to the extent that the aggregate principal amount of the 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 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 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 Securities originally issued in any period of 12 consecutive months or (b) 25 per cent. of the aggregate principal amount of the Securities originally issued in any period of 10 consecutive years, or
- (iii) the 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 4 December 2039.

Rating: The 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 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. 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 "*Subscription and Sale*".

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 Securities, expected to amount to €847,025,000 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:	XS1148359356.
Common Code:	114835935.

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 audited unconsolidated 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 audited unconsolidated 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 unaudited unconsolidated interim financial statements of Telefónica Europe B.V. for the six months ended 30 June 2014 are available on http://www.rns-pdf.londonstockexchange.com/rns/9840P_-2014-8-26.pdf; the audited 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; the audited 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; the unaudited but reviewed condensed consolidated interim financial statements of Telefónica, S.A. for the six months ended 30 June 2014 are available on http://www.rns-pdf.londonstockexchange.com/rns/8388N_-2014-7-31.pdf; and the interim consolidated management statement January-September 2014 of Telefónica, S.A. is available on http://www.rns-pdf.londonstockexchange.com/rns/8040W_-2014-11-12.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, and the financial statements and notes to the financial statements for the six months ended 30 June 2014, 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, the financial statements, the notes to financial statements and the Auditor's review report for the six months ended 30 June 2014, and the interim management statement January-September 2014, for the Guarantor.

Telefónica Europe B.V.

Financial Statements Year ended 31 December 2013

Balance sheet.....	Page 6
Statement of income and expenses.....	Page 7
Notes to Financial Statements.....	Pages 8 to 25
Auditors Report.....	Pages 28 and 29 of the PDF

Financial Statements Year ended 31 December 2012

Balance sheet.....	Page 6
Statement of income and expenses.....	Page 7
Notes to Financial Statements.....	Pages 8 to 25
Auditors Report.....	Pages 28 and 29 of the PDF

Unaudited interim financial statements for the six months ended 30 June 2014

Balance sheet.....	Page 4
Statement of income and expenses.....	Page 5
Notes to Financial Statements.....	Pages 6 to 16

Telefónica, S.A.

Consolidated Financial Statements Year ended 31 December 2013

Income statement.....	Page 5
Statement of Financial position.....	Page 4
Statement of Cash flow.....	Page 8
Notes to Financial Statements.....	Pages 9 to 162

Auditors Report Page 3 of the PDF

Consolidated Financial Statements Year ended 31 December 2012

Income statement..... Page 4

Statement of Financial position Page 3

Statement of Cash flow Page 7

Notes to Financial Statements Pages 8 to 198

Auditors Report Page 3 of the PDF

Unaudited but reviewed condensed consolidated interim financial statements for the six months ended 30 June 2014

Income statement..... Page 4

Statement of Financial position Page 3

Statement of Cash flow Page 7

Notes to Financial Statements Pages 8 to 34

Auditors Review Report Pages 2 and 3 of the PDF

Interim management statement January-September 2014

Consolidated Results Pages 3-17

Consolidated Income Statement Page 11

Consolidated Statement of financial position Page 14

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 SECURITIES

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

The issue of the Securities was authorised by a resolution of the Board of Managing Directors of the Issuer dated 21 November 2014 and the guarantee of the Securities was authorised by a resolution of the Delegated Committee of the Board of Directors of the Guarantor dated 14 November 2014, by a resolution of the Board of Directors of the Guarantor dated 30 May 2014, and by a resolution of the shareholders acting through the General Shareholders' Meeting of the Guarantor dated 30 May 2014. A fiscal agency agreement dated 4 December 2014 (the "**Fiscal Agency Agreement**") has been entered into in relation to the 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 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 Securities and the Holders of the Coupons (each as defined in Condition 1(b) below) (whether or not attached to the 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 Securities are serially numbered and in bearer form in the denomination of €100,000, each with Coupons attached on issue.
- (b) **Title:** Title to the Securities and Coupons passes by delivery. The holder of any 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 Securities and Coupons**

- (a) **Status of the Securities and Coupons:** The 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 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 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 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.

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 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 Securities bear interest at the Prevailing Interest Rate from (and including) 4 December 2014 (the "**Issue Date**") in accordance with the provisions of this Condition 4.

Subject to Condition 5, interest shall be payable on the 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 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 Securities is not made, in which event interest shall continue to accrue in respect of unpaid amounts on the 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 Security shall be calculated per €100,000 in principal amount thereof (the "**Calculation Amount**"). The interest payable on each 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 Security for any Interest Period and where it is necessary to compute an amount of interest in respect of any 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 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 4.200 per cent. per annum, payable annually in arrear on each Interest Payment Date commencing on 4 December 2015; and
- (ii) from (and including) the First Reset Date, at the applicable 5 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) 4 December 2024, 3.806 per cent. per annum;

(B) in respect of the period commencing on 4 December 2024 to (but excluding) 4 December 2039, 4.056 per cent. per annum³; and

(C) from and including 4 December 2039, 4.806 per cent. per annum⁴,

all as determined by the Agent Bank (each a "**Subsequent Fixed Interest Rate**"), payable annually in arrear on each Interest Payment Date, commencing on 4 December 2020, subject to Condition 5,

and where:

"**5 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 5 year Swap Rate does not appear on the Reset Screen Page on the relevant Reset Interest Determination Date, the 5 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 5 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 5 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 "**5 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 5 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 Agent, the Paying Agents, any stock exchange on which the Securities are for the time being listed or admitted to trading and, in accordance with Condition 14, the Holders of the 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

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

⁴ Additional step-up of 75 basis points 25 years after the Issue Date

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 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 Deferred Interest Payment 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 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 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,

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 Deferred Interest Payment 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 Deferred Interest Payment 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 Securities are undated securities with no specified maturity date. The Securities may not be redeemed at the option of the Issuer other than in accordance with Conditions 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 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 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 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 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 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 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 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 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 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 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 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 Securities and shall not be deemed to be outstanding for the purposes of calculating quorums at meetings of the Holders of Securities or for the purposes of Condition 12.
- (i) **Cancellation:** All 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 Securities only to the extent that the aggregate principal amount of the 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 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 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 Securities originally issued in any period of 12 consecutive months or (b) 25 per cent. of the aggregate principal amount of the Securities originally issued in any period of 10 consecutive years, or*
- (iii) *the 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 4 December 2039.*

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 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 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 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 Security, unmatred Coupons relating to such Security (whether or not attached) shall become void and no payment shall be made in respect of them. Where any 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 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 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 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 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 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 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 Security or Coupon who is liable for Taxes in respect of such 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 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 Securities are represented by a Security in global form and such Security in global form is deposited with a common depositary for Euroclear and/or Clearstream, Luxembourg, to, or to a third party on behalf of, a Holder or to the beneficial owner of any 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 Additional Provision One of Law 10/2014, 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 Securities are represented by Securities in definitive form, 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 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 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;
- (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 Security to another Paying Agent in a Member State of the European Union; or
- (ix) any taxes that are imposed or withheld pursuant to Sections 1471 through 1474 of the Internal Revenue Code of 1986 (FATCA) (or any amended or successor version of such sections that is substantively comparable and not materially more onerous to comply with), any regulations promulgated thereunder, any official interpretations thereof or any agreements entered into in connection with the implementation thereof.

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 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 One of Law 10/2014 to the Securities for Spanish tax purposes.

Payments in respect of the 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 4 of Additional Provision One of Law 10/2014 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 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 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 Security, in respect of such 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 Security and all interest then accrued but unpaid on such 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 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 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 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 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 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 Securities and Coupons**

If any 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 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 Securities and Modification**

- (a) **Meetings of Holders of Securities:** The Fiscal Agency Agreement contains provisions for convening meetings of Holders of 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 Securities holding not less than one twentieth in principal amount of the 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 Securities for the time being outstanding, or at any adjourned meeting one or more persons being or representing Holders of Securities whatever the principal amount of the Securities held or represented. Any Extraordinary Resolution duly passed shall be binding on Holders of

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 Securities outstanding shall for all purposes be as valid and effective as an Extraordinary Resolution passed at a meeting of Holders of 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 Securities.

- (b) **Modification:** The Securities, these Conditions, the Deed of Covenant and the Deed of Guarantee may be amended without the consent of the Holders of Securities to correct a manifest error. No other modification may be made to the Securities, these Conditions the Deed of Covenant or the Deed of Guarantee except with the sanction of a resolution of the Holders of the 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 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 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 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 Securities) or upon such terms as the Issuer may determine at the time of their issue. References in these Conditions to the Securities include (unless the context requires otherwise) any other securities issued pursuant to this Condition and forming a single series with the Securities.

14. **Notices**

Notices to Holders of 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 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 Securities are represented by a Security in global form and such global form Security is deposited with a common depository for Euroclear and/or Clearstream, Luxembourg, notices to Holders of 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 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 Securities under the Contracts (Rights of Third Parties) Act 1999.

16. **Governing Law**

- (a) **Governing Law:** The Fiscal Agency Agreement, the 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 Securities or the Coupons (including a dispute relating to the existence, validity or termination of the Securities or any non-contractual obligations arising out of or in connection with the 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:

"**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;

"**2014 Non-Call Securities**" means the March 2014 6 Year Non-Call Securities and the March 2014 10 Year 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;

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

"**5 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 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 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 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 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);

"**Dividend Declaration**" has the meaning given to it in Condition 5(c);

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

"**First Reset Date**" means 4 December 2019;

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

"**Further Securities**" means any Securities issued pursuant to Condition 13 and forming a single series with the outstanding 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 4 December 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 4 December 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 and any other shares (*acciones*) in the capital of the Guarantor (and, if divided into classes, each class thereof);

"**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 Securities, including (i) Ordinary Shares of the Issuer and (ii) Preferred Shares of the Issuer, if any;

"**Law 10/2014**" means Law 10/2014 of 26 June 2014, on regulation, supervision and solvency of credit entities (*Ley 10/2014, de 26 de junio, de ordenación, supervisión y solvencia de entidades de crédito*);

"**March 2014 6 Year Non-Call Securities**" means the €750,000,000 Undated 6 Year Non-Call Deeply Subordinated Guaranteed Fixed Rate Reset Securities (ISIN: XS 1050460739) issued by the Issuer on 31 March 2014 and unconditionally and irrevocably guaranteed on a subordinated basis by the Guarantor;

"**March 2014 10 Year Non-Call Securities**" means the €1,000,000,000 Undated 10 Year Non-Call Deeply Subordinated Guaranteed Fixed Rate Reset Securities (ISIN: XS 1050461034) issued by the Issuer on 31 March 2014 and unconditionally and irrevocably guaranteed on a subordinated basis by the Guarantor;

"**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, as amended by an Extraordinary Resolution of the holders adopted at a meeting held on 10 July 2014;

"**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 Additional Provision One of Law 10/2014, 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 Additional Provision One of Law 10/2014 or any other law or regulation of Spain or of any other jurisdiction) 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 2014 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 Securities including (i) the 2014 Non-Call Securities and (ii) the 2013 Non-Call Securities;

"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 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 or, in each case, any successor to the rating agency business thereof;

"Redemption Date" means the date fixed for redemption of the 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 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 fifth 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, as amended by an Extraordinary Resolution of the holders adopted at a meeting held on 10 July 2014;

"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, as amended by an Extraordinary Resolution of the holders adopted at a meeting held on 10 July 2014;

"Subordinated Loan" means the subordinated loan made by the Issuer to the Guarantor dated 4 December 2014, pursuant to which the proceeds of the issue of the 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 Securities originally issued (which for these purposes shall include any Further 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));

"Target System" means the Trans-European Automated Real-Time Gross Settlement Express Transfer payment system which utilises a single shared platform and which was launched on 19 November 2007;

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 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 27 November 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 27 November 2014;

"Taxes" has the meaning given to it in Condition 8(a);

"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 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 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 a Temporary Global Security 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.

The Temporary Global Security will be exchangeable in whole or in part for interests in the 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 the Temporary Global Security unless exchange for interests in the 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.

The 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 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 Securities is not paid when due and payable.

Whenever the 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 Permanent Global Security to the bearer of the Permanent Global Security against the surrender of the Permanent Global Security to or to the order of the Fiscal Agent within 30 days of the bearer requesting such exchange.

If:

- (a) the Temporary Global Security is not duly exchanged, whether in whole or in part, for the 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 the Permanent Global Security for Definitive Securities; or
- (c) the Temporary or Permanent Global Security (or any part of it) has become due and payable in accordance with the Conditions of the 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 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 4 December 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, the Temporary Global Security and Permanent Global Security will contain provisions which modify the Terms and Conditions of the Securities as they apply to the Temporary Global Security and the Permanent Global Security. The following is a summary of certain of those provisions:

Payments: All payments in respect of the 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 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 Securities. On each occasion on which a payment of principal or interest is made in respect of the Temporary Global Security or (as the case may be) the 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 the 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 are represented by the Permanent Global Security (or by a Permanent Global Security and/or the Temporary Global Security) and the Permanent Global Security is (or the Permanent Global Security and/or Temporary Global Security are) deposited with a common depository for Euroclear and Clearstream, Luxembourg, notices to Holders of the 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 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 4 December 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 €850,000,000 Undated 5 Year Non-Call Deeply Subordinated Guaranteed Fixed Rate Reset Securities (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 4 December 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 4 December 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 847,025,000 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
Eduardo José Alvarez Gómez	Director	Head of Financing at Telefónica, S.A.
Jose Miguel Hernández Rabbat	Director	Managing Director of Telfisa Global B.V.

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 (stable 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 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, a.s. ("**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, Telefónica Europe and Telefónica Latin America 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.
- On 31 March 2014, two issuances of undated deeply subordinated reset rate guaranteed securities of Telefónica Europe B.V., with the subordinated guarantee of Telefónica were issued and paid-up, with a face value of €750 million in the case of the 6 Year Non-Call Securities, and €1,000 million in the case of the 10 Year Non-Call Securities.
- On 6 May 2014, Telefónica submitted a binding offer for the acquisition of 56% of the share capital of Distribuidora de Televisión Digital, S.A. ("**DTS**"), directly or indirectly owned by Promotora de Informaciones, S.A. (PRISA).
- On 2 June 2014, after the due process of negotiation, Telefónica's subsidiary Telefónica de Contenidos, S.A.U. ("**Telefónica Contenidos**") executed a share purchase agreement with PRISA. The price agreed amounts to €750 million, subject to customary adjustments at closing. The closing of this purchase agreement is subject to obtaining the relevant authorisation of the competition authorities and to the approval of a representative panel of the banks financing PRISA.
- On 7 May 2014, Telefónica paid a dividend of €0.40 per share in cash (dividend distribution charged against 2014 net income) corresponding to the second tranche of the 2013 dividend which in total amounted to €0.75 per share.

- On 30 May 2014, Telefónica's Annual General Shareholders' Meeting took place on second call with the attendance, present or represented, of 54.81% of the share capital. In this meeting, all the resolutions submitted by the Board of Directors for deliberation and approval were approved by majority of votes.
- On 4 July 2014, Telefónica de Contenidos acquired 22% of the share capital of DTS owned by Mediaset España Comunicación, S.A. ("**Mediaset**") for an amount of €295 million.

A payment of an amount of €30 million has been agreed as consideration for the waiver of Mediaset's pre-emptive rights relating the stake held by PRISA in DTS. Pursuant to the agreement, Mediaset will receive (i) an amount of €10 million in the event that Telefónica de Contenidos closes the acquisition of the 56% stake of DTS held by PRISA and, in that case, (ii) an amount of up to €30 million depending on the evolution of the pay-TV customers in Spain of the Telefónica Group during the 4 years following the closing of such acquisition.

- On 2 July 2014, Telefónica Deutschland received the EU Commission's conditional clearance to acquire the E-Plus Mobilfunk GmbH & Co. KG group (the "**E-Plus Group**") from the Dutch telecommunication corporation Koninklijke KPN N.V. In connection to such conditional clearance, on 25 June 2014, Telefónica Deutschland signed an agreement with the Drillisch Group according to which the latter agreed to acquire, in addition to the agreed capacity to provide services to its existing customers through Telefónica Deutschland's or E-Plus' networks, 20% of the capacity of all mobile networks that belong to Telefónica Deutschland after the acquisition of the E-Plus Group. The 20% capacity will be reached through a glide path over a 5-year period. In addition, the Drillisch Group shall have the right to acquire up to an additional 10% of capacity of the aforementioned mobile networks.

Telefónica Deutschland will grant the Drillisch Group, through a Mobile Bitstream Access model, access to the future joint network of Telefónica Deutschland and E-Plus, as well as to the existing and future technology developments on that network, which the Drillisch Group will be able offer to its customers. Final clearance for the acquisition was given on 29 August 2014. On 1 October 2014, Telefónica Deutschland completed the acquisition of E-Plus, following its execution of a capital increase intended to fund the acquisition of E-Plus. Telefonica maintains a stake of 62.1% in Telefónica Deutschland, which now includes 100% of E-Plus, the Dutch company Koninklijke KPN N.V. holds a 20.5% stake, and the rest is free float.

- On 7 July 2014, Telefónica reached an agreement with Reti Televisive Italiane S.p.A. ("**RTI**") for the acquisition by the former of an 11.11% stake of the capital of a newly created company, which will consolidate the pay-TV business of Mediaset Group in Italy, currently commercialised under the name of "Mediaset Premium". The purchase price for this stake is €100 million.
- On 15 July 2014, after obtaining the corresponding regulatory authorisations, Telefónica concluded the 100% sale of Telefónica Ireland, Ltd.'s participation to the Hutchison Whampoa Group. The value of the sale amounted to €850 million, including an initial cash consideration of €780 million received at the closing of the transaction, and an additional deferred payment of €70 million, based on the completion of agreed financial objectives.
- On 24 July 2014, Telefónica issued €750 million bonds mandatorily exchangeable into ordinary shares of Telecom Italia, S.p.A. ("**Telecom Italia**"), maturing on 24 July 2017. The bonds will accrue a nominal fixed interest rate of 6.0% per annum. The minimum exchange price of the bonds has been set at €0.8600 and the maximum exchange price at €1.0320 per ordinary share of Telecom Italia, which represents a premium of 20% over the minimum exchange price.
- On 5 August 2014, Telefónica and Telefónica Brasil, S.A. submitted an initial offer to Vivendi, S.A. for the combination of Telefónica Brasil, S.A. and Global Village Telecom, S.A. (GVT).

Further to negotiations, on 18 September 2014, a definitive agreement with Vivendi, S.A. for the acquisition by Telefónica Brasil, S.A. of GVT was formalised. The acquisition value of GVT was set at a consideration in cash of €4,663 million and newly issued shares representing 12.0% of the share capital of Telefónica Brasil, S.A. after its combination with GVT. The cash

consideration will be funded through a capital increase at Telefónica Brasil, S.A. in which Telefónica will subscribe its proportional share, funded, in turn, through a capital increase

In addition, Vivendi, S.A. accepted Telefónica's offer to acquire 1,110 million ordinary shares of Telecom Italia (which represent, as at such date, a stake of 8.3% of Telecom Italia's voting share capital and a 5.7% of its total share capital) in exchange for a stake of 4.5% in Telefónica Brasil, S.A. after its combination with GVT, which represents all the ordinary shares and a portion of the preferred shares (representing 0.7% of such class of shares) in Telefónica Brasil, S.A. that Vivendi, S.A. will receive as a consequence of the GVT.

The closing of the transaction remains subject to obtaining the relevant regulatory authorisations (including approval by telecommunications and anti-trust authorities) and the fulfilment of other customary conditions in this type of transactions.

- On 24 September 2014, through its wholly-owned subsidiary Telefónica Participaciones, S.A.U., Telefónica issued €1,500 million notes mandatorily exchangeable into Telefónica ordinary shares, maturing on 25 September 2017. The notes will accrue at a nominal fixed interest rate of 4.90% per annum. The minimum conversion price of the notes will be equal to €11.9000 per share and the maximum conversion price will be equal to €14.5775 per share, resulting in a premium equal to 22.5% over the minimum conversion price.
- On 30 September 2014, Telefónica Brasil, S.A. was granted a national block of 2x10 MHz, in the 700 MHz band spectrum auction, called by ANATEL, for the minimum amount reserved to that block, equivalent to 1,927,964,770 Brazilian Reals (approximately €619 million).

With this acquisition Telefónica Brasil, S.A. has reached its goal of ensuring the necessary spectrum for the medium and long term expansion of the 4G service in order to meet the growing demand for mobile access to high speed Internet.

- On 7 October 2014, through its wholly-owned subsidiary Telefónica Emisiones, S.A.U. under its Guaranteed Euro Programme for the Issuance of Debt Instruments (EMTN Programme), Telefónica launched an issuance of notes guaranteed by Telefónica in the Euro market amounting to €800 million. The notes mature on 17 October 2029, pay an annual coupon of 2.932% with a reoffer price of 100%. Settlement took place on 17 October 2014.
- On 10 October 2014, the Executive Commission of Telefónica's Board of Directors agreed that, at the Executive Commission scheduled for 14 November 2014, the appropriate corporate resolutions to carry out the execution of the free-of-charge capital increase, related to the shareholder compensation by means of a scrip dividend ("**Telefónica's Flexible Dividend**"), approved by the Annual General Shareholder's Meeting held on 30 May 2014, should be adopted. On 14 November 2014, the Executive Commission agreed the implementation of the aforementioned capital increase. As a result, the five trading sessions prior to 14 November 2014 will determine the market price that will apply to the free-of-charge allotment rights purchase price setting formula and to the provisional number of shares to issue formula.

It is also expected that the free-of-charge allotment rights derived from the capital increase will be allotted to Telefónica shareholders who appear as such in the book-entry records of Sociedad de Gestión de los Sistemas de Registro, Compensación y Liquidación de Valores, S.A.U. (Iberclear), at 11:59 p.m. Madrid time, on the day of publication of the capital increase notice in the Official Commercial Registry Gazette (*Boletín Oficial del Registro Mercantil*), which took place on 18 November 2014.

- On 27 October 2014, following a report of the Nominating, Compensation and Corporate Governance Committee, the Board of Directors of Telefónica approved, with regard to the first cycle (2014-2017) of the long-term incentive plan (which consists in the granting of shares of Telefónica to Telefónica Group Executives (including Executive Directors of Telefónica) as approved by the Annual General Shareholders Meeting held on 30 May 2014, (which determined, also, the maximum possible number of shares to be received by the Executive Directors of Telefónica at the end of the first cycle of the Plan)), the amount of theoretical shares to be assigned to the other Executives, and the maximum possible number of shares to be received by

them, in the event of fulfilment of the co-investment requirement, and of the maximum achievement of the Total Shareholder Return (TSR) established in such plan.

- On 10 November 2014, Telefónica, through its 100% subsidiary, Telefónica Internacional, S.A.U., proceeded to the sale of 597,844,100 shares of China Unicom (Hong Kong) Limited ("China Unicom") as further described under "Strategic Partnerships - China United Network Communications Group Co., Ltd. (China Unicom)", below.

Business Overview

On 26 February 2014, the Board of Directors of Telefónica approved the implementation of a new organisational structure focused on clients and which incorporates the digital offering as the main focus for commercial policies. The structure is intended to give greater visibility to local operators, bringing them closer to the corporate decision-making centre, simplifying the Group's global structure and strengthening the transverse areas to improve flexibility and agility in decision making.

As a result of this re-organisation, the new structure is made up of the following segments: Telefónica Spain, Telefónica Brazil, Telefónica Germany, Telefónica UK and Telefónica Hispanoamérica (formed by the Group's operators in Argentina, Chile, Peru, Colombia, México, Venezuela and Central America, Ecuador and Uruguay). These segments include all information relating to wireline, wireless, cable, Internet and television businesses and other digital services in accordance with each location. "Other companies and eliminations" includes the companies belonging to the transverse areas as well as other Group companies and eliminations in the consolidation process.

ACCESSES	September		Percentage variation (%) 2013/2014
	2013	2014	
	<i>Unaudited figures (thousands)</i>		
Final Clients Accesses	314,141.6	309,561.4	(1.5)
Fixed telephony accesses ⁽¹⁾⁽²⁾⁽³⁾	39,399.8	37,325.4	(5.3)
Internet and data accesses	19,112.4	18,168.1	(4.9)
Narrowband	567.7	397.8	(29.9)
Broadband ⁽⁴⁾	18,395.6	17,657.9	(4.0)
Other ⁽⁵⁾	149.1	112.4	(24.6)
Mobile accesses	252,188.1	249,417.9	(1.1)
Prepay ⁽⁶⁾	165,133.3	160,535.5	(2.8)
Contract	87,054.9	88,882.5	2.1
M2M ⁽⁷⁾	8,175.8	8,957.5	9.6
Pay TV ⁽⁸⁾	3,441.2	4,650.0	35.1
Wholesale Accesses	6,173.9	6,585.6	6.7
Unbundled loops	3,665.4	4,034.1	10.1
Shared ULL	147.3	96.6	(34.4)
Full ULL	3,518.1	3,937.5	11.9
Wholesale ADSL	864.0	849.5	(1.7)
Other	1,644.5	1,702.0	3.5
Total Accesses.....	320,315.5	316,147.0	(1.3)
	<i>Unaudited figures</i>		
TELEFÓNICA MOBILE ACCESSES	2013	2014	Percentage variation (%) 2013/2014
Prepay percentage (%)	65.5%	64.4%	(1.1 p.p.)*
Contract percentage (%)	34.5%	35.6%	1.1 p.p.
MBB accesses ('000).....	67,420.1	89,112.6	32.2%
MBB penetration (%).....	26.7%	35.7%	9.0 p.p.
Smartphone penetration (%)	25.2%	35.2%	10.0 p.p.

Note:

- Telefónica Czech Republic accesses are de-consolidated since the first quarter of 2014. T. Ireland accesses are de-consolidated since the third quarter of 2014.

- (1) PSTN (including Public Use Telephony) x1; ISDN Basic access x1; ISDN Primary access; 2/6 Digital Access x30. Company's accesses for internal use included. Voice fixed wireless accesses included. Includes VoIP and Naked ADSL.
- (2) In the first quarter of 2014, 45 thousand fixed wireless inactive accesses were disconnected in Mexico.
- (3) In the second quarter of 2014, fixed telephony accesses include 50 thousand "fixed wireless" additional customers in Peru.
- (4) Includes ADSL, satellite, optical fiber, cable modem and broadband circuits.
- (5) Retail circuits other than broadband.
- (6) In the first quarter of 2014, 1.9 million inactive accesses were disconnected in Mexico.
- (7) In the first quarter of 2014, 569 thousand inactive accesses were disconnected in Spain.
- (8) In the second quarter of 2014, Pay TV accesses included 131 thousand "TV Mini" customers in Spain.
- * Percentage points

With regard to operating variables, Telefónica managed 316.1 million accesses at the end of September 2014, up 2% year-on-year, excluding the accesses of Telefónica Czech Republic and Telefónica Ireland from the basis of 2013, following their disposal in January and July 2014, respectively. This increase is driven by the sustained growth of higher value and quality segments such as mobile contract (smartphones and LTE), fiber and pay TV, which maintained a high level of commercial activity during the first nine months ended 30 September 2014.

Accesses in Hispanoamérica accounted for 41% of the total accesses of the Telefónica Group, which increased by 2.7% year-on-year, and in Brazil accesses accounted for 30% of the total, an increase of 4.0% year-on-year.

Mobile accesses stood at 249.4 million at the end of September 2014, up 2% in comparison to the figure as at 30 September 2013 excluding the accesses of Telefónica Czech Republic and Telefónica Ireland from the basis of 2013, driven by the strong growth of the contract segment (+8% year-on-year) which, as at 30 September 2014, accounted for 36% of total mobile accesses (+1 percentage points).

As a result of Telefónica's focus on expanding data services, smartphones accesses (all with a data plan attached) stood at 82.3 million, up 43% year-on-year excluding the accesses of Telefónica Czech Republic and Telefónica Ireland from the basis of 2013, reaching a penetration rate of 35% over total access base (+10 percentage points year-on-year).

Retail fixed broadband accesses (17.7 million at the end of September 2014) maintained a year-on-year growth rate of 1% excluding the accesses of Telefónica Czech Republic from the basis of 2013, underpinned by the growth of Hispanoamérica and Brazil.

Pay TV accesses totalled 4.6 million at the end of September 2014, an increase of 41% year-on-year excluding the accesses of Telefónica Czech Republic from the basis of 2013. This acceleration in commercial activity was primarily driven by Telefónica España, reaching 1.6 million (2.6 times compared with September 2013), reflecting the strong take-up for "Movistar TV", the key differentiation lever of the refreshed convergent offer (several commercial products, such as Fixed Telephony, Broad Band, TV and Mobile products, sold as one combined product). In addition, both Brazil and Hispanoamérica posted double-digit year-on-year growth in their customer bases.

Segment Outlook

Spain

TELEFÓNICA SPAIN ACCESSES	September		% Chg
	2013	2014	
	<i>Unaudited figures (thousands)</i>		
Final Clients Accesses	37,171.2	35,845.3	(3.6)
Fixed telephony accesses ⁽¹⁾	11,261.3	10,595.2	(5.9)
Naked ADSL	22.4	21.9	(2.3)
Internet and data accesses	5,872.6	5,920.9	0.8
Narrowband	46.1	35.9	(22.2)
Broadband ⁽²⁾	5,812.3	5,872.7	1.0
Fiber	494.0	1,068.9	116.4
Other ⁽³⁾	14.3	12.3	(13.7)
Mobile accesses	19,428.0	17,749.7	(8.6)
Prepay	4,560.0	3,559.2	(21.9)
Contract	14,867.9	14,190.5	(4.6)
M2M ⁽⁴⁾	1,979.4	1,566.9	(20.8)
Pay TV ⁽⁵⁾	609.3	1,579.4	159.2

TELEFÓNICA SPAIN ACCESSES	September		% Chg
	2013	2014	
	<i>Unaudited figures (thousands)</i>		
Wholesale Accesses	4,792.2	5,309.0	10.8
WLR ⁽⁶⁾	506.6	564.0	11.3
Unbundled loops	3,619.0	4,034.1	11.5
Shared ULL	147.3	96.6	(34.4)
Full ULL ⁽⁷⁾	3,471.7	3,937.5	13.4
Wholesale ADSL	666.2	710.6	6.7
Other ⁽⁸⁾	0.4	0.3	(25.2)
Total Accesses	41,963.3	41,154.3	(1.9)

Note:

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

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

⁽³⁾ Leased lines.

⁽⁴⁾ In the first quarter of 2014, 569 thousand inactive accesses were disconnected.

⁽⁵⁾ Since the second quarter of 2014, Pay TV accesses include 131 thousand "TV Mini" customers.

⁽⁶⁾ Wholesale Line Rental.

⁽⁷⁾ Includes naked shared loops.

⁽⁸⁾ Wholesale circuits.

TELEFÓNICA SPAIN	September		% Chg Local Cur
	2013	2014	
	<i>Unaudited figures</i>		
Voice Traffic (Million minutes)	25,659	26,567	3.5
ARPU (EUR) ⁽¹⁾	18	16	(11.5)
Prepay	7.5	6.3	(15.9)
Contract ⁽²⁾	24.5	20.8	(15.3)
Data ARPU (EUR)	6.7	7.0	3.2
% non-SMS over data revenues	91.6%	94.9%	3.3

Note:

- ARPU: monthly average revenue divided by the monthly average accesses of the period.

- Voice traffic is defined as minutes used by the company's customers, both outbound and inbound. On-net traffic is only included once (outbound), and promotional traffic is also included. Traffic not associated to the Company's mobile customers (roaming-in, MVNOs, interconnection of third parties and other business lines) is excluded. Traffic volume is non-rounded.

⁽¹⁾ Impacted by the disconnection of 569 thousand inactive M2M accesses in the first quarter of 2014.

⁽²⁾ Excludes M2M.

- Telefónica Spain had 41.2 million accesses at the end of September 2014, down 2% year-on-year. More than half of the year-on-year decline in accesses is associated with the disconnection of 569 thousand inactive M2M mobile contract accesses in the first quarter of 2014.
- "Movistar Fusión", with a customer base of 3.6 million and 1.4 million additional mobile lines, maintained solid year-on-year growth, representing 70% of fixed broadband base and 55% of mobile contract in the consumer segment for the first nine months of 2014. The new convergent portfolio (including IP TV services in packages from 60 euro/month) continues to attract customers.
- The "Movistar Fusión TV" convergent catalogue was modified on 18 September 2014, with no increase in prices, and the main mobile line now includes: i) 500 MB of 4G data in the "Movistar Fusión TV Contigo" package, and ii) 2GB of 4G data in the superior "Movistar Fusión TV" package. Additional mobile lines also increased 4G mobile data allowance to 2GB for 25 euro/month, VAT included.
- All the tariffs include 4G service and have no permanence commitment; i) the "Vive 11" package includes calls at zero cents per minute (€0.1815 call connection fee) and 800 MB of data for €11 euro per month; ii) the "Vive 22" package includes 200 minutes of calls and 1.1GB for 22 euro/month; iii) the "Vive 30" package includes unlimited voice calls and SMS and 2GB for 30 euro/month; and iv) the "Vive 43" package includes unlimited voice calls and SMS, 4GB and up to 3 additional MultiSIM cards for different mobile devices and 12 months' free access to "Nubico Premium" (virtual library) for 43 euro/month. The monthly prices include VAT.

- Retail fixed telephony accesses, decreased by 6% year-on-year compared with the figure as at 30 September 2013.
- Retail broadband accesses, 5.9 million at the end of September, grew by 1% year-on-year.
- Fiber customer growth accelerated, more than doubling year-on-year the accesses connected to 1.1 million (including 183 thousand 10 Mb fiber customers). Fiber customers with 100 Mb speed, with higher ARPU (currently, a €10 price premium, €12 with VAT) and lower churn (0.5 times) compared with ADSL customers, totalled 886 thousand accesses. The pace of fiber deployment continued to accelerate, reaching 8.8 million premises passed at the end of September.
- Pay TV accesses reached 1.6 million (2.6 times compared with September 2013), reflecting the strong take-up for "Movistar TV", which is considered to be the key differentiation lever of the refreshed convergent offer. Also noteworthy is the significant reduction in churn (1.0% at the end of September 2014; -2.2 percentage points year-on-year).
- Total mobile accesses stood at 17.7 million, down 9% compared with September 2013, impacted by the disconnection of inactive M2M mobile contract accesses in the first quarter, as mentioned above. There was an improved performance posted by the contract base. The net additions of the first nine months of 2014 reverted the negative trend (+20 thousand accesses), and the total contract base is virtually stable year-on-year (-1%), excluding the impact of inactive M2M disconnections.
- The improved performance of contract accesses is mainly due to the ongoing improvement in churn and the reduction in the net portability balance since the launch of the new convergent offer (-456 thousand accesses at the end of September, -19.5% year-on-year).
- 75% of mobile voice customers in the consumer segment have already migrated to "Fusión" or the new mobile tariffs launched in 2013.
- Smartphone penetration grew to 57% (+9 percentage points in comparison to the figure in September 2013). LTE network rollout continues to progress and coverage reached 50% of the population as at the end of September 2014.
- Mobile ARPU is becoming less representative of the business performance as "Movistar Fusión" penetration increases, owing to the allocation of revenue between the fixed and mobile businesses and the changes in the offer. Mobile ARPU declined by 11.5% in the first nine months of 2014.

UK

TELEFÓNICA UK ACCESSES	September		% Chg
	2013	2014	
	<i>Unaudited figures (thousands)</i>		
Final Clients Accesses	23,639.5	24,324.5	2.9
Fixed telephony accesses ⁽¹⁾	198.7	221.5	11.5
Internet and data accesses	13.6	17.8	30.5
Broadband	13.6	17.8	30.5
Mobile accesses	23,427.2	24,085.2	2.8
Prepay	10,764.7	10,658.4	(1.0)
Contract	12,662.4	13,426.7	6.0
M2M	1,943.3	2,116.2	8.9
Wholesale Accesses ⁽²⁾	40.7	-	-
Total Accesses	23,680.2	24,324.5	2.7

Note:

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

⁽²⁾ From the first quarter of 2014, the company stopped offering a wholesale service.

TELEFÓNICA UK	September		% Chg Local Cur
	2013	2014	
	<i>Unaudited figures</i>		
Voice Traffic (Million minutes).....	36,241	36,587	1.0
ARPU (EUR).....	19.8	18.9	(9.1)
Prepay.....	7.7	7.3	(10.1)
Contract ⁽¹⁾	35.4	33.3	(10.5)
Data ARPU (EUR).....	10.5	10.8	(1.3)
% non-SMS over data revenues.....	49.9%	57.7%	7.7p.p.

Note:

- ARPU: monthly average revenue divided by the monthly average accesses of the period.
- Voice traffic is defined as minutes used by the company customers, both outbound and inbound. On-net traffic is only included once (outbound), and promotional traffic is included. Traffic not associated to the Company's mobile customers (roaming-in, MVNOs, interconnection of third parties and other business lines) is excluded. Traffic volume non-rounded.

⁽¹⁾ Excludes M2M.

Total accesses amounted to 24.3 million at the end of September 2014, a growth of 3% year-on-year, with the following operating highlights:

- The contract mobile customer base grew 6% year-on-year as of September 2014 to account for 56% of the mobile base, an increase of 2 percentage points year-on-year. Total mobile accesses reached 24.1 million (+3% year-on-year).
- Contract net additions, excluding M2M, totalled 189 thousand in September 2014 (209 thousand including M2M), and grew 28% year-on-year as a result of the launch of new devices in the third quarter coupled with handset apathy in the market in the first half of 2014.
- Prepay net additions in the nine months to 30 September 2014 reached 436 thousand (542 thousand in the contract segment).
- Contract churn excluding M2M remained at levels of 1.0% in the first nine months of 2014, improving 0.1 percentage points year-on-year.
- Smartphone penetration reached 50% (+2 percentage points year-on-year) with the base totalling 10.8 million accesses at the end of the September.
- Data traffic increased 66% year-on-year in comparison with the first nine months of 2013 due to increased smartphone penetration and higher usage per customer.
- ARPU in the first nine months of 2014 was 3.1% down in comparison to the same period of 2013, excluding "O2 Refresh".

Germany

TELEFÓNICA GERMANY ACCESSES	September		% Chg
	2013	2014	
	<i>Unaudited figures (thousands)</i>		
Final Clients Accesses.....	24,306.2	24,113.2	(0.8)
Fixed telephony accesses ⁽¹⁾	2,144.9	2,050.9	(4.4)
Internet and data accesses.....	2,543.5	2,413.4	(5.1)
Narrowband.....	277.2	252.5	(8.9)
Broadband.....	2,266.2	2,160.8	(4.7)
Mobile accesses.....	19,576.4	19,648.9	0.4
Prepay.....	9,260.7	8,989.3	(2.9)
Contract.....	10,315.7	10,659.6	3.3
M2M.....	89.9	106.0	18.0
Pay TV ⁽²⁾	41.5	-	-
Wholesale Accesses.....	1,130.4	1,137.6	0.6
Total Accesses.....	25,436.6	25,250.8	(0.7)

Note:

- (1) PSTN (including Public Use Telephony) x1; ISDN Basic access x1; ISDN Primary access; 2/6 Digital Access x30. Company's accesses for internal use included. Includes VoIP and Naked ADSL.
- (2) In the fourth quarter of 2013, all TV accesses were disconnected.

TELEFÓNICA GERMANY	September		% Chg Local Cur
	2013	2014	
	<i>Unaudited figures</i>		
Voice Traffic (Million minutes).....	22,632	22,745	0.5
ARPU (EUR).....	12.7	12.4	(2.2)
Prepay	5.2	5.2	0.5
Contract ⁽¹⁾	19.6	18.8	(4.2)
Data ARPU (EUR).....	6.2	6.1	(0.9)
% non-SMS over data revenues	65.5%	72.8%	7.3p.p.

Note:

- ARPU: monthly average revenue divided by the monthly average accesses of the period.
- Voice traffic is defined as minutes used by the company customers, both outbound and inbound. On-net traffic is only included once (outbound), and promotional traffic is included. Traffic not associated to the Company's mobile customers (roaming-in, MVNOs, interconnection of third parties and other business lines) is excluded. Traffic volume non-rounded.

(1) Excludes M2M

Telefónica Deutschland's total access base stood at 25.3 million at the end of September 2014, with a minimal reduction year-on-year (-0.7%). Operating highlights were:

- The contract mobile customer base accelerated its growth to +3% year-on-year driven by the performance in both consumer and business segments. Total mobile accesses reached 19.6 million (+0.4% year-on-year), of which contract represented 54% (+2 p.p. year-on-year).
- Smartphone penetration reached 34% at the end of September 2014, 4 percentage points higher than in the same period in 2013. As a result of the increasing focus from new and existing customers on LTE, the demand for LTE-enabled handsets further accelerated to 88% of the total September 2014 smartphone shipments.
- Total mobile net additions for the nine months period, reached 248 thousand, a significant year-on-year improvement in contract (374 thousand, +80% year-on-year), while 126 thousand net disconnections were registered in the prepay segment versus 69.4 thousands net additions from the previous year. Contract churn excluding M2M was increased by 1.5% in the period from January to September 2014 in comparison to the figures from the same period in 2013, owing to a more dynamic competitive environment.
- Mobile ARPU reached €12.4 in the nine month period ended 30 September 2014 in comparison to €12.7 for the same period ended 30 September 2013. This resulted from a customer mix in both acquisition and renewals, plus a stabilisation of the declining SMS usage evolution. The adoption of LTE enabled smartphones and related tariffs from new and existing customers continued to be an important driver, while not yet completely offsetting the ongoing headwinds from the lower usage of SMS and the repositioning of the customer base within the new mobile tariff portfolio.
- Data ARPU declined 0.9% year-on-year from January to September 2014. Non-SMS data ARPU continued to grow (+10.1% year-on-year for the nine month period ended 30 September 2014).
- Data traffic grew 32% in the nine month period ended 30 September 2014 in comparison to the same period in 2013, mainly driven by the increasing number of LTE-enabled handsets, which show 3 times higher traffic usage in comparison to non-LTE smartphones.
- Retail broadband fixed Internet accesses (2.2 million, -5% year-on-year) registered a net loss of 83 thousand in the first nine months, as new high speed additions (with an increasing share of VDSL lines) failed to compensate DSL disconnections in an intense competitive market.

Brazil

TELEFÓNICA BRAZIL ACCESSES	September		% Chg
	2013	2014	
	<i>Unaudited figures (thousands)</i>		
Final Clients Accesses	91,907.9	95,601.5	4.0
Fixed telephony accesses ⁽¹⁾	10,624.1	10,942.1	3.0
Internet and data accesses	4,081.8	4,114.8	0.8
Narrowband	105.6	82.0	(22.3)
Broadband ⁽²⁾	3,898.0	3,961.6	1.6
Fiber	170.9	322.1	88.4
Other ⁽³⁾	78.2	71.2	(9.0)
Mobile accesses	76,614.3	79,817.0	4.2
Prepay	54,476.4	52,639.8	(3.4)
Contract	22,138.0	27,177.2	22.8
M2M	2,071.2	3,197.5	54.4
Pay TV	587.7	727.6	23.8
Wholesale Accesses	19.7	26.2	33.4
Total Accesses T. Brasil	91,927.6	95,627.7	4.0

Note:

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

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

⁽³⁾ Retail circuits other than broadband.

BRAZIL SELECTED MOBILE BUSINESS OPERATING DATA	September		% Chg Local Cur
	2013	2014	
	<i>Unaudited figures</i>		
Voice Traffic (Million minutes)	85,665.7	93,539.8	9.2
ARPU (EUR)	8.1	7.2	(0.7)

Note:

- ARPU: monthly average revenue divided by the monthly average accesses of the period.

- Voice traffic is defined as minutes used by the company customers, both outbound and inbound. On-net traffic is only included once (outbound), and promotional traffic is included. Traffic not associated to the Company's mobile customers (roaming-in, MVNOs, interconnection of third parties and other business lines) is excluded. Traffic volume non rounded.

As at 30 September 2014, Telefónica managed 95.6 million accesses in Brazil, 4% more than at September 2013, despite a more restrictive reporting criteria for prepay customers.

Regarding operating trends in the mobile business:

- Mobile accesses reached 79.8 million as at 30 September 2014 (+4% year-on-year), driven by the 23% year-on-year growth in the contract segment, which accounted for 34% of total mobile accesses (+5 percentage points year-on-year). The strategic focus on data growth was reflected in the strong increase in smartphones, doubling year-on-year, to a penetration of 40% (+19 percentage points year-on-year).
- Net additions in the nine month period ended 30 September 2014 totalled 2.6 million accesses, driven by net additions of 3.5 million accesses in the contract segment. The prepaid segment posted a net loss of 0.9 million accesses in the first nine months of 2014, affected by more restrictive reporting criteria for customers and as a result of campaigns to migrate higher-value customers to the contract segment. The increased weight of accesses in the "Vivo Tudo" plans (integrated service package that aims to expand data services in the prepaid segment) to a total of 9.9 million users was notable.
- As a result of the higher quality of accesses and the strategic focus on data, data traffic rose 54% year-on-year in the first nine months of 2014. Voice traffic also showed a solid performance, increasing by 9% in the first nine months in comparison to the figure as at 30 September 2013.
- The higher penetration of the contract accesses, with an ARPU 4 times higher than the prepay, led to an outgoing ARPU increase of 5.2% year-on-year in the first nine months of 2014,

mainly underpinned by data. This growth allowed for the effects of the strong regulatory impact reflected in the nine months ended 30 September 2014, keeping total ARPU virtually stable (-0.7% year-on-year in the first nine months of 2014).

Regarding commercial activity in the fixed business as at 30 September 2014:

- Traditional accesses stood at 10.9 million, with year-on-year growth of 3%, after posting net additions of 194 thousand accesses in the nine month period ended 30 September 2014, driven mainly by Fixed Wireless technology accesses (+424 thousand in the first nine months of 2014).
- Retail broadband accesses totalled 4.0 million (+2% year-on-year), after reaching net additions of 25 thousand accesses in the first nine months of 2014. Fiber accesses, reached 322 thousand as at 30 September 2014 with 118 thousand net additions in the first nine months of 2014. This trading acceleration is translated into a positive impact on business metrics as fiber accesses have lower churn levels and higher ARPU (0.6 times and 1.7 times, respectively, compared to fixed broadband accesses). In addition, the company maintained its strong fiber deployment already reaching 3.4 million premises in Sao Paulo.
- Pay TV accesses stood at 728 thousand, up 24% year-on-year after posting net additions of 88 thousand in the first nine months of 2014 and as in the case of broadband, the growing number of accesses connected to fiber (32 thousand in the first nine months of 2014) had a significant impact.

Hispanoamérica

TELEFÓNICA HISPANOAMERICA ACCESSES	September		% Chg
	2013	2014	
	<i>Unaudited figures (thousands)</i>		
Final Clients Accesses	125,990.1	129,347.1	2.7
Fixed telephony accesses ⁽¹⁾⁽²⁾⁽³⁾	13,758.7	13,515.7	(1.8)
Internet and data accesses	5,106.0	5,371.3	5.2
Narrowband	61.0	27.3	(55.2)
Broadband ⁽⁴⁾	5,015.6	5,315.1	6.0
Other ⁽⁵⁾	29.4	28.9	(1.8)
Mobile accesses	105,070.4	108,117.1	2.9
Prepay ⁽⁶⁾	82,734.1	84,688.7	2.4
Contract	22,336.3	23,428.4	4.9
M2M	1,693.9	1,970.9	16.4
Pay TV	2,055.1	2,343.0	14.0
Wholesale Accesses	22.4	112.7	n.m.
Total Accesses T. Hispanoamérica	126,012.5	129,459.8	2.7

TELEFÓNICA MOBILE ACCESSES	September		% Chg
	2013	2014	
	<i>Unaudited figures</i>		
Prepay percentage (%)	78.7%	78.3%	(0.4 p.p.)
Contract percentage (%)	21.3%	21.7%	0.4 p.p.
MBB accesses ('000)	21,284.0	28,831.0	35.5%
Smartphone penetration (%)	20.3%	26.7%	6.4 p.p.

Note:

⁽¹⁾ PSTN (including Public Use Telephony) x1; ISDN Basic access x1; ISDN Primary access; 2/6 Digital Access x30. Company's accesses for internal use included. Voice fixed wireless accesses included.

⁽²⁾ In the first quarter of 2014, 45 thousand fixed wireless inactive accesses were disconnected in Mexico.

⁽³⁾ In the second quarter of 2014, fixed telephony accesses include 50 thousand "fixed wireless" additional customers in Peru.

⁽⁴⁾ Includes ADSL, optical fiber, cable modem and broadband circuits.

⁽⁵⁾ Retail circuits other than broadband.

⁽⁶⁾ In the first quarter of 2014, 1.9 million inactive accesses were disconnected in Mexico.

As at 30 September 2014, Telefónica Hispanoamérica managed a total of 129.5 million accesses in the region, up 3% year-on-year.

The main trends in the mobile business for the nine month period ended 30 September 2014 included the following:

- Mobile accesses stood at 108.1 million (+3% year-on-year), with net additions of 850 thousand accesses in the first nine months of 2014. Accesses in the contract segment rose by 5% year-on-year, accounting for 22% of the total, following net additions of 686 thousand during the year. The prepay segment posted a year-on-year increase of 2%, with net additions of 165 thousand accesses in the year, although the base of customers with frequent top-ups rose 6% year-on-year.
- On the other hand, smartphones continued to be the highest growing access area, rising 42% year-on-year, that almost doubled that of the same period of 2013, reaching a penetration of 26% over mobile accesses (+7 percentage points year-on-year).
- Voice traffic showed growth of 18% year-on-year for the first nine months of 2014, while the year-on-year rise in data traffic remained strong growing by 63% in the first nine months, underpinned by both the increase in smartphones and in the average usage per access.
- The focus on quality of the customer base, which was reflected in the aforementioned strong increases in traffic, led to a year-on-year rise in ARPU of +9.4% in the first nine months.

Highlights in the fixed business include:

- Traditional business accesses stood at 13.5 million (-2% year-on-year), with a net loss of 263 thousand accesses in the first nine months of 2014, associated to the lower commercial activity primarily in accesses under "Fixed Wireless" technology and despite the steady churn levels.
- Broadband accesses reached 5.3 million (+6% year-on-year) following net additions of 240 thousand accesses in the first nine months of 2014, with the greater weight of accesses in higher speeds (48% of accesses with speeds above 4Mbps; +12 percentage points year-on-year) being of significant impact. Fixed broadband accesses penetration over traditional business accesses reached 39% (+3 percentage points year-on-year).
- Pay TV accesses totalled 2.3 million (+14% year-on-year) with net additions of 210 thousand accesses in the first nine months of 2014. The penetration over total traditional business accesses stood at 17% (+2 percentage points year-on-year).

Argentina

TELEFÓNICA ARGENTINA ACCESSES

	September		% Chg
	2013	2014	
	<i>Unaudited figures (thousands)</i>		
Final Clients Accesses	26,985.6	25,910.5	(4.0)
Fixed telephony accesses ⁽¹⁾	4,819.3	4,750.4	(1.4)
Fixed wireless	315.6	304.5	(3.5)
Internet and data accesses	1,835.2	1,870.7	1.9
Narrowband	16.4	11.8	(28.4)
Broadband ⁽²⁾	1,818.8	1,859.0	2.2
Mobile accesses	20,331.0	19,289.4	(5.1)
Prepay	13,389.8	12,337.2	(7.9)
Contract	6,941.3	6,952.1	0.2
M2M	406.2	470.8	15.9
Wholesale Accesses	13.9	104.9	n.m.
Total Accesses	26,999.4	26,015.4	(3.6)

Note:

⁽¹⁾ PSTN (including Public Use Telephony) x1; ISDN Basic access x1; ISDN Primary access; 2/6 Digital Access x30. Company's accesses for internal use included. Voice fixed wireless accesses included.

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

ARGENTINA SELECTED MOBILE BUSINESS OPERATING DATA	September		% Chg Local Cur
	2013	2014	
	<i>Unaudited figures</i>		
Voice Traffic (Million minutes).....	16,555.3	17,122.6	3.4
ARPU (EUR).....	9.6	7.1	14.2

Note:

- ARPU: monthly average revenue divided by the monthly average accesses of the period.
- Voice traffic is defined as minutes used by the company customers, both outbound and inbound. On-net traffic is only included once (outbound), and promotional traffic is included. Traffic not associated to the Company's mobile customers (roaming-in, MVNOs, interconnection of third parties and other business lines) is excluded. Traffic volume non rounded.

Telefónica in Argentina managed 26.0 million accesses at 30 September 2014, down 4% year-on-year.

Operating highlights in the mobile business for the nine months ended 30 September 2014 included:

- Mobile accesses totalled 19.3 million (-5% year-on-year), with a growth of smartphones, up 11% year-on-year, which accounted for 31% of total accesses (+5 percentage points year-on-year).
- Net loss in the first nine months of 2014 stood at 665 thousand accesses, due to the slowdown in consumption in the country and the high prepay churn (4.3% in the first nine months of the year; +1.9 percentage points year-on-year) associated with low-value customers.
- Churn in the contract segment remained at 1.1% in the first nine months of 2014, allowing contract accesses to increase slightly (+0.2% year-on-year) despite the lower commercial activity.
- Voice traffic rose by 3% year-on-year in the first nine months of 2014, while data traffic by 44% year-on-year, driven by the strong expansion of smartphones.
- ARPU accelerated its growth to 14.2% in the first nine months period of 2014, leveraged by growth in both the contract and prepay segments.

Regarding commercial activity in the fixed business for the nine months ended 30 September 2014:

- Traditional fixed accesses reached 4.8 million (-1% year-on-year) affected by lower commercial activity which caused net losses of 83 thousand accesses in the first nine months of 2014 and low churn continued (0.9% in the first nine months of 2014).
- Retail broadband accesses totalled 1.9 million (+2% year-on-year), after posting net additions of 23 thousand accesses in the first nine months of 2014. The increase of accesses with speeds of at least 4 Mb (+14% year-on-year) was of note.

Chile

TELEFÓNICA CHILE ACCESSES	September		% Chg
	2013	2014	
	<i>Unaudited figures (thousands)</i>		
Final Clients Accesses	13,447.4	13,586.1	1.0
Fixed telephony accesses ⁽¹⁾	1,674.5	1,593.9	(4.8)
Internet and data accesses	972.5	1,030.5	6.0
Narrowband	5.2	4.9	(7.5)
Broadband ⁽²⁾	964.9	1,023.4	6.1
Other ⁽³⁾	2.4	2.3	(6.3)
Mobile accesses	10,319.8	10,381.4	0.6
Prepay	7,656.1	7,563.7	(1.2)
Contract	2,663.8	2,817.7	5.8
M2M	263.2	319.9	21.5
Pay TV	480.5	580.3	20.8
Wholesale Accesses	4.8	5.4	13.8
Total Accesses	13,452.2	13,591.5	1.0

Note:

⁽¹⁾ PSTN (including Public Use Telephony) x1; ISDN Basic access x1; ISDN Primary access; 2/6 Digital Access x30. Company's accesses for internal use included. Voice fixed wireless accesses included.

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

⁽³⁾ Retail circuits other than broadband.

CHILE SELECTED MOBILE BUSINESS OPERATING DATA	September		% Chg Local Cur
	2013	2014	
	<i>Unaudited figures</i>		
Voice Traffic (Million minutes)	10,001.6	9,353.8	(6.5)
ARPU (EUR)	11.0	8.6	(7.2)

Note:

- ARPU: monthly average revenue divided by the monthly average accesses of the period.
- Voice traffic is defined as minutes used by the company customers, both outbound and inbound. On-net traffic is only included once (outbound), and promotional traffic is included. Traffic not associated to the Company's mobile customers (roaming-in, MVNOs, interconnection of third parties and other business lines) is excluded. Traffic volume non rounded.

During the first nine months of 2014, Telefónica in Chile intensified the roll-out of LTE in the mobile business, achieving 60% population coverage as at 30 September 2014. The deployment of fiber continued in the fixed business (reaching 278 thousand premises), VDSL with an offer in fixed broadband of speeds up to 150 Mb, and pay TV offering 40 HD channels.

As at 30 September 2014, Telefónica in Chile managed 13.6 million accesses (+1% year-on-year). Operating highlights in the mobile business for the nine months ended 30 September 2014 included:

- Mobile accesses standing at 10.4 million (+1% year-on-year), reflecting the growth in contract accesses (6% year-on-year) that, as of 30 September 2014, accounted for 27% of total mobile accesses (+1 percentage points year-on-year) following the commercial repositioning in the first half of 2013. Additionally, smartphones increased by 33% year-on-year and, as of 30 September 2014, accounted for 28% of mobile accesses (+7 percentage points year-on-year).
- Net additions in the contract segment reached 134 thousand accesses in the first nine months of 2014, as a result of bundle plan offers focused on data growth. Contract portability performance, with a net balance of +73 thousand in the first nine months of 2014, was notable despite increasing competition.
- Net additions in the first nine months of 2014 were negative (a decrease of 109 thousand year-on-year), affected by the high churn in the prepaid segment (disconnection of low value accesses). However, the volume of gross additions rose year-on-year in the first nine months (+6%), mainly driven by the contract segment (+20% in the first nine months of 2014, year-on-year).

- Data traffic continued showing a sharp year-on-year growth during the first nine months of 2014 increasing from 21.9 terabytes as at 30 September 2013 to 39.7 as at 30 September 2014 (+81% year-on-year in the first nine months of 2014), resulting from the company's focus on data. During the first nine months of 2014, the pace of decline in voice traffic slowed to a year-on-year decrease of 6%.
- During the first nine months of 2014, ARPU decreased by 7.2% year-on-year, reflecting the impact of the reduction in mobile termination rates. This impact was partially offset by the good performance of outgoing ARPU (+5.5% year-on-year in the first nine months of 2014), mainly driven by the strong performance of data (year-on-year growth of 28.8% in the first nine months of 2014).

Regarding the commercial activity in the fixed business, as in the mobile business, there were new high-value customers, with an increased weight of gross additions with higher speeds in broadband and the good performance of pay TV services.

- Traditional fixed accesses stood at 1.6 million as at 30 September 2014 (-5% year-on-year), posting a net loss of 60 thousand accesses in the first nine months of the year.
- Retail broadband accesses totalled 1.0 million (+6% year-on-year), with net additions of 53 thousand accesses in the first nine months of 2014. The higher weight of fiber and VDSL gross additions was especially noteworthy (25% of gross additions in the first nine months of 2014 compared to 16% in the same period of 2013).

Pay TV accesses stood at 580 thousand, up 21% year-on-year following net additions of 77 thousand in the first nine months of 2014 (+36% year-on-year).

Peru

TELEFÓNICA PERU ACCESSES	September		% Chg
	2013	2014	
	<i>Unaudited figures (thousands)</i>		
Final Clients Accesses	20,896.9	21,632.6	3.5
Fixed telephony accesses ⁽¹⁾	2,844.2	2,749.3	(3.3)
Fixed wireless ⁽²⁾	328.8	280.2	(14.8)
Internet and data accesses	1,425.5	1,505.2	5.6
Narrowband	5.4	1.2	(78.7)
Broadband ⁽³⁾	1,399.2	1,483.2	6.0
Other ⁽⁴⁾	20.8	20.8	0.0
Mobile accesses	15,722.4	16,489.0	4.9
Prepay	11,385.5	11,450.9	0.6
Contract	4,336.8	5,038.1	16.2
M2M	80.5	87.8	9.2
Pay TV	904.8	889.1	(1.7)
Wholesale Accesses	0.4	0.4	9.4
Total Accesses	20,897.2	21,633.0	3.5

Note:

⁽¹⁾ PSTN (including Public Use Telephony) x1; ISDN Basic access x1; ISDN Primary access; 2/6 Digital Access x30. Company's accesses for internal use included. Voice fixed wireless accesses included.

⁽²⁾ In the second quarter of 2014, fixed telephony accesses include 50 thousand additional customers.

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

⁽⁴⁾ Retail circuits other than broadband.

PERU SELECTED MOBILE BUSINESS OPERATING DATA	September		% Chg Local Cur
	2013	2014	
	<i>Unaudited figures</i>		
Voice Traffic (Million minutes)	17,653.6	21,825.1	23.6
ARPU (EUR)	6.7	6.3	2.1

Note:

- ARPU: monthly average revenue divided by the monthly average accesses of the period.

- Voice traffic is defined as minutes used by the company customers, both outbound and inbound. On-net traffic is only included once (outbound), and promotional traffic is included. Traffic not associated to the Company's mobile customers (roaming-in, MVNOs, interconnection of third parties and other business lines) is excluded. Traffic volume non rounded.

At the end of September 2014, Telefónica Peru managed 21.6 million accesses, up 4% year-on-year. Operating highlights in the mobile business for the nine months ended 30 September 2014 included:

- Mobile accesses stood at 16.5 million, up 5% year-on-year, driven by contract accesses (+16% year-on-year; 31% of the total; +3 p.p. year-on-year) and prepay accesses (+1%), with the customer base with frequent top-ups growing by 11% year-on-year. Smartphones remained as the main growth driver, increasing by 44% year-on-year and reaching a 14% penetration rate at the end of September 2014 (+4 percentage points year-on-year).
- Net additions reached 727 thousand accesses in the first nine months of 2014, driven by strong contract net additions (535 thousand for the first nine months). This performance was boosted by the contract churn improvement to (-0.6 percentage points year-on-year).

At the same time the prepay segment recovery is notable, with 192 thousand for the first nine months of 2014, despite the high churn level (4.8%) upon the application of more restrictive reporting criteria for customers.

- Voice traffic increased by +24% in the first nine months of 2014, reflecting the accesses base growth and its higher quality, with a greater weight of contract and smartphone customers. At the same time, these customers underpinned the performance of data traffic (+70% in the first nine months of 2014 in comparison to the figure as at 30 September 2013).
- ARPU growth accelerated to +2.1% year-on-year for the first nine months of 2014, primarily due to the increased growth in data ARPU (+25.3% year-on-year in the first nine months of 2014), that enabled to offset the negative effect of the reduction in termination rates applied from October 2013.

Regarding commercial activity in the fixed business:

- Traditional fixed accesses totalled 2.7 million at 30 September 2014 (-3% year-on-year), with a net loss of 52 thousand in the first nine months of the year, due to lower commercial activity and in spite of the stability in the level of churn.
- Retail broadband accesses reached 1.5 million at 30 September 2014 (+6% year-on-year), after posting net additions of +72 thousand customers in the first nine months of 2014, with an ongoing repositioning and acquisition of customers towards higher-speed plans. Accordingly, 70% of accesses have speed plans of 4 Mbps or more as at 30 September 2014 (+31 percentage points year-on-year).
- Pay TV accesses stood at 889 thousand customers at the end of September 2014 (-2% year-on-year), with an improvement in the volume of gross additions (+5% year-on-year). This improvement is the result of the momentum of high definition channels, the exclusive content offer and the new commercial proposals for expanding the service, through bundled services jointly with broadband starting at 1 Mbps.

Colombia

TELEFÓNICA COLOMBIA ACCESSES	September		% Chg
	2013	2014	
	<i>Unaudited figures (thousands)</i>		
Final Clients Accesses	14,247.6	15,403.9	8.1
Fixed telephony accesses ⁽¹⁾	1,445.8	1,468.6	1.6
Internet and data accesses	836.2	952.9	14.0
Narrowband	8.5	8.5	(0.6)
Broadband ⁽²⁾	827.7	944.5	14.1
Mobile accesses	11,633.5	12,581.6	8.1
Prepay	8,369.6	9,313.3	11.3
Contract	3,263.8	3,268.3	0.1
M2M	372.4	421.5	13.2
Pay TV	332.1	400.8	20.7
Wholesale Accesses	3.3	1.9	(41.1)
Total Accesses	14,250.9	15,405.9	8.1

Note:

⁽¹⁾ PSTN (including Public Use Telephony) x1; ISDN Basic access x1; ISDN Primary access; 2/6 Digital Access x30. Company's accesses for internal use included. Voice fixed wireless accesses included.

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

COLOMBIA SELECTED MOBILE BUSINESS OPERATING DATA	September		% Chg Local Cur
	2013	2014	
	<i>Unaudited figures</i>		
Voice Traffic (Million minutes)	14,818.5	16,735.2	12.9
ARPU (EUR)	6.9	6.3	(0.4)

Note:

- ARPU: monthly average revenue divided by the monthly average accesses of the period.
- Voice traffic is defined as minutes used by the company customers, both outbound and inbound. On-net traffic is only included once (outbound), and promotional traffic is included. Traffic not associated to the Company's mobile customers (roaming-in, MVNOs, interconnection of third parties and other business lines) is excluded. Traffic volume non rounded.

As at 30 September 2014, Telefónica Colombia managed 15.4 million accesses (+8% year-on-year).

Operating highlights in the mobile business for the nine months ended 30 September 2014 included:

- Mobile accesses stood at 12.6 million, up 8% compared to September 2013, primarily fostered by the good performance of the prepay segment (+11% year-on-year) following the launch of new data plans and per-second rates, and the stability of accesses in the contract segment. Smartphones amounted to 4.1 million accesses (almost doubling year-on-year), with a penetration rate of 35% (+14 percentage points year-on-year).
- Net additions reached 460 thousand accesses for the first nine months of 2014 in comparison to -70 thousand accesses as at 30 September 2013.
- Voice traffic increased +13%, and data traffic increased by +33% year-on-year for the first nine months of 2014, driven by the Telefónica Colombia's focus on data services expansion.
- ARPU decreased -0.4% year-on-year in the first nine months of 2014 due to the negative impact of termination rates cut. This was partially offset by data ARPU growth (+7.1% in the first nine months of the 2014 in comparison to the results for the same period in 2013).

Regarding commercial activity in the fixed business as at 30 September 2014:

- Traditional fixed accesses reached 1.5 million as at 30 September 2014 (+2% year-on-year), and posted net additions of 22 thousand in the first nine months of 2014 as a result of the focus on bundling services.

- Retail broadband accesses stood at 944 thousand (+14% year-on-year) following net additions of 91 thousand accesses in the first nine months of the year.
- Pay TV accesses stood at 401 thousand as at 30 September 2014, an increase of 21% year-on-year, after registering net additions of 17 thousand accesses (+53 thousand accesses in the first nine months of 2014) underpinned by the launch of high definition channels and by the enhanced interactive applications.

Mexico

TELEFÓNICA MEXICO ACCESSES	September		% Chg
	2013	2014	
	<i>Unaudited figures (thousands)</i>		
Mobile accesses.....	19,145.8	20,561.0	7.4
Prepay ⁽¹⁾	17,662.4	19,127.6	8.3
Contract.....	1,483.4	1,433.4	(3.4)
M2M.....	333.0	362.1	8.7
Fixed wireless ⁽²⁾	1,476.3	1,540.4	4.3
Total Accesses.....	20,622.1	22,101.5	7.2

Note:

⁽¹⁾ In the first quarter of 2014, 1.9 million thousand inactive accesses were disconnected.

⁽²⁾ In the first quarter of 2014, 45 thousand inactive accesses were disconnected.

MEXICO SELECTED MOBILE BUSINESS OPERATING DATA	September		% Chg Local Cur
	2013	2014	
	<i>Unaudited figures</i>		
Voice Traffic (Million minutes).....	14,394.0	21,803.5	51.5
ARPU (EUR) ⁽¹⁾	5.2	4.9	0.7

Note:

- ARPU: monthly average revenue divided by the monthly average accesses of the period.

- Voice traffic is defined as minutes used by the company customers, both outbound and inbound. On-net traffic is only included once (outbound), and promotional traffic is included. Traffic not associated to the Company's mobile customers (roaming-in, MVNOs, interconnection of third parties and other business lines) is excluded. Traffic volume non rounded.

⁽¹⁾ Impacted by the disconnection in the first quarter of 2014 of 1.9 million inactive accesses.

The implementation of the Federal Telecommunications and Broadcasting Law is reflected in the company's results as at 30 September 2014.

Since 14 August 2014, as part of the different regulatory measures approved, the differing rates charged by the preponderant operator and the remainder of competitors were ended, with the termination of the costs of calls on the preponderant operator's network being set at zero pesos.

Operating highlights in the mobile business for the nine months ended 30 September 2014 included:

- Accesses totalled 22.1 million at 30 September 2014, increasing 7% year-on-year, despite the disconnection of 1.9 million inactive accesses in the prepay segment and fixed accesses through Fixed Wireless technology in the first quarter of 2014.
- Mobile accesses stood at 20.6 million (+7% year-on-year), with net additions of 228 thousand accesses in the first nine months of the year (-22 thousand accesses in the same period of 2013), despite the impact of the disconnection of mobile customers mentioned above. This commercial recovery is driven by the sharp increase in gross additions (+45% year-on-year in the first nine months of 2014) as a result of the commercial repositioning undertaken in the fourth quarter of 2013, and following the expansion and improvement of both network capacity and coverage and distribution channel.
- Prepay accesses grew by 8% year-on-year at September 2014, and the customer base that tops up frequently by 23% year-on-year.

- Voice traffic grew by +51% year-on-year in the first nine months of 2014. In addition, the sharp increase of smartphone customers is reflected in data traffic, which maintained growth (3x year-on-year in the first nine month period of 2014).
- ARPU increased by +0.7% in the first nine months of 2014 driven by the increase in voice and data traffic.
- Fixed accesses through Fixed Wireless technology reached 1.5 million as at 30 September 2014 (+4% year-on-year), posting net additions of -18 thousand accesses in the first nine months of 2014, affected by the disconnection of 45 thousand accesses in the first quarter of 2014 mentioned above.

Venezuela & Centroamérica

VENEZUELA & CENTROAMERICA ACCESSES	September		% Chg
	2013	2014	
	<i>Unaudited figures (thousands)</i>		
Fixed telephony accesses ⁽¹⁾	1,445.2	1,361.8	(5.8)
Fixed wireless	1,194.6	1,128.7	(5.5)
Internet and data accesses	36.6	11.9	(67.3)
Narrowband	25.4	1.1	(95.8)
Broadband ⁽²⁾	5.0	5.1	1.1
Other ⁽³⁾	6.2	5.8	(5.9)
Mobile accesses	21,029.2	21,947.2	4.4
Prepay ⁽⁴⁾	18,892.5	19,721.3	4.4
Contract	2,136.7	2,225.9	4.2
M2M	112.9	134.9	19.6
Pay TV	337.6	472.8	40.1
Total Accesses	22,848.6	23,793.7	4.1

Note:

⁽¹⁾ PSTN (including Public Use Telephony) x1; ISDN Basic access x1; ISDN Primary access; 2/6 Digital Access x30. Company's accesses for internal use included. Voice fixed wireless accesses included.

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

⁽³⁾ Retail circuits other than broadband.

⁽⁴⁾ Includes prepay M2M accesses.

VENEZUELA & CAM SELECTED MOBILE BUSINESS OPERATING DATA	September		% Chg Local Cur
	2013	2014	
	<i>Unaudited figures</i>		
Voice Traffic (Million minutes).....	23,542.27	27,848.0	18.3
ARPU (EUR) ⁽¹⁾	11.4	8.8	22.5

Note:

- ARPU: monthly average revenue divided by the monthly average accesses of the period.

- Voice traffic is defined as minutes used by the company customers, both outbound and inbound. On-net traffic is only included once (outbound), and promotional traffic is included. Traffic not associated to the Company's mobile customers (roaming-in, MVNOs, interconnection of third parties and other business lines) is excluded. Traffic volume non rounded.

⁽¹⁾ For comparative purposes and in order to facilitate the interpretation of the year-on-year change versus 2013 results, the variation in local currency of the ARPU in Venezuela is reported excluding the impact of the hyperinflation adjustment.

Operating highlights in the mobile business for the nine months ended 30 September 2014 included:

- Accesses totalled 23.8 million at 30 September 2014, up 4% year-on-year, reaching 11.5 million in Venezuela (-3% year-on-year) and 12.3 million in Central America (+12% year-on-year).
- Mobile accesses stood at 21.9 million (+4% year-on-year). In Venezuela, accesses reached 10.3 million, down 4% year-on-year, (-243 thousand in the first nine months). In Central America, mobile accesses stood at 11.7 million (+13% year-on-year), with net additions of 523 thousand accesses in the first nine months of 2014.

- Smartphones with an attached data plan rose by 36% year-on-year to reach a penetration of 30% (+7 percentage points year-on-year), further consolidated as the main growth driver for accesses. In Venezuela, smartphones growth stood at 13% year-on-year, with a penetration of 47% of mobile accesses; +7 percentage points year-on-year.
- Churn stood at 2.9% in the first nine months of 2014, increasing by 0.2 percentage points year-on-year (+0.9 percentage points year-on-year), mainly due to higher prepay churn. Contract churn in the first nine months of 2014 remained at similar levels year-on-year (1.2%).
- Voice traffic maintained a strong growth in the first nine months of 2014 (+18% year-on-year), underpinned by the growth in the customer base and higher usage per customer. Data traffic continued showing a positive trend advancing 53% in the first nine months of 2014.
- Pay TV accesses in Venezuela reached 473 thousand at 30 September 2014 (+40% year-on-year), following net additions of +87 thousand in the first nine months of 2014.

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 in 2014 include the following:

- *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 chronic patients, 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*: set of facilities and elements allowing the protection of physical assets (electronic security), in order to guarantee the safety of, amongst other things, roads, malls, airports, prisons, railways; and information assets (information security), focused to protect the access to PCs, laptops, smartphones, servers, communication pipes (amongst other things) in addition to the information stored inside and the identity of the end customer
- *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).
- *Advertising*: advertising products based on SMS and IT Technologies such as SMS campaigns or bulk SMS sales to corporations, banners, mobile portals and any other advertising related activities.

- *Big Data*: revenues generated from the sale of Smart Steps (crowd analytics) split between Retail and Transport sectors. Smart Steps provide insights based on the behaviour of crowds.

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 towards stimulating usage, including segmented packages and innovative tariff options; and initiatives that are responsive to the latest market trends, including those aimed towards 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 subsidised handsets.

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 major 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.

On 10 November 2014, within the framework of the proactive management of its asset portfolio and financial flexibility optimisation, Telefónica, through its 100% subsidiary, Telefónica Internacional, S.A.U., proceeded to the sale of 597,844,100 shares of China Unicom, representing 2.5% of the share capital of the company, by a block trade process, at a price of HK\$11.14 per share, for a total amount of HK\$6,660 million, approximately €687 million at the exchange rate as at the date of the sale.

Further to the sale, Telefónica maintains its commitment to the strategic alliance with China Unicom.

As of the date of this Prospectus, Telefónica's shareholding in China Unicom amounts 2.51% 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 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 Reals, 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.

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.

On 16 June 2014, the three Italian shareholders of Telco requested the initiation of the process of "demerger" (spin off) of the company, as provided in the shareholders agreement. Implementation of the demerger, approved by the General Meeting of Shareholders of Telco held on 9 July 2014, remains subject to obtaining the required anti-trust and telecommunications approvals (including those from Brazil and Argentina). Once the aforementioned approvals are obtained, this decision will be implemented by transferring all the current stake of Telco in Telecom Italia to four newly created companies. The share capital of each of these companies will belong in its entirety to each of the shareholders of Telco and each of these companies will receive a number of shares of Telecom Italia proportional to the current economic stake in Telco of each respective shareholder.

The application process of the aforementioned anti-trust and telecommunications approvals (including those in Brazil and Argentina) to proceed to the "demerger" (spin off) of Telco started, once the corresponding corporate documents were entered into in Italy.

Furthermore, on 24 July 2014, Telefónica issued €750 million bonds mandatorily exchangeable into ordinary shares of Telecom Italia maturing on 24 July 2017, representing, as of that date, 6.5% of its current voting share capital. The bonds may be exchanged in advance of the transfer of the shares, except under certain circumstances where the company may opt to redeem the bonds in cash. As a result of this transaction, Telefónica, after the Telco demerger and the later transfer of the underlying shares of the bonds, will reduce its stake in Telecom Italia which will be between 8.3% and 9.4% in Telecom Italia current voting share capital.

It is also significant that, within the framework of the GVT transaction, (see "*Description of the Guarantor - Introduction*" above) on 18 September 2014, Vivendi, S.A. accepted Telefónica's offer to acquire 1,110 million ordinary shares of Telecom Italia (which represented, as at such date, a stake of 8.3% of Telecom Italia voting share capital and 5.7% of its total share capital) in exchange of 4.5% of the share capital of Telefónica Brasil, S.A. after its combination with GVT, which represent all the ordinary shares and a portion of the preferred shares (representing 0.7% of such class of shares) in Telefónica Brasil, S.A. that Vivendi, S.A. will receive as a consequence of the GVT transaction.

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 the appeal on 5 January 2011. On 23 April 2013, Telefónica was notified of 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.

On 10 July 2014 the European Union Court of Justice dismissed the appeal, maintaining the fine imposed for abuse of dominant position (margin squeeze) on wholesale prices charged by Telefónica and Telefónica de España, S.A.U., for broadband access in Spain. This ended the appeal process.

The fine was satisfied with no impact on the profit and loss account due to the amount having already been provisioned by Telefónica.

*Appeal against the decision by 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 Telefónico 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 Reals (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 Reals (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.

Judicial appeals against the decisions by the Conselho Administrativo de Defesa Econômica (CADE) regarding the acquisition by Telefónica, S.A. of stakes in Portugal Telecom and Telco

On 4 December 2013, the Brazilian Antitrust Regulator, 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. ("**Vivo**):

- (a) The entry of a new shareholder in Vivo, sharing the control of Vivo with Telefónica 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 Reals, 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 increase. This decision also requires Telefónica to divest such non-voting shares of Telco.

The fine imposed by CADE on Telefónica, S.A. relates to the agreement reached on 24 September 2013 between Telefónica and the other shareholders of the Italian company Telco (which holds a 22.4% stake with voting rights of Telecom Italia) whereby Telefónica subscribed and paid out a share capital increase in Telco, through a cash contribution of €324 million, in exchange for shares with non-voting rights in Telco. As a result of this capital increase, the interest held by Telefónica in the voting share capital of Telco remains unchanged (46.18%), although its interest in the total share capital of Telco stands at 66%.

On 9 July 2014, Telefónica filed a judicial appeal against both decisions, requesting they be overturned citing numerous procedural improprieties (the rulings were issued before Telefónica presented its allegations) and a clear lack of legal grounds. At the same time, it requested the decisions be rendered null as CADE has not provided any proof that Telefónica's actions undermine competition or infringe on applicable legislation. In this respect, the decision regarding the acquisition by Telefónica of PT Companies' indirect stake in Vivo Participações, S.A. was issued three years after the deal was approved by ANATEL. The transaction was completed - prior approval by the CADE was not required at the time - immediately after ANATEL's approval on 27 September 2010.

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.

With regards to the tax litigation currently being pursued by the Telefónica Group companies in Peru, the courts did not hand down any final ruling during the first half of 2014 that would alter the classification given to these lawsuits.

In the case in which Telefónica del Perú, S.A.A. is questioning the legality of the fine imposed by the Peruvian tax authority (*La Superintendencia Nacional de Aduanas y de Administración Tributaria*) (SUNAT) in relation to payments on account for financial year 2000, precautionary measures have been requested, for which a counter-measure (*contracautela*) for the sum of €105 million will have to be posted. Further precautionary measures for a combined total of €357 million had already been obtained as of 31 December 2013.

Furthermore, Telefónica del Perú, S.A.A. has requested SUNAT to return the amounts it had unduly charged in 2012 and 2013. This request finds support in the rulings of the Peruvian Tax Court (*Tribunal Fiscal*) which, marking an end to the complaint proceedings instituted by Telefónica del Perú, S.A.A., found that the amounts in question did not constitute valid and enforceable tax debts.

As at 30 June 2014 the Group has assessed the situation with respect to all tax inspections outstanding, and does not expect that the conclusion thereof would give rise to the need to recognise any material liabilities in the Group's condensed consolidated interim 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%
Fundación Bancaria 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 twelve 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	69	1997	2017
Vice-chairmen				
Mr. Isidro Fainé Casas ⁽¹⁾⁽²⁾	10/07/1942	72	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	66	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	70	2001	2016
Mr. Peter Erskine ⁽¹⁾⁽⁷⁾⁽⁸⁾⁽⁹⁾	10/11/1951	63	2006	2016
Mr. Santiago Fernández Valbuena	22/04/1958	56	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	68	2008	2018
Mr. Gonzalo Hinojosa Fernández de Angulo ⁽¹⁾⁽⁴⁾⁽⁵⁾⁽⁶⁾⁽⁸⁾⁽⁹⁾⁽¹⁰⁾	10/07/1945	69	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	60	1995	2016
Mr. Ignacio Moreno Martínez ⁽³⁾⁽⁴⁾⁽⁶⁾⁽¹⁰⁾	30/07/1957	57	2011	2017
Mr. Francisco Javier de Paz Mancho ⁽¹⁾⁽⁵⁾⁽⁶⁾⁽¹⁰⁾	24/07/1958	56	2007	2018
Mr. Chang Xiaobing ⁽¹¹⁾	27/03/1957	57	2011	2016

- (1) Member of the Executive Commission of the Board of Directors.
(2) Nominated by Fundación Bancaria 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) Chairman of the Consejo Empresarial de la Competitividad (Business Competitiveness Council). Trustee of Fundación Bancaria Caja de Ahorros y Pensiones de Barcelona ("la Caixa").
Isidro Fainé Casas	Vice Chairman of Telefónica, S.A.	Chairman of Fundación Bancaria Caja de Ahorros y Pensiones de Barcelona ("la Caixa") Chairman of CaixaBank, S.A. Chairman of Criteria Caixaholding, S.A. Vice Chairman 1° of Abertis Infraestructuras, S.A. Chairman of Confederación Española de Cajas de Ahorros Vice Chairman 1° of Repsol, S.A. Director of Banco Português de Investimento, SA (BPI) Vice Chairman 2° 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

Name	Principal activities inside the Group	Principal Activities outside the Group
		Member of the Consejo Empresarial de la Competitividad (Business Competitiveness Council)
		Non-executive president of Metrovacesa, S.A.
Ignacio Moreno Martínez	Director of Telefónica, 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.	Substitute Director of BBVA Bancomer, S.A.
	Director of Telefónica Móviles México, S.A. 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 Independent Director of MDF Family Partners Chairman of Haugron Holdings S.L. Independent 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 Director of BRF, S.A. Director of AGCO Corporation Member of the Consultative Board of Abertis Infraestructuras S.A. Member of the Global Ocean Commission.
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.	Vice-President of CaixaBank, S.A. Director of Sociedad de Gestión de Activos Inmobiliarios procedentes de la Reestructuración Bancaria (SAREB). Chairman of Barcelona Digital Centre Tecnologic Non-executive Chairman of CECA BANK Director of Bousorama S.A. Director of Mediterranea Beach & Golf Community, S.A. Member of the Plenary of the Chamber of Commerce of Barcelona. Member of the Euro Retail Payments Board (ERPB).
Francisco Javier de Paz Mancho	Director of Telefónica, S.A. Director of Telefónica de Argentina, S.A. Director of Telefónica Brasil, S.A. Chairman of Telefónica Gestión de Servicios Compartidos, S.A.U.	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

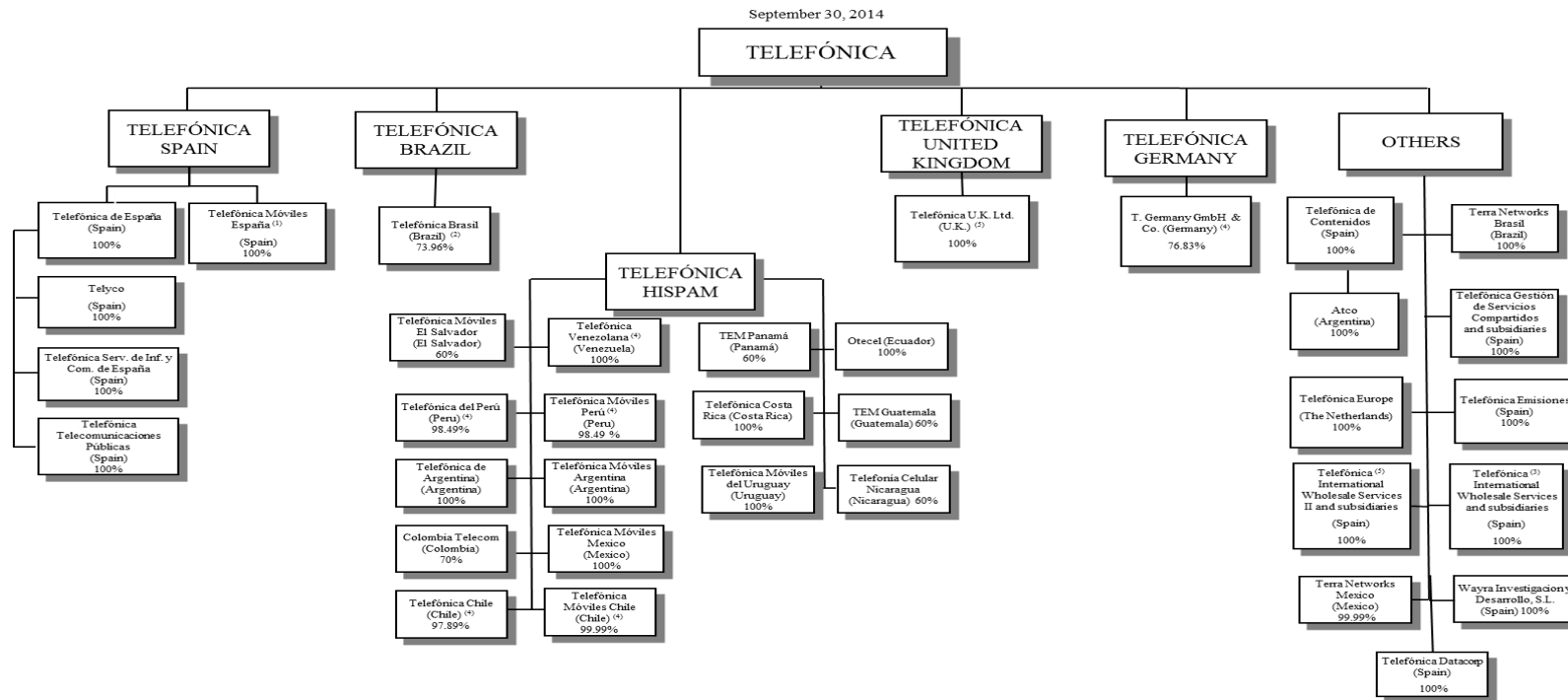
Name	Principal activities inside the Group	Principal Activities outside the Group
		Limited Executive Chairman of China Unicom (Hong Kong) Limited Chairman of China United Network Communications Corporation Limited

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 30 September 2014, 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.

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.

With respect to references in Section 2 of this summary to an individual who has elected to be treated as resident in the Netherlands for the relevant tax purposes, it is noted that as per 1 January 2015, the election regime will be replaced by a mandatory qualification as a 'qualifying foreign taxpayer' on the basis of certain objective criteria.

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 and capital gains 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 and capital gains derived from the Securities at rates up to 52 per cent if:

- (i) the income and capital gains are attributable to an enterprise from which the holder derives profits (other than as a shareholder); or
- (ii) the income and capital gains qualify 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 and capital gains 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 and capital gains derived from the Securities unless:

- (i) the income and capital gains are 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 and capital gains 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 One of Law 10/2014 (as defined in the Conditions of the Securities) shall apply to the Securities according to its Section 8, provided that the Securities are issued by a company which is (i) tax resident in the European Union and (ii) whose voting rights are completely held directly by an entity which is resident in Spain for tax purposes.

The Guarantor will comply with the reporting obligations set out in Section 4 of Additional Provision One of Law 10/2014 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 One of Law 10/2014 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 issuer (that is, the Guarantor with respect to any payments of interest under the Guarantee) 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 issuer (that is, the Guarantor with respect to any payments of interest under the Guarantee) 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 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 (as at the date of this Prospectus, 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 One of Law 10/2014 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 Securities.

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 Council of the European Union formally adopted a Council Directive amending the Directive on 24 March 2014 (the "**Amending Directive**"). The Amending Directive broadens the scope of the requirements described in the first paragraph above. Member States have until 1 January 2016 to adopt the national legislation necessary to comply with the Amending Directive and are required to apply these new requirements from 1 January 2017. The changes made under the Amending Directive include extending the scope of the Directive to payments made to, or collected for, certain other entities and legal arrangements. They also broaden the definition of "interest payment" to cover income that is equivalent to interest.

The proposed financial transactions tax ("FTT")

On 14 February 2013, the European Commission published a proposal (the "**Commission's Proposal**") for a Directive for a common FTT in Belgium, Germany, Estonia, Greece, Spain, France, Italy, Austria, Portugal, Slovenia and Slovakia (the "**participating Member States**").

The Commission's Proposal has very broad scope and could, if introduced, apply to certain dealings in the Securities (including secondary market transactions) in certain circumstances.

Under the Commission's Proposal 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. A financial institution may be, or be deemed to be, "established" in a participating Member State in a broad range of circumstances, including (a) by transacting with a person established in a participating Member State or (b) where the financial instrument which is subject to the dealings is issued in a participating Member State.

A joint statement issued in May 2014 by ten of the eleven participating Member States indicated an intention to implement the FTT progressively, such that it would initially apply to shares and certain derivatives, with this initial implementation occurring by 1 January 2016.

The FTT proposal remains subject to negotiation between the participating Member States. It may therefore be altered prior to any implementation. Additional EU 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

Barclays Bank PLC, BNP Paribas, J.P. Morgan Securities plc, Société Générale and UniCredit Bank AG (the "**Joint Bookrunners**") have, in a subscription agreement dated 28 November 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 21 November 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 November 2014, by a resolution of the Board of Directors of the Guarantor dated 30 May 2014, and by a resolution of the shareholders acting through the General Shareholders' Meeting of the Guarantor dated 30 May 2014.

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 17 of this Prospectus, and under "*Description of the Guarantor - Legal Proceedings*" on pages 87 – 91 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 of the Issuer, and since 30 June 2014 there has been no significant change in the financial or trading position of the Issuer save for the repayment by the Issuer on 31 October 2014 of GBP 100 million of its syndicated loan (tranche E2) dated 2 March 2012. Since 31 December 2013 there has been no material adverse change in the prospects of the Guarantor and the Group, and since 30 September 2014 there has been no significant change in the financial or trading position of the Guarantor and the Group, save for on 17 October 2014, Telefónica Emisiones S.A.U. issued fifteen-year notes in an aggregate principal amount of €800 million under its Guaranteed Euro Programme for the Issuance of Debt Instruments (EMTN Programme) filed with the Financial Conduct Authority (FCA) in London on 10 June 2014. These notes are guaranteed by the Guarantor.

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 the unaudited interim financial statements of the Issuer for the six months ended 30 June 2014; and
- (e) the audited consolidated financial statements of the Guarantor for the years ended 31 December 2013 and 2012, the unaudited but reviewed condensed consolidated interim financial statements of the Guarantor for the six months ended 30 June 2014 and the interim management statement for the first nine months of 2014.

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 Securities will be 4.200% per annum. The yield is calculated at the Issue Date on the basis of the Issue Price and 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 5 December 2014, subject to the issue of the Temporary Global Security.

Fees

- 9. The estimated costs and expenses in relation to admission to trading are £4,200.

ISIN and Common Code

- 10. The Securities have been accepted for clearance through Euroclear and Clearstream, Luxembourg. The ISIN is XS1148359356 and the common code is 114835935.

**REGISTERED AND HEAD
OFFICE OF THE ISSUER**

Telefónica Europe B.V.
Zuidplein 112, H Tower
1077 XV, Amsterdam
The Netherlands

**REGISTERED AND HEAD
OFFICE OF THE GUARANTOR**

Telefónica, S.A.
Gran Vía, 28
28013 Madrid
Spain

FISCAL AGENT

The Bank of New York Mellon, London Branch
One Canada Square
London E14 5AL
United Kingdom

THE JOINT BOOKRUNNERS

Barclays Bank PLC
5 The North Colonnade
Canary Wharf
London E14 4BB
United Kingdom

BNP Paribas
10 Harewood Avenue
London NW1 6AA
United Kingdom

J.P. Morgan Securities plc
25 Bank Street
Canary Wharf
London E14 5JP
United Kingdom

Société Générale
29, boulevard Hausmann
75009 Paris
France

UniCredit Bank AG
Arabellastrasse 12
D-81925 Munich
Germany

LEGAL ADVISORS

To the Issuer and the Guarantor as to English and Spanish law: *To the Issuer and the Guarantor as to Dutch law:*

Clifford Chance, S.L.
Paseo de la Castellana, 110
28046 Madrid
Spain

Clifford Chance LLP
Droogbak 1A
1013 GE Amsterdam
The Netherlands

To the Joint Bookrunners as to English and Spanish law:

To the Joint Bookrunners as to Dutch law:

Linklaters, S.L.P.
Almagro 40
28010 Madrid
Spain

Linklaters LLP
World Trade Centre Amsterdam
Tower H, 22nd Floor
Zuidplein 180
1077 XV, Amsterdam
The Netherlands

AUDITORS TO THE ISSUER

Ernst & Young Accountants LLP
Antonio Vivaldistrat 150
1083 HP, Amsterdam
The Netherlands

AUDITORS TO THE GUARANTOR

Ernst & Young, S.L.
Torre Picasso, Plaza Pablo Ruiz Picasso, 1
28020 Madrid
Spain