



Telefónica Europe B.V.

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

**EUR 1,000,000,000 Undated 5.5 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 1,000,000,000 Undated 5.5 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 3.750% per annum from (and including) the Issue Date to (but excluding) the First Reset Date (as defined in the Conditions) payable annually (except for a short first Interest Period) in arrear on 15 March in each year, with the first Interest Payment Date on 15 March 2017; 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) 15 March 2027, 3.858 per cent. per annum; (B) in respect of the period commencing on 15 March 2027 to (but excluding) 15 March 2042, 4.108 per cent. per annum; and (C) from and including 15 March 2042, 4.858 per cent. per annum, all as determined by the Agent Bank, payable annually in arrear on 15 March in each year (each, an Interest Payment Date as defined in the Conditions), commencing on 15 March 2023.

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, US 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 BB+ 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

BNP PARIBAS
Citigroup
Société Générale Corporate & Investment Banking
UniCredit Bank

BofA Merrill Lynch
Commerzbank
The Royal Bank of Scotland

9 September 2016

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IMPORTANT NOTICES

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

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

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

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

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

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

In particular, the Securities have not been and will not be registered under the Securities Act and are subject to United States tax law requirements. Subject to certain exceptions, Securities may not be offered, sold or delivered within the United States or to US 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 "**US\$**", and "**US 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 Citigroup Global Markets Limited the "Stabilisation Manager" (or persons acting on behalf of the Stabilisation Manager may over-allot Securities or effect transactions with a view to supporting the market price of the Securities at a level higher than that which might otherwise prevail. However, stabilisation may not necessarily occur. 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 cease 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 Stabilisation Manager (or person(s) acting on behalf of the Stabilisation 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. A single fixed customer may contract for multiple services, and Telefónica believes that it is more useful to count the number of accesses a customer has contracted for, than to merely count the number of its customers. For example, a customer that has fixed line telephony service and broadband service is counted as two accesses rather than as one customer.

"**ARPU**" is the average revenues per user per month. ARPU is calculated by dividing total gross service revenues (excluding inbound roaming revenues) from sales to customers for the preceding 12 months by the weighted average number of accesses for the same period, and then dividing by 12.

"**Bundles**" refer to combination products that combine fixed services (wirelines, broad bands and television) and mobile services.

"**Churn**" is the percentage of disconnections over the average customer base in a given period.

"**Cloud computing**" is the delivery of computing as a service rather than a product, whereby shared resources, software and information are provided to computers and other devices as a utility over a network (typically the Internet).

"**Commercial activity**" includes the addition of new lines, replacement of handsets and migrations.

"**Data ARPU**" is the average data revenues per user per month. Data ARPU is calculated by dividing total data revenues (from sources such as Short Message Service ("**SMS**"), Multimedia Messaging Services ("**MMS**"), other mobile data services such as mobile connectivity and mobile Internet, premium messaging, downloading ringtones and logos, mobile mail and wireless application protocol ("**WAP**") connectivity from sales to customers for a given period by the weighted average number of accesses for the same period, and then dividing by the relevant period.

"**Data revenues**" include revenues from SMS, MMS, other mobile data services such as mobile connectivity and mobile Internet, premium messaging, downloading ringtones and logos, mobile mail and WAP connectivity from sales to customers.

"**Data traffic**" includes all traffic from Internet access, messaging (SMS, MMS) and connectivity services that is transported by the networks owned by Telefónica.

"**FaaST**" is a cybersecurity technology that scans an organisation's system 24 hours a day, seven days a week, in order to prevent cybernetic attacks.

"**Final client accesses**" means accesses provided directly to residential and corporate clients.

"**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 the purpose of calculating Telefónica's number of fixed line accesses, Telefónica multiplies its lines in service as follows: PSTN (x1); basic ISDN (x1); primary ISDN (x30, x20 or x10); and 2/6 digital accesses (x30).

"**Fixed termination rates**" is an established fixed network tariff that applies when a customer makes a call to someone in a network operated by another operator.

"**FTTx**" is a generic term for any broadband network architecture that uses optical fiber to replace all or part of the metal local loop.

"**Gross adds**" means the gross increase in the customer base measured in terms of accesses in a period.

"**HDTV**" or "**high definition TV**" has at least twice the resolution of standard definition television (SDTV), allowing it to show much more detail than an analog television or digital versatile disc (DVD).

"**Incoming revenues**" refers to the interconnection revenues derived from the completion of calls made from outside mobile or fixed carriers into Telefónica's network.

"**Interconnection revenues**" means revenues received from other operators which use Telefónica's networks to connect to or finish their calls and SMS or to connect to their customers.

"**Internet and data accesses**" include broadband accesses (including 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 the remaining non-broadband final customer circuits. Internet and data accesses also include "Naked ADSL", which allows customers to subscribe for a broadband connection without a monthly fixed line fee.

"**IPTV**" (Internet Protocol Television) refers to distribution systems for television subscription signals or video using broadband connections over the IP protocol.

"**ISP**" means Internet service provider.

"**IT**", or information technology, is the acquisition, processing, storage and dissemination of vocal, pictorial, textual and numerical information by a microelectronics-based combination of computing and telecommunications.

"**Latch**", is a cybernetic application, protecting accounts and on-line services.

"**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.

"**Market share**" is the percentage ratio of the number of final accesses or operator revenues over the existing total market in an operating area.

"**Metashield**" is a cybernetic product for protecting metadata (information on data) in digital documents and archives.

"**Mobile accesses**" includes accesses to the mobile network for voice and/or data services (including connectivity). Mobile accesses are categorised into contract and pre-pay accesses.

"**Mobile broadband**" includes Mobile Internet (Internet access from devices also used to make voice calls such as 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).

"**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 a determined tariff to such mobile network operator for using the infrastructure to facilitate coverage to their customers.

"**Net adds**" means the number of new accesses in a certain period.

"**Non SMS data revenues**" means data revenues excluding SMS revenues.

"**OTT services**" or "**over the top services**" means services provided through the Internet (such as television).

"**Outgoing revenues**" refers to mobile voice or data revenues (SMS, MMS) derived from Telefónica's consumers' consumed service.

"**P2P SMS**" means person to person short messaging service (usually sent by mobile customers).

"**Pay-TV**" includes cable TV, direct to home satellite TV, or DTH, and Internet Protocol TV, or IPTV.

"**p.p.**" means percentage points.

"**Revenues**" means net sales and revenues from rendering of services.

"**Service revenues**" means revenues less revenues from handset sales. Service revenues are mainly related to telecommunications services, especially voice revenues and data revenues (SMS and data traffic download and upload revenues) 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.

"**Tacyt**" is a cybersecurity tool that supervises, stores, analyses, correlates and classifies mobile applications.

"**Unbundled 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 ULL) or only DSL service (shared unbundled loop, "shared ULL").

"**Voice Traffic**" means voice minutes used by Telefónica's customers over a given period, both outbound and inbound.

"**VoIP**" means voice over Internet protocol.

"**Wholesale accesses**" means accesses Telefónica provides to its competitors, who then sell services over such accesses to their residential and corporate clients.

"**Wholesale ADSL**" means accesses of broadband or fiber that Telefónica provides to its competitors, who then sell services over such accesses to their residential and corporate clients.

In this Prospectus certain comparisons are made in local currency or on a "constant Euro basis" or "excluding foreign exchange rate effects" in order to present an analysis of the development of the Group's results of operations from year-to-year without the effects of currency fluctuations. To make comparisons on a local currency basis, financial items in the relevant local currency are compared for the periods indicated as recorded in the relevant local currency for such periods. To make comparisons on a "constant Euro basis" or "excluding foreign exchange rate effects," the relevant financial item is converted into Euro using the prior year's average Euro to relevant local currency exchange rate. In addition, certain financial information is presented excluding the effects of Venezuela being considered a hyperinflationary economy in 2012, 2013 and 2014 by eliminating all adjustments made as a result of such consideration.

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 to the Guarantor.

No regulation of the Issuer by any regulatory authority

The Issuer is not required to be licensed, registered or authorised under any current relevant laws in the Netherlands, and will operate without supervision by any authority in any jurisdiction. Regulatory authorities in one or more jurisdictions may decide, however, that the Issuer is subject to certain laws in such jurisdiction, which could have an adverse impact on the Issuer or the holders of Securities.

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 Telefónica which could affect its business, financial position, reputation, corporate image and brand and its results of operations, must be considered jointly with the information contained in its consolidated financial statements, and are as follows:

Risks relating to the Group

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

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

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.

Growth in Europe and financial stability may be affected by political uncertainty in some European countries due to upcoming general elections, a possible revival of the crisis in Greece, restructuring of the banking sector and due to the impact of steps taken towards an EU banking union and a capital markets union. In particular, the British exit process from the European Union following the vote to leave in the recent referendum, will require an adjustment of the economy to whatever new trade and investment relationships are put in place in the future, with the consequences in the meantime being uncertainty regarding investment, activity and the volatility of financial markets. In the first half of 2016, the

Telefónica Group obtained 25.1% of its revenues in Spain, 14.6% in Germany and 13.7% in United Kingdom.

In Latin America, there is an increasing exchange rate risk following the depreciation undergone by most currencies in this region throughout 2015, affected by the fall in commodity prices due to the uncertainties about growth in China, and the interest rate evolution in the United States, among other macroeconomic factors. Abrupt exchange rate movements could especially be triggered by scenarios characterised by high inflation and fiscal and external deficits. In this regard, it should be noted that the Venezuelan bolívar fuerte exchange rate quoted in the Sistema Marginal de Divisas (SIMADI) has experienced a depreciation in recent months in a context of high inflation figures, shortage of currencies and deep economic adjustment. In addition, the Argentine peso (which experienced a sharp depreciation in December 2015) is experiencing some depth constraints in its trading market, and the Brazilian real has strongly appreciated in the first half of 2016 partly reversing 2015's depreciation. Cash flows from countries in this region could decrease, and financial conditions could become more unfavourable if any of these elements were to worsen in the future.

Some of the most significant macroeconomic risk factors in the region affect Brazil, where there is a combination of high inflation, negative economic growth rates and significant internal and external financing needs. All these elements have led to new downgrades to the country's credit rating.

Moreover, the recent fall in oil prices and other commodity prices is having a negative impact on the external and fiscal accounts in Chile, Peru, Colombia, Mexico, and Ecuador (which has a dollarized economy, and is currently experiencing a lower supply of US dollars).

In Argentina, the new government is focused on resolving Argentina's macroeconomic and financial imbalances and on recovering international confidence. Although reforms taking place may have positive effects in the medium term, short term risks persist.

In Venezuela, after the parliamentary elections in which the Democratic Unity Roundtable (an opposition coalition to the ruling United Social Party of Venezuela) claimed the majority of seats in the National Assembly, a new economic emergency decree was announced which could increase state control of private businesses. In addition, there continues to be very limited access to US dollars.

At 30 June 2016, Telefónica Hispanoamérica and Telefónica Brazil represented 23.8% and 20.2% of the Telefónica Group's revenues, respectively. Moreover, approximately 28.6% of the Group's revenues in the telephony business were generated in countries that do not have investment grade status (in order of importance, Brazil, Argentina, Ecuador, Nicaragua, Venezuela, Guatemala, Costa Rica and El Salvador), and other countries are only one notch away from losing this threshold. As at 30 June 2016, the percentage of Telefónica's net financial debt in Latin American currencies stood at 13%.

"Country risk" factors include, among others, the following:

- unexpected adverse changes in regulation or administrative policies, including changes that modify the terms and conditions of licences and concessions and their renewal (or delay their approval);
- abrupt exchange-rate movements;
- expropriation or nationalisation of assets, adverse tax decisions, or other forms of state intervention;
- economic-financial downturns, political instability and civil disturbances; and
- maximum limits on profit margins imposed in order to limit the prices of goods and services through the analysis of cost structures (for example, in Venezuela, a maximum profit margin has been introduced that will be set annually by the Superintendence for Defense of Socioeconomic Rights).

Any of the foregoing may adversely affect the business, financial position, results of operations and cash flows of the Group.

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 June 2016, 46% of the Group's net debt (in nominal terms) was pegged to fixed interest rates for over a year, while 21% 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 June 2016: (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 €241 million, (ii) whereas a 100 basis points decrease in interest rates in all currencies (even if negative interest rates are reached), would lead to a reduction in financial expenses of €215 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 arising from a 10% depreciation of Latin American currencies against the US dollar and a 10% depreciation of other global currencies against the euro, excluding the pound sterling, would result in exchange losses of €42.6 million, primarily due to the weakening of the Venezuelan bolívar fuerte and, to a lesser extent, the Argentinean peso. These calculations were made assuming a constant currency financial position with an impact on profit or loss at 30 June 2016, including derivative instruments in place. However, in the case of the pound sterling, it would result in exchange profits of €39.5 million as a consequence of an option portfolio the Group entered into for the purpose of hedging a Brexit event, which matured in July 2016.

As at 30 June 2016, 21.2% of the Telefónica Group's operating income before depreciation and amortization (OIBDA) was concentrated in Telefónica Brazil and 21.9% in Telefónica Hispanoamérica.

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 Telefónica's strategic plan and new technologies, the renewal of licences or the expansion of the Telefónica Group's business in countries where it operates, may require a substantial amount of financing.

A decrease in the liquidity of Telefónica, a difficulty in refinancing maturing debt or raising new funds as debt or equity could force Telefónica to use resources allocated to investments or other commitments to pay its financial debt, which could have a negative effect on the Group's business, financial condition, results of operations and/or cash flows.

Funding could be more difficult and costly in the event of a significant deterioration of conditions in the international or local financial markets (especially considering the recent volatility resulting from uncertainties regarding China, the decline in commodity prices and the hikes in interest rates approved by the US Federal Reserve, all of which impact Latin America), or if there is an eventual deterioration in the solvency or operating performance of Telefónica, or as a consequence of a credit rating downgrade of Spanish sovereign risk by rating agencies.

At 30 June 2016, gross financial debt scheduled to mature in 2016 amounted to €6,385 million (which includes the net position of derivative financial instruments and certain current payables), and gross financial debt scheduled to mature in 2017 amounted to €8,407 million.

In accordance with its liquidity policy, Telefónica has fully covered its gross debt maturities for the next twelve months with cash and credit lines available at 30 June 2016. Telefónica's liquidity could be affected if market conditions make it difficult to renew existing undrawn credit lines, 10% of which, at 30 June 2016, were scheduled to mature prior to 30 June 2017.

In addition, given the interrelation between economic growth and financial stability, the materialisation of any of the economic, political and exchange rate risks referred to above could lead to a negative impact on the availability and cost of Telefónica's financing and its liquidity strategy; which could have a negative effect on the Group's business, financial condition, results of operations and/or cash flows.

Risks relating to the Group's Industry

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

The telecommunications sector is subject to laws and regulations in different countries, and additionally, many of the services the Group provides 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 those related to spectrum regulation and licences/concessions, rates, universal service regulation, regulated wholesale services over fiber networks, privacy, functional separation of businesses and network neutrality. The fact that the Group's business is highly regulated both affects its revenues and imposes costs on its operations.

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, potentially, 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.

In this regard, 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, service and coverage standards 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 licences

Further to the European Commission's new "Digital Single Market" (DSM) Strategy, Europe is expected to undergo an important review of its regulatory framework. The new European DSM Strategy comprises a series of policy initiatives to promote the development of the single market of digital services and networks. As a result, the European Commission has indicated it will initiate legislative processes, which could have significant implications, inter alia, for access to networks, spectrum use, auction conditions, duration and renewal of licenses, universal service, consumer protection, audiovisual services and platforms.

On 8 May 2015, the European Commission approved a decision on the harmonisation of the 1452 - 1492 MHz frequency band (1500 MHz band), which encourages Member States to designate and to make available this band frequency from November 2015 on a non-exclusive basis. As a result, new spectrum award processes are expected in the short and mid term across the EU. Germany and the United Kingdom have already auctioned the frequency band and therefore the decision will not have a material impact on Telefónica's cash flow in those markets. In Spain, the Government launched a consultation which ended on 21 June 2015 to evaluate demand for spectrum in the 1500 MHz band. The tender of the 1500 MHz band in Spain is not expected to take place before 2017.

Additionally, the European Parliament and Council are discussing the use and availability of the 700 MHz band. This could require new cash outflows from Telefónica between 2018 and 2022 in both the United Kingdom and Spain, where it is expected that the 700 MHz band will be available between 2020-2022. In Germany the 700 MHz band was already awarded in 2015.

On 7 March 2016, the German regulator initiated a public consultation with regards to the frequency distributions of the 2 GHz spectrum band granted to Telefónica Deutschland.

United Internet and the regional cable operator Airdata have filed complaints before the General Court against the EU decision allowing the merger between Telefónica Deutschland Holding AG and E-Plus. Telefónica Deutschland has been accepted as an interested party in these proceedings and filed its statements in both cases. United Internet has filed a second complaint against the EU Commission regarding the content of the self-commitment letter provided by Telefónica Deutschland with regard to the implementation of the Non-Mobile Network Operator Remedy. Telefónica Deutschland has requested to intervene upon which the General Court has not yet decided.

On 24 September 2015, the telecommunication regulator in the United Kingdom (Ofcom) issued a decision to increase the annual fees which mobile operators must pay for the use of 900 MHz and 1800 MHz spectrum. Accordingly, from 31 October 2015, the annual charge that Telefónica UK must pay is 32.2 million pounds sterling (increased from 15.6 million pounds sterling), rising to 48.7 million pounds sterling. This decision is subject to an appeal by EE Limited. Finally, following consultation, on 3 December 2015, Ofcom published an update stating that it would not conduct an auction procedure to award 2.3 GHz and 3.4 GHz spectrum before decisions were made by the relevant competition authorities, in relation to the proposed acquisition of Telefónica UK Limited by the Hutchison Whampoa Group. In July 2016, Ofcom announced that, following the European Commission's decision to block the proposed acquisition, it intends to publish a consultation in the autumn of 2016 concerning Competition measures and on further specifics regarding the auction of the 2.3 GHz and 3.4 GHz spectrum bands.

In Latin America, spectrum auctions are expected to take place implying potential cash outflows to obtain additional spectrum or to meet the coverage requirements associated with these licences. Specifically, the procedures expected to take place in 2016 are:

- *Costa Rica*: In December 2015, the Government of Costa Rica communicated its intention to auction 40 MHz in the 1800 MHz band and 30MHz in the 1900/2100 MHz band. The regulatory authority has the mandate to start the procedure to design the auction but no specific date has been set as at the date of this Prospectus.
- *Mexico*: The Federal Telecommunications Institute (*Instituto Federal de Telecomunicaciones* or "IFT") has proposed to auction spectrum in the 2500 MHz band by the end of 2017. In addition, and in light of the constitutional reform resulting from the "Pact for Mexico" political initiative, a wholesale network offering services in the 700 MHz band will be created under a Public-Private Partnership. On 29 January 2016, the SCT (*Secretaría de Comunicaciones y Transportes*) published the rules for the International Competitive Tender. On 18 March 2016, SCT amended the tender schedule. Participants must submit to the IFT the request for approval to participate in the auction no later than 1 August 2016. The rules state that the tender will be awarded on 28 September 2016, and commercial operations must begin no later than 31 March 2018.
- *Panama*: On 4 December 2015, the process of reallocation of the AWS band (140 MHz, 1710-1780 / 2110-2180 MHz) was announced. As of the date of this Prospectus, the date for a potential auction has not yet been set.
- *Uruguay*: The Government of Uruguay approved a resolution allowing for a spectrum auction for mobile services. The auction will contain 15 + 15 MHz in the "AWS Ext" spectrum band and 45 + 45 MHz in the 700 MHz spectrum band (of which 20 + 20 MHz of 700 MHz has been reserved for the National Telecommunications Administration, ANTEL). As of the date of this Prospectus, the date of auction has not been set.
- *Guatemala*: There is a possibility that the Guatemalan regulator allocates AWS and 2.6 GHz during 2016. As of the date of this Prospectus, the date for a potential auction has not been set.
- *Colombia*: In May 2015, the regulator published a consultation document for comment which analyses alternatives and other considerations regarding the structuring of the allocation process for radio spectrum in the 700 MHz bands (which is part of the "Digital dividend", being the set of frequencies that have been available to mobile communications services in the frequency bands traditionally used for television broadcast (700 MHz and 800 MHz) due to the migration from analogue TV to digital TV), 900 MHz, 1900 MHz and 2500 MHz for mobile services. The

Ministry of Information Technologies and Communications stated that it would publish the conditions in 2016, but the date of auction has not been set. Colombia has established spectrum caps for lower bands, which are currently set at 30 MHz, and Telefónica has 25 MHz in lower bands.

- *Venezuela*: The regulator has indicated the possibility of awarding spectrum in the 2600 MHz band (20 + 20 MHz) for 4G services, in the 1900 MHz band (5 + 5 MHz) for 3G services and in the 900 MHz band, also for 3G services, during 2016, although the regulator has not formally announced the commencement of the spectrum awarding process.

Further to the above, certain administrations may not have announced their intention to release new spectrum and may do so during the year. The above does not include processes announced via general statements by administrations, which involve bands not key to Telefónica's needs. Telefónica may also seek to acquire spectrum on the secondary market where opportunities might arise.

Risks relating to concessions and licences previously granted

In the state of São Paulo, Telefónica Brazil provides local and national long-distance Fixed Switched Telephony Service ("**STFC**") under the public regime, through a concession agreement, which is expected to remain in force until 2025. In accordance with current regulations, Telefónica Brasil informed the Brazilian regulatory authority (*Agencia Nacional de Telecomunicações* or "**ANATEL**") that the net value, as of 31 December 2015, of assets assigned to the provision of the STFC (which include, among others, switching and transmission equipment and public use terminals, external network equipment, energy equipment and system and operation support equipment) were estimated to total 7,856 million Brazilian reais. In principle, the assets assigned to the provision of the STFC are considered reversible assets; the scope of such reversibility is subject to a complex debate at different levels.

On 27 June 2014, as established in the concession agreement, ANATEL issued a public consultation for the revision of the concession agreement. Although definitive conditions (which might deal, among others, with the reversibility of assets, universalisation goals and, in general, the obligational regime of the concessionaire) were expected to be published during 2015, such publication has been postponed until the end of December 2016. On 8 April 2016, the Ministry of Communications published the Ordinance No. 1455 with a set of guidelines aimed to review the current model concerning the provision of telecommunications to be implemented by ANATEL. ANATEL is currently working on the new telecommunications model, which is aimed at reformulating the entire sector by establishing new rules for telecommunications services provisioning. The proposed new model focus on broadband expansion (instead of fixed telephony) and, therefore, would determine the redefinition of STFC concessions and the extinction of the reversible assets regime. In return, the former concessionaire would be committed to achieve broadband expansion goals. The new model is under discussion by the ANATEL and it is expected to be completed during the second half of 2016.

In Colombia, the ICT Ministry issued Resolution 597 on 27 March 2014, to renew 850 MHz/1900 MHz licenses for 10 additional years. The reversion of assets (other than radio frequencies, which it is clear must be returned) and its scope, has been discussed in the context of 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, and Law 1341 of 2009. Discussions on the matter concluded on 16 February 2016. The ITC Ministry has announced that it is going to convene the Arbitral Tribunal, after having filed a response to the claim. Alongside this, efforts continue to determine the conditions needed to reach a conciliation with the ITC Ministry.

In Peru, Telefónica has concessions for the provision of the fixed-line service until November 2027. In December 2013, Telefónica filed a partial renewal of these concessions for five more years. In December 2014 and May 2016, Telefónica also filed a renewal request for twenty more years in relation to a concession for the provision of local carrier service (which will otherwise expire on 24 December 2016) and one of the concessions to provide mobile-line services in provinces (which will otherwise expire on 1 June 2018), respectively. As of the date of this Prospectus, the decision of the Ministry of Transport and Communications (*Ministerio de Transportes y Comunicaciones*) in all such proceedings is still pending, however the concessions continue in force. In addition, on 20 June 2016, the concessions granted to Telefónica Multimedia S.A.C. and Star Global Com S.A.C. to provide cable broadcasting services were renewed for a further 19 and 20 year period, respectively, having commenced in March 2013.

Telefónica Móviles Chile, S.A. was awarded spectrum on the 700 MHz (2x10 MHz) band in March 2014. A claim was brought by a consumer organisation against the 700 MHz assignments which was rejected by the Court of Defense of Free Competition in a judgment of 24 July 2015 and the appeal before the Supreme Court submitted by the consumer organisation is still awaiting resolution. By judgment on 20 April 2016, the Supreme Court accepted the appeal presented by a consumer organisation and ordered the Court of first instance (Court of Defense of Free Competition) to judge the substance of the case (spectrum hoarding).

In El Salvador, the process of renewal of the Group's licenses, which expires in 2018, has been postponed.

In Ecuador, once the Group's concession for mobile services expires in 2023, the renewal of such concession or the granting of a new concession will be subject to negotiation with the Ecuadorian Government. If the Group fails to renew such concession or obtain a new concession, assets assigned to the provision of mobile services will revert to the State of Ecuador in exchange for a fee.

The Group's consolidated investment on 30 June 2016 in spectrum acquisitions and renewals amounted to €10 million. On 26 May 2016, Telefónica obtained 2x15 MHz, in the 700 MHz Band C auction in Peru for US\$315 million.

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

Regulation of wholesale and retail charges

The European Regulation 2015/2120 on Net Neutrality and Roaming was adopted on 25 November 2015. Under this regulation, from 30 April 2016, when its implementation becomes effective, until 15 June 2017, operators may charge users roaming within the EU an additional fee on their domestic prices for roaming calls, SMS and data services, subject to certain regulated limits. In particular, the surcharges allowed during this period are 0.05 euro/minute for calls, €0.02 per SMS sent and €0.05 per megabits data (excluding VAT). During this period, the sum of the domestic retail price and any such surcharge may not exceed 0.19 euro/minute for calls, €0.06 per SMS sent and €0.20 per megabits data. However, surcharges will not be permitted from 15 June 2017, onwards. However, in some circumstances, operators may apply an additional surcharge under a "fair use policy" which is expected to be adopted in December 2016. The impact of this measure is very difficult to quantify because it will depend on the elasticity of traffic to decreases in the rates charged.

The European Commission launched a public consultation (which closed on 7 June 2016) on the Termination Rates Recommendation (the "**TRR**") which encompasses fixed and mobile termination rates. The public consultation sought to evaluate the impact of the TRR on the termination markets and on the EU internal market. Secondly, it sought views on whether the regulatory approach towards termination rates should be maintained and/or amended. The results of this public consultation are expected to provide guidance to the Commission in the revision process of the 2009 TRR.

The decreases in wholesale MTRs in Europe are also noteworthy. In the United Kingdom, wholesale MTRs have been reduced to 0.503 pence per minute from 1 April 2016. A further cut of 3.1% (in real terms) will come into effect from 1 April 2017.

In Germany, on 24 April 2015, BNetzA adopted its final decision to slightly reduce MTRs. The new prices will gradually decrease from 0.0172 euro per minute to 0.0166 euro per minute from 1 December 2015, until the end of November 2016. This decision was based on a "Long-run Incremental Cost Plus" approach which takes account of common costs. On 18 May 2016, BNetzA published draft regulatory orders which anticipate that BNetzA will set the MTR which will become effective as of December 2016 on the basis of the "Pure Long-Run Incremental Cost" approach. This approach is recommended by the European Commission, which has already been implemented in almost all other EU Member States, and does not take account of common costs. There is consequently a risk that, with effect as of December 2016, MTRs will significantly decrease.

In Spain, on 1 July 2016, the Spanish National Regulatory and Competition Authority (*Comisión Nacional de los Mercados y la Competencia* or "**CNMC**") has launched a public consultation which proposes to eliminate within 6 months the obligations imposed on Telefónica, Vodafone and Orange in the mobile networks access market (Market 15). In addition, it has initiated the process of reviewing the prices of mobile termination, with a final decision expected to be adopted by the end of 2016. Additionally, in May 2015, the CNMC launched a public consultation on the analysis of the market for access and call origination on fixed networks. The CNMC has proposed to maintain the obligation of Telefónica to provide a wholesale interconnection offer and a wholesale line rental ("**WLR**"), both with cost-oriented prices. The scope of the WLR obligation is expected to broaden in order to include certain supplementary services for the business segment. The final decision is expected to be issued during the second half of 2016.

In Latin America, it is likely that MTRs will also be reduced in the short to medium term. For example, in Mexico, the IFT adopted the MTRs for 2015 at 0.2505 Mexican pesos per minute and for 2016 at 0.1869 Mexican pesos per minute which is consistent with the Pure LRIC model. As at the date of this Prospectus, the IFT has initiated proceedings to determine the MTRs for 2017.

Telefónica has appealed the decisions concerning the MTRs applicable from 2011 to 2016.

In Brazil, ANATEL has issued ex-ante regulations to ensure competition in the wholesale market, which includes reductions of the MTR. In this regard, the "Plano Geral de Metas de Competição", as amended by Resolution 649/2015, established that mobile termination fees are subject to successive yearly reductions from 2016 until 2019, when the definitive cost-oriented-model fees are expected to be in force (such Resolution has been challenged in courts without a definitive outcome as at the date of this Prospectus).

In Argentina, the new legal framework "*Argentina Digital*" provides the new regulator with the possibility to regulate the tariffs and prices of essential public services, wholesale services and those which the regulator determines, based on reasons of public interest on which the law does not set parameters. As a result, there may be a negative impact, depending on how the new regulator exercises its powers. In addition, until the Secretary of Communications determines that there is effective competition for telecommunications services, the "dominant" providers in the relevant areas (which include Telefónica de Argentina) must respect the maximum tariffs established in the general tariff structure.

Regulation of Universal Services

In September 2015, as a part of the DSM Strategy, the European Commission issued a public consultation on the review of the regulatory framework for electronic communications, including certain aspects of the Universal Service obligations. Depending on the outcome of this public consultation, the European Commission could initiate a legislative process, including both the potential inclusion of certain broadband speeds in its scope and a possible reduction of some of the current Universal Service obligations that are becoming obsolete. Depending on the terms that will be 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.

In Spain, the licences of Telefónica de España and Telefónica Telecomunicaciones Públicas (who both own public terminals) for the provision of Universal Services will expire on 31 December 2016. A new tender for the award of the provision of the Universal Services is expected in the second half of 2016.

In Brazil, a new version of the General Plan for Universalisation of Fixed Switched Telephony Services is currently being analysed by ANATEL. It is expected that its final version will be published by the end of December 2016, together with the new concession agreements.

Regulation of fiber networks

On 24 February 2016, the Spanish CNMC adopted a final Resolution on the wholesale broadband market regulation, which raises a geographical segmentation in competitive (66 cities, 34% of total population) and non-competitive areas. It is anticipated that this Resolution will last for at least four years. Its implementation is expected to result in a moderate increase of the current regulatory obligations of Telefónica in Spain, in terms of its granting of access to other operators to its fiber network and with

respect to certain aspects relating specifically to the business segment (high quality bitstream service for business customers with national coverage). This Resolution has been appealed by Telefónica España.

Regulations on privacy

In Europe, on 14 April 2016, the new General Data Protection Regulation ("**GDPR**") was formally adopted. The GDPR is expected to become effective in the first quarter of 2018. In general the Group believes the GDPR has reached a good balance between consumer protection in terms of privacy and innovation in new services (i.e. BigData Services). However, the GDPR will introduce administrative fines of up to 4% of an undertaking's annual global turnover for breaching the new data protection rules.

The European Commission is in the process of reviewing the current e-Privacy Directive which has been submitted for public consultation and is expected to produce a legislative proposal at the beginning of 2017. The impact is still uncertain, however, it is expected to lead to a more consistent and horizontal approach aimed at ensuring a level playing field and thus contributing to users trust and awareness.

In October 2015, the Court of Justice of the European Union declared invalid the Decision of the European Commission of 26 July 2002, known as the "Safe Harbor Agreement", relating to the transfer of personal data from the EU to the United States. Since November 2015, EU and US Authorities have been negotiating a new agreement to ensure a level of protection similar to that provided by the EU. Failure to reach this agreement could create difficulties in the provision of services which involve the flow of EU citizens' personal data to the US.

In Brazil, it is expected, in the near future, that the Personal Data Protection Act will be adopted. This could lead to further obligations and restrictions for operators in relation to the collection of personal data and its treatment. Bill 5276/2016, which establishes a set of rules for a personal data protection, is currently under debate in the Federal Congress and was submitted for public consultation at the end of June 2016.

In Peru, on 8 May 2015, the new Personal Data Protection Law came into force. In Ecuador, the Telecommunications Act (*Ley Orgánica de Telecomunicaciones*), adopted in February 2015, devotes a whole chapter to regulate the use of personal data.

Regulation of functional separation

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

Regulation of network neutrality

In Europe, the application of the net neutrality Regulation will be monitored by National Regulatory Authorities following guidance to be delivered by the European Regulatory Authority (BEREC) no later than 30 August 2016. This guidance could directly impact internet access service commercial practices (for example, zero rating offers) and it may limit network management practices or increase transparency requirements on the Internet Access Service.

Telefónica operates in Latin American countries where net neutrality is being implemented, such as Chile, Colombia, Mexico and Peru (where Osiptel published the Draft Regulation on Net Neutrality on 8 September 2015).

In Brazil, the President approved the Net Neutrality and Personal Data Protection Law (*Marco Civil*), on 11 May 2016. In Mexico, the IFT has scheduled a public consultation to be carried out in August 2016 in respect of the guidelines that will be issued regarding Net Neutrality. 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 on its business, financial condition, results of operations and cash flows.

The Telefónica Group is exposed to risks in relation to compliance with anti-corruption laws and regulations and economic sanctions programmes.

The Telefónica Group is required to comply with the laws and regulations of various jurisdictions where it conducts operations. In particular, the Group's international operations are subject to various anti-corruption laws, including the US Foreign Corrupt Practices Act of 1977 and the United Kingdom Bribery Act of 2010, and economic sanction programmes, including those administered by the United Nations, the European Union and the United States, including the US Treasury Department's Office of Foreign Assets Control. The anti-corruption laws generally prohibit providing anything of value to government officials for the purposes of obtaining or retaining business or securing any improper business advantage. As part of the Telefónica Group's business, it may deal with entities, the employees of which are considered government officials. In addition, economic sanctions programmes restrict the Group's business dealings with certain sanctioned countries, individuals and entities.

Although the Group has internal policies and procedures designed to ensure compliance with applicable anti-corruption laws and sanctions regulations, there can be no assurance that such policies and procedures will be sufficient or that the Group's employees, directors, officers, partners, agents and service providers will not take actions in violation of the Group's policies and procedures (or otherwise in violation of the relevant anti-corruption laws and sanctions regulations) for which the Group or they may be ultimately held responsible. Violations of anti-corruption laws and sanctions regulations could lead to financial penalties, exclusion from government contracts, damage to the Group's reputation and other consequences, that could have a material adverse effect on the Group's business, results of operations and financial condition.

As at the date of this Prospectus, Telefónica is currently conducting an internal investigation regarding possible violations of applicable anti-corruption laws. Telefónica has been in contact with governmental authorities about this matter and intends to cooperate with those authorities as the investigation continues. It is not possible at this time to predict the scope or duration of this matter or its likely outcome.

Customers' perceptions of services offered by Telefónica 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 Telefónica'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 adequately could have an adverse impact on the Group's business, financial condition, results of operations and cash flows.

Telefónica 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, secure 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 of these 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 customer preferences that are taking place in the industry, as well as economic, political and social circumstances.

Failure to do so adequately could have an adverse impact on the Group's business, financial condition, results of operations and cash flows.

New products and technologies arise constantly, and their 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, 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 €472 million in the first half of 2016;

representing a decrease of 0.9% from €487 million of the same period in 2015. These expenses represented 1.9% and 1.8% of the Group's consolidated revenues in the first half of 2016 and 2015, respectively. These figures have been calculated using the guidelines established in the Organization for Economic Cooperation and Development ("OECD") manual. 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. While an increasing demand for the capabilities offered by these new networks to end users exists, 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 the Group's 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 adequately could have an adverse impact on the Group's business, financial condition, results of operations and cash flows.

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

Telefónica depends on its 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 Telefónica's operations, and may cause legal contingencies or damages to its image in the event that inappropriate practices are produced by a participant in the supply chain.

As of 30 June 2016, the Telefónica Group depended on 4 handset suppliers and 11 network infrastructure suppliers, which together accounted for 80% of the awarded contracts for the year then ended. These suppliers may, among other things, extend delivery times, raise prices and limit supply due to their own stock shortfalls 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 otherwise 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, stealing of infrastructure elements or cyber-attacks, which affect the quality of or cause an interruption in the Telefónica Group's service, could lead to customer dissatisfaction, reduced revenues and traffic, costly repairs, penalties or other measures imposed by regulatory authorities and could harm the Telefónica Group's image and reputation.

Telecommunications companies worldwide face increasing cybersecurity threats as businesses become increasingly dependent on telecommunications and computer networks and adopt cloud computing technologies. Cybersecurity threats include gaining unauthorised access to Telefónica's systems or inserting computer viruses or malicious software in its systems to misappropriate consumer data and other sensitive information, corrupt Telefónica's data or disrupt its operations. Unauthorised access may also be gained through traditional means such as the theft of laptop computers, portable data devices and mobile phones and intelligence gathering on employees with access.

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 these types of incidents, and the claims and loss in revenue caused by service interruptions to date have been covered by these policies, these policies may not be sufficient to cover all possible monetary losses.

The telecommunications industry may be affected by the possible effects that 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 certain expert groups and public health agencies, including the World Health Organisation, that states that currently there are no established risks associated with exposure to low frequency signals in mobile communications. However, the scientific community is still investigating this issue especially with respect to mobile devices. Exposure limits for radio frequency suggested in the guidelines of the Protection of Non-Ionising Radiation Protection Committee have been internationally recognised. The mobile industry has adopted these exposure limits and works to request authorities worldwide to adopt these standards.

Worries about radio frequency 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 mobile telephones and the massive deployment of smart meters and other products using mobile technology. This could lead to Telefónica 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 of operations 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 costs. Potential changes in the regulatory, business, economic or political environment may result in the need to introduce changes to estimates made and to recognise impairments 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 impairments on certain of its investments, affecting its results of operations in the year in which they were experienced.

The Telefónica Group's networks carry and store large 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.

The Telefónica Group's networks carry and store large volumes of confidential, personal and business data, through both voice and data traffic. The Telefónica Group stores increasing quantities and types of customer data in both business and consumer segments. Despite its best efforts to prevent it, the Telefónica Group may be found liable for any loss, transfer, or inappropriate modification of the customer data or general public data stored on its servers or transmitted through its networks, any of 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.

In addition, the Telefónica Group'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 any loss, transfer or inappropriate modification of the customer data stored on its servers or carried by its networks.

In most countries in which the Telefónica Group 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.

Any of the foregoing could have an adverse impact on the business, financial position, results of operations and cash flows of the Group.

Telefónica and Telefónica Group companies are party to lawsuits, tax claims 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, the Telefónica Group is party to certain judicial tax proceedings in Peru concerning the clearance of certain previous years' income tax, in respect of which a contentious-administrative appeal is currently pending and to certain tax proceedings in Brazil, primarily relating to the CIMS (a Brazilian tax on telecommunication services). Further details on these matters are provided in notes 17 and 21 of the audited consolidated financial statements of the Guarantor for the year ended 31 December 2015.

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, 19 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 therefore.

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*").

US Foreign Account Tax Compliance Withholding

The US "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-US 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-US 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 US withholding tax were to be deducted or withheld from any payments on the Securities, the Issuer or the Guarantor, as the case may be, 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 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) (*Optional Interest Deferral – Optional Settlement of Arrears of Interest*) and 5(c) (*Optional Interest Deferral – Mandatory Settlement of Arrears of Interest*) 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.

Substitution or variation of the Securities

There is a risk that, after the issue of the Securities, a Tax Event, a Withholding Tax Event, an Accounting Event or a Capital Event may occur which would entitle the Issuer and/or the Guarantor, without any requirement for the consent or approval of the Holders, to substitute or vary the Securities, subject to certain conditions intended to protect the interests of the Holders, so that after such substitution or variation the Securities remain or become, as the case may be, eligible for the same or (from the perspective of the Issuer or the Guarantor) more favourable tax, accounting or ratings treatment than the treatment to which they were entitled prior to the relevant event occurring.

Any such substitution or variation may have an adverse impact on the price of, and/or the market for, 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, suspension 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 no 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, any attachment by a creditor 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 or a 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 competent Dutch court. 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 debtor (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 the debtor's 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 the debtor's 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 or Additional Provision 4 of the Spanish Insolvency Law (100% in the case that the funds are lent before 2 October 2016) 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 or, even if they dissent or abstain from voting, if the applicable majority (which depends on the content of the arrangement) of the relevant class of the privileged creditors vote 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.

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:	€1,000,000,000 Undated 5.5 Year Non-Call Deeply Subordinated Guaranteed Fixed Rate Reset Securities (the " Securities "), to be issued by the Issuer on 15 September 2016 (the " Issue Date ").
Joint Bookrunners:	BNP Paribas, Citigroup Global Markets Limited, Commerzbank Aktiengesellschaft, Merrill Lynch International, Société Générale, The Royal Bank of Scotland plc 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:	15 September 2016.
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 3.750 per cent. per annum, payable annually in arrear on each Interest Payment Date, commencing on 15 March 2017; 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) 15 March 2027, 3.858 per cent. per annum;(B) in respect of the period commencing on 15 March 2027 to (but excluding) 15 March 2042, 4.108 per cent. per annum; and(C) from and including 15 March 2042, 4.858 per cent. per annum, <p>all as determined by the Agent Bank, payable annually in arrear on each Interest Payment Date, commencing on 15 March 2023, subject to Condition 5 (<i>Optional Interest Deferral</i>), all as more particularly described in Condition 4 (<i>Interest Payments</i>) of the Terms and Conditions of the Securities.</p>
Interest Payment Dates:	Interest payments in respect of the Securities will be payable annually (except for a short first Interest Period) in arrear on 15 March in each year, commencing on 15 March 2017.

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) (<i>Status and Subordination of the Securities and Coupons – Subordination of the Securities</i>) 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) (<i>Status and Subordination of the Securities and Coupons – Subordination of the Securities</i>) 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 Interest Deferral - 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*".

Substitution or Variation:

If at any time a Tax Event, a Withholding Tax Event, an Accounting Event or a Capital Event has occurred on or after the Issue Date, then the Issuer or the Guarantor may, subject to Condition 12(c) (without any requirement for the consent or approval of the Holders) and having given not less than 30 nor more than 60 days' notice to the Fiscal Agent and, in accordance with Condition 14, the Holders (which notice shall be irrevocable), at any time either (i) exchange the Securities for new securities of the Issuer, the Guarantor or any wholly-owned direct or indirect finance subsidiary of the Guarantor with a guarantee of the Guarantor or (ii) vary the terms of the Securities, so that after such substitution or variation the Securities remain or become, as the case may be, eligible for the same or (from the perspective of the Issuer or the Guarantor) more favourable tax, accounting or ratings treatment than the treatment to which they were entitled prior to the relevant event occurring.

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) in the case of a repurchase, is in an amount necessary to allow the Issuer's aggregate principal amount of hybrid capital outstanding after such repurchase to remain below the maximum aggregate principal amount of hybrid capital to which S&P would assign equity content under its prevailing methodology, or
- (iv) the Securities are redeemed pursuant to a Tax Event, a Capital Event, a Substantial Purchase Event, an Accounting Event or a Withholding Tax Event, or
- (v) such redemption or repurchase occurs on or after the Reset Date falling on 15 March 2042.

Rating:	The Securities will be rated BB+ by S&P, Ba1 by Moody's and BB+ 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 " <i>Subscription and Sale</i> ". Category 2 selling restrictions will apply for the purposes of Regulation S under the Securities Act.
Use of Proceeds:	The net proceeds of the issue of the Securities, expected to amount to €994,500,000 will be used for general corporate purposes of the Guarantor and its Group, including the preservation of the liquidity cushion and debt refinancing.
Risk Factors:	Prospective investors should carefully consider the information set out in " <i>Risk Factors</i> " in conjunction with the other information contained or incorporated by reference in this Prospectus.
ISIN:	XS1490960942.
Common Code:	149096094.

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 2015 are available on http://www.rns-pdf.londonstockexchange.com/rns/2747S_-2016-3-16.pdf; the audited unconsolidated financial statements of Telefónica Europe B.V. for the year ended 31 December 2014 are available on http://www.rns-pdf.londonstockexchange.com/rns/5805K_1-2015-4-17.pdf; the audited consolidated financial statements of Telefónica, S.A. for the year ended 31 December 2015 (the "2015 Consolidated Financial Statements") are available on http://www.rns-pdf.londonstockexchange.com/rns/3770Q_2-2016-2-26.pdf; the audited consolidated financial statements of Telefónica, S.A. for the year ended 31 December 2014 are available on http://www.rns-pdf.londonstockexchange.com/rns/1544G_1-2015-2-27.pdf; and the unaudited interim consolidated financial information for the 6 months ended 30 June 2016 of Telefónica, S.A. is available on http://www.rns-pdf.londonstockexchange.com/rns/4898F_-2016-7-28.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 2015 and 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 2015 and 2014, and the financial statements, the notes to financial statements and the unaudited interim consolidated financial information for the 6 months ended 30 June 2016 for the Guarantor.

Telefónica Europe B.V.

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Telefónica, S.A.

Consolidated Financial Statements Year ended 31 December 2015

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Interim Consolidated Financial Information for the 6 months ended 30 June 2016

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

Any documents which are themselves incorporated by reference in the information incorporated by reference in this Prospectus will not form part of 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 1 September 2016 and the guarantee of the Securities was authorised by a resolution of the Delegated Committee of the Board of Directors of the Guarantor dated 29 July 2015, 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 15 September 2016 (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) (*Form Denomination and Title – Title*) 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) 15 September 2016 (the "**Issue Date**") in accordance with the provisions of this Condition 4.

Subject to Condition 5 (*Optional Interest Deferral*), interest shall be payable on the Securities with respect to any Interest Period annually (except for a short first Interest Period) 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 (*Redemption and Purchase*) or the date of any Substitution thereof pursuant to Condition 12(c) 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 3.750 per cent. per annum, payable annually in arrear on each Interest Payment Date commencing on 15 March 2017; 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) 15 March 2027, 3.858 per cent. per annum;
 - (B) in respect of the period commencing on 15 March 2027 to (but excluding) 15 March 2042, 4.108 per cent. per annum; and
 - (C) from and including 15 March 2042, 4.858 per cent. per annum,all as determined by the Agent Bank (each a "**Subsequent Fixed Interest Rate**"), payable annually in arrear on each Interest Payment Date, commencing on 15 March 2023, subject to Condition 5 (*Optional Interest Deferral*),

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 (*Notices*), 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

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) (*Interest Payments - Prevailing Interest Rate*), 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) (*Optional Interest Deferral – Optional Settlement of arrear of Interest*) and 5(c) (*Optional Interest Deferral – Mandatory Settlement of Arrear of Interest*) 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 (*Notices*), 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 "**Arrear 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) (*Optional Interest Deferral – Mandatory Settlement of Arrear of Interest*), 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 Arrear of Interest:*** Arrear 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 (*Notices*), 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 Arrear of Interest (or part thereof) and specifying the relevant Optional Deferred Interest Settlement Date.
- (c) ***Mandatory Settlement of Arrear of Interest:*** Notwithstanding the provisions of Condition 5(b) (*Optional Interest Deferral – Optional Settlement of arrear of Interest*), the Issuer shall pay any outstanding Arrear 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 (*Notices*), 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 (*Redemption and Purchases*) or become due and payable in accordance with Condition 9 (*Enforcement Events and No Events of Defaults*); and
- (iv) the date on which the Securities are substituted or varied in accordance with Condition 12(c).

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) (*Redemption and Purchase – Issuer's Call Option*), 6(c) (*Redemption and Purchase – Redemption for Taxation Reasons*), 6(d) (*Redemption and Purchase – Redemption for Accounting Reasons*), 6(e) (*Redemption and Purchase – Redemption for Rating Reasons*), or 6(f) (*Redemption and Purchase – Redemption following a Substantial Purchase Event*).
- (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 (*Notices*), 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 (*Notices*), the Holders (which notice shall be irrevocable) and subject to Condition 6(g) (*Redemption and Purchase – Preconditions to Redemption*), 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 (*Notices*), the Holders (which notice shall be irrevocable) and subject to Condition 6(g) (*Redemption and Purchase – Preconditions to Redemption*), 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 (*Notices*), the Holders (which notice shall be irrevocable) and subject to Condition 6(g) (*Redemption and Purchase – Preconditions to Redemption*), 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 (*Notices*), the Holders (which notice shall be irrevocable) and subject to Condition 6(g) (*Redemption and Purchase – Preconditions to Redemption*), 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) (*Redemption and Purchase – Issuer's Call Option*)), 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 (*Meetings of Holders of Securities and Modification*).
- (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) *in the case of a repurchase, such repurchase is in an amount necessary to allow the Issuer's aggregate principal amount of hybrid capital outstanding after such repurchase to remain below the maximum aggregate principal amount of hybrid capital to which S&P would assign equity content under its prevailing methodology, or*
- (iv) *the Securities are redeemed pursuant to a Tax Event, a Capital Event, an Accounting Event, a Substantial Purchase Event or a Withholding Tax Event, or*
- (v) *such redemption or repurchase occurs on or after the Reset Date falling on 15 March 2042.*

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 (*Taxation*). 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, unmatured 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 unmatured Coupons relating to it, redemption shall be made only against the provision of such indemnity as the Issuer and the Guarantor may require.
- (d) **Exchange of Talons:** On or after the Interest Payment Date for the final Coupon forming part of a Coupon sheet issued in respect of any 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 (*Prescription*)).
- (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 (*Notices*).

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 the First Additional Provision 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) (*Taxation – Tax Credit Payment*) and (c) (*Taxation – Tax Credit Clawback*) 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 (*Payments*) 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 (*Interest Payments*) 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 the First Additional Provision 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 the First Additional Provision 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 (*Payments*) 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 therefore, pay such Coupon when due.

12. **Meetings of Holders of Securities and Modification, Substitution and Variation**

- (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.

- (c) **Substitution and Variation:** If at any time after the Issue Date the Issuer and/or the Guarantor determines that a Tax Event, a Withholding Tax Event, an Accounting Event or a Capital Event has occurred, the Issuer may, as an alternative to an early redemption of the Securities, on any applicable Interest Payment Date, without the consent of the Holders, (i) exchange the Securities (the "**Exchanged Securities**") into new securities of the Issuer, the Guarantor or any wholly-owned direct or indirect finance subsidiary of the Guarantor with a guarantee of the Guarantor, or (ii) vary the terms of the Securities (the "**Varied Securities**"), so that in either case (A) in the case of a Tax Event, in respect of (I) the Issuer's obligation to make any payment of interest under the Exchanged Securities or Varied Securities; or (II) the obligation of the Guarantor to make any payment of interest in favour of the Issuer under the Subordinated Loan, the Issuer or the Guarantor (as the case may be) is entitled to claim a deduction or a higher deduction (as

the case may be) in respect of interest paid when computing its tax liabilities in The Netherlands or in Spain (as the case may be), as compared with the entitlement after the occurrence of the relevant Tax Event, (B) in the case of a Withholding Tax Event, in making any payments in respect of the Exchanged Securities or Varied Securities or the Exchanged or Varied Guarantee (as defined below) the Issuer or the Guarantor are not required to pay Additional Amounts in respect of the Exchanged Securities or Varied Securities or the Exchanged or Varied Guarantee, (C) in the case of an Accounting Event, the aggregate nominal amount of the Exchanged Securities or Varied Securities (as the case may be) is 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, or (D) in the case of a Capital Event, the aggregate nominal amount of the Exchanged Securities or Varied Securities (as the case may be) is assigned "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) by the relevant Rating Agency that is equal to or greater than that which was assigned to the Securities on the Issue Date.

Any such exchange or variation shall be subject to the following conditions:

- (i) the Issuer giving not less than 30 nor more than 60 days' notice to the Fiscal Agent and the Holders in accordance with Condition 14 (*Notices*);
- (ii) the Issuer complying with the rules of any stock exchange (or any other relevant authority) on which the Securities are for the time being admitted to trading, and (for so long as the rules of such exchange require) the publication of any appropriate supplement, listing particulars or offering circular in connection therewith, and the Exchanged Securities or Varied Securities continue to be admitted to trading on the same stock exchange as the Securities if they were admitted to trading immediately prior to the relevant exchange or variation;
- (iii) the Issuer paying any outstanding Arrears of Interest in full prior to such exchange or variation;
- (iv) the Exchanged Securities or Varied Securities shall: (A) rank at least *pari passu* with the ranking of the Securities prior to the exchange or variation, (B) have the benefit of a guarantee (the "**Exchanged or Varied Guarantee**") from the Guarantor on terms not less favourable to Holders than the terms of the Guarantee (as reasonably determined by the Issuer and the Guarantor) and (C) benefit from the same or more favourable interest rates and the same Interest Payment Dates, the same First Reset Date and early redemption rights (provided that the relevant exchange or variation may not itself trigger any early redemption right), the same rights to accrued interest or Arrears of Interest and any other amounts payable under the Securities which, in each case, has accrued to the Holders and has not been paid, the same rights to principal and interest, and, if publicly rated by S&P, Moody's and/or Fitch immediately prior to such exchange or variation, at least the same credit rating immediately after such exchange or variation by each of S&P, Moody's and/or Fitch (as the case may be), as compared with the relevant rating(s) immediately prior to such exchange or variation (as determined by the Issuer and the Guarantor using reasonable measures available to it including discussions with S&P, Moody's and/or Fitch to the extent practicable) (D) shall not contain terms providing for the mandatory deferral of interest and (E) not contain terms providing for loss absorption through principal write-down or conversion to shares;
- (v) the preconditions to redemption set out in Condition 6(g) having been satisfied and the terms of the exchange or variation (in the sole opinion of the Issuer or the Guarantor, as the case may be) not being prejudicial to the interests of the Holders, including compliance with (iv) above, as certified to the benefit of the Holders by two directors of the Guarantor, having consulted with an independent investment bank of international standing, and any such certificate shall, absent fraud or manifest error, be final and binding on all parties; and

- (vi) the issue of legal opinions addressed to the Fiscal Agent (and which shall be made available to the Holders at the specified offices of the Fiscal Agent during usual office hours) for the benefit of the Holders from one or more international law firms of good reputation selected by the Issuer or the Guarantor and confirming (x) that each of the Issuer and the Guarantor has capacity to assume all rights, duties and obligations under the Exchanged Securities or Varied Securities and the Exchanged or Varied Guarantee (as the case may be) and has obtained all necessary corporate or governmental authorisation to assume all such rights and obligations and (y) the legality, validity and enforceability of the Exchanged Securities or Varied 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 depositary 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) (*Status and Subordination of the Securities and Coupons – 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 3(c) (*Guarantee, Status and Subordination of the Guarantee – 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.
- (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 Digital Limited, 20 Air Street, London W1B 5AN, 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 7 Year Non-Call Securities;

"**2014 Non-Call Securities**" means the March 2014 6 Year Non-Call Securities, the March 2014 10 Year Non-Call Securities and the December 2014 5 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) (*Interest Payments – Prevailing Interest Rate*);

"**5 year Swap Rate Quotations**" has the meaning given to it in Condition 4(c) (*Interest Payments – Prevailing Interest Rate*);

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 (*Notices*) 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) (*Taxation – Additional Amounts*);

"**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) (*Optional Interest Deferral – Deferral of Interest Payments*);

"**business day**" has the meaning given to it in Condition 7(e) (*Payments – Payments on Business Days*);

"**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) (*Interest Payments – Interest Accrual*);

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 (*Notices*) that it has so received, confirmation from any Rating Agency that, due to 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; 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) (*Optional Interest Deferral – Mandatory Settlement of Arrears of Interest*);

"**Condition**" means the terms and conditions of the Securities;

"**December 2014 5 Year Non-Call Securities**" means the €850,000,000 Undated 5 Year Non-Call Deeply Subordinated Guaranteed Fixed Rate Reset Securities (ISIN: XS 1148359356) issued by the Issuer on 4 December 2014 and unconditionally and irrevocably guaranteed on a subordinated basis by the Guarantor;

"**Deferral Notice**" has the meaning given to it in Condition 5(a) (*Optional Interest Deferral – Deferral of Interest Payments*);

"**Deferred Interest Payment**" has the meaning given to it in Condition 5(a) (*Optional Interest Deferral – Deferral of Interest Payments*);

"**Dividend Declaration**" has the meaning given to it in Condition 5(c) (*Optional Interest Deferral – Mandatory Settlement of Arrears of Interest*);

"**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 15 March 2022;

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

"**Further Securities**" means any Securities issued pursuant to Condition 13 (*Further Issues*) 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) (*Form, Denomination and Title – Title*);

"**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 Payments*);

"**Interest Payment Date**" means 15 March in each year;

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

including) an Interest Payment Date and ending on (but excluding) the next succeeding Interest Payment Date;

"**Issue Date**" means 15 September 2016;

"**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) (*Optional Interest Deferral – Mandatory Settlement of Arrears of Interest*);

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

"**November 2013 7 Year 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 the First Additional Provision 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 the First Additional Provision 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 (*Interest Payments*);

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

"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 (*Redemption and Purchase*);

"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 (*Notices*) 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) (*Interest Payments – Prevailing Interest Rate*);

"Reset Reference Bank Rate" has the meaning given to it in Condition 4(c) (*Interest Payments – Prevailing Interest Rate*);

"Reset Screen Page" has the meaning given to it in Condition 4(c) (*Interest Payments – Prevailing Interest Rate*);

"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 15 September 2016, 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) (*Redemption and Purchase – Cancellation*));

"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 16 of Law 27/2014 dated 27 November, on Corporate Income Tax, as at 8 September 2016;

"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 8 September 2016;

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

"Taxing Authority" has the meaning given to it in Condition 8(a) (*Taxation – Additional Amounts*); 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-US 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-US 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 15 September 2016 (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 15 September 2016

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 €1,000,000,000 Undated 5.5 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 15 September 2016 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 15 September 2016.
- (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 (*Taxation*).

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) (*Guarantee, Status and Subordination of the Guarantee – Status of the Guarantee*).
- 5.3 In the event of the Guarantor being declared in insolvency ("*concurso*") under Spanish insolvency law, the provisions of Condition 3(c) (*Guarantee, Status and Subordination of the Guarantee – Subordination of the Guarantee*) 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: Eduardo Álvarez Gómez

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) (*Guarantee, Status and Subordination of the Guarantee – Status of the Guarantee*) and 3(c) (*Guarantee, Status and Subordination of the Guarantee – Subordination of the Guarantee*) 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 Digital Limited, 20 Air Street, London W1B 5AN, 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 €994,500,000 will be used for general corporate purposes of the Guarantor and its Group, including the preservation of the liquidity cushion and debt refinancing.

DESCRIPTION OF THE ISSUER

Introduction

Telefónica Europe B.V. (the "**Issuer**") was incorporated for an indefinite period in 1996 in The Netherlands as a private company with limited liability (*besloten vennootschap met beperkte aansprakelijkheid*) under the laws of The Netherlands. Its statutory seat is at Amsterdam, The Netherlands, and its business address since 1 October 2013 is at Zuidplein 112, H Tower, 13th floor, 1077XV Amsterdam, The Netherlands. The Issuer's telephone number is +31(0)20 575 3370. Telefónica Europe B.V. is registered with the trade register of the Dutch 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 Soualiga, B.V.
Eduardo José Alvarez Gómez	Director	Head of Financing Director at Telefónica, S.A. Board Member Fonditel Pensiones E.G.F.P. S.A. Joint and several Director of Telefónica Participaciones, S.A.U. and Telefónica Emisiones, S.A.U.
Jose Miguel Hernández Rabbat	Director	Managing Director of Telefisa 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 and its telephone number is +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 (stable 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 occurred in 2015:

- On 24 March 2015, Telefónica signed an agreement with Hutchison for the acquisition by the latter of Telefónica's operations in the UK (O2 UK) for a price (firm value) of £10,250 million in cash (approximately €14,000 million at the exchange rate as of the date of the agreement), composed of (i) an initial amount of £9,250 million (approximately €12,640 million as of the date of the agreement) due to be paid at closing and (ii) an additional deferred payment of £1,000 million (approximately €1,360 million as of the date of the agreement) to be paid once the cumulative cash flow of the combined company in the United Kingdom reached an agreed threshold. According to the sale agreement, the price was to be adjusted by the debt, the working capital and other defined circumstances that could ultimately have arisen upon a closing of the O2 UK divestiture.

Completion of the transaction was subject to, among other conditions, the approval of the European Commission and the obtainment of waivers to some contractual provisions affected by the sale, including those related to network alliances, as well as change of control provisions under certain contractual arrangements with third parties. As of the date of this Prospectus, the European Commission has prohibited the sale (see further "*Recent Developments*" below).

- On 25 March 2015, pursuant to the authorisation granted by the General Shareholders' Meeting held on 18 May 2011, Telefónica increased its share capital by a nominal amount of €281,213,184, by means of issuing and circulating 281,213,184 new ordinary shares, with a nominal value of one (1) euro each, of the same class and series as those already existing, and duly represented by book entries (the "**New Shares**" and the "**Share Capital Increase**", respectively).

The subscription price of the New Shares was €10.84 per share, 1 euro corresponding to the nominal value and €9.84 to the issue premium, with the Share Capital Increase amounting to €3,048,350,914.56.

The shareholders of Telefónica hold pre-emptive subscription rights over the New Shares.

On 17 April 2015, Telefónica declared that the share capital increase had been fully subscribed and granted the public deed evidencing the Share Capital Increase, which was registered with the Commercial Registry of Madrid on 20 April 2015.

- On 25 March 2015, the Brazilian antitrust authority, *Conselho Administrativo de Defesa Economica* ("**CADE**"), approved both the GVT Acquisition (as defined below) and the demerger of Telco, S.p.A. ("**Telco**") (described below), subject to restrictions similar to those imposed by ANATEL. These restrictions required, among other things, that Telefónica Brasil, S.A. ("**Telefônica Brasil**") commit to provide certain service coverage in certain geographical areas

and cities in Brazil, to maintain certain products, contract requirements and services and to maintain a minimum quality with respect to certain other services. Moreover, as part of this authorisation, Telefónica undertook, among other obligations, to not exercise its voting rights and ultimately to divest its entire stock participation in Telecom Italia, S.p.A. ("**Telecom Italia**"). In addition, Telefónica and Telefônica Brasil have undertaken to comply with certain other restrictions agreed between CADE and the Vivendi, S.A. group.

- On 30 April 2015, after obtaining the relevant regulatory authorisation, the acquisition by Telefónica de Contenidos, S.A.U. of 56% of the capital stock of Distribuidora de Televisión Digital, S.A. ("**DTS**") owned by Promotora de Informaciones, S.A. was completed.
- On 12 May 2015, Telefónica paid a dividend of €0.40 per share in cash corresponding to the second tranche of the 2014 dividend.
- On 28 May 2015 after obtaining the relevant regulatory authorisations, the Extraordinary General Shareholders' Meeting of Telefônica Brasil held on that date approved the acquisition of Global Village Telecom, S.A. and its holding company, GVT Participações, S.A. (collectively "**GVT**") from Vivendi, S.A. (the "**GVT Acquisition**") and the issuance of shares of Telefônica Brasil to Vivendi, S.A. as partial payment of the purchase price of the shares of GVT. Consequently, the closing of such acquisition (for an amount of €4,663 million and the delivery of 12% of the share capital of the new Telefônica Brasil resulting from the integration) was completed.
- On 12 June 2015, Telefónica's Annual General Shareholders' Meeting took place on its second call with the attendance of holders, present or represented, of 58.40% of the share capital. In this meeting, all the resolutions submitted by the Board of Directors for deliberation and approval were approved by the majority of votes.
- On 17 June 2015, having obtained the required anti-trust and telecommunications approvals (including in Brazil and Argentina), Telco carried out its demerger, which became effective on 18 June 2015. As a consequence of the demerger, the Telecom Italia ordinary shares held by Telco – which represented 22.3% of the company's ordinary share capital - were allocated as follows: 14.72% of Telecom Italia's share capital was allocated to Telco TE, S.p.A., a newly created company owned by Telefónica, S.A.; 4.31% to a newly created company owned by the Generali group; and 1.64% to each of the newly created companies owned by Intesa Sanpaolo and Mediobanca respectively.

Moreover, the shareholders' agreement in force between the shareholders in Telco ceased to have effect on 18 June 2015.

- On 24 June 2015, in compliance with the undertakings assumed in the agreement entered into on 19 September 2014 for the GVT Acquisition, Telefónica, through its 100%-subsidiary Telco TE S.p.A., delivered 1,110 million ordinary shares of Telecom Italia (representing 8.2% of its ordinary shares) to Vivendi, S.A. and received from Vivendi, S.A. all the ordinary shares and part of the preferred shares of Telefônica Brasil that Vivendi S.A. had received as consideration for the sale of GVT, which together represented 4.5% of the total share capital of Telefônica Brasil.

Moreover, Telefónica (through its 100% subsidiary Telco TE S.p.A.), entered into a purchase agreement with a financing institution for the sale of 872 million ordinary shares of Telecom Italia, representing 6.5% of the ordinary shares of this company, for an amount of approximately €1,025 million. Consequently, Telefónica completed the divestment of its entire stake in Telecom Italia, in accordance with regulatory and competition commitments.

Furthermore, Telefónica has arranged several hedging instruments which will allow Telefónica to repurchase the shares of Telecom Italia that are necessary to meet its exchange obligations under the mandatory exchangeable bonds for shares of Telecom Italia, issued by Telefónica, S.A. in July 2014.

- On 10 July 2015, DTS reached an agreement, for an amount of €600 million, with the Spanish Professional Soccer League ("**LFP**") for the audiovisual content rights of pay per view soccer events in the domestic market, for the 2015/2016 season.

- On 27 July 2015, Telefónica announced that, pursuant to the resolution adopted by the Annual General Shareholders' Meeting of Telefónica held on 12 June 2015 which approved a share capital reduction through the cancellation of own shares, and following the execution agreement adopted by the Board of Directors of Telefónica, the public deed of this share capital reduction was registered in the Madrid Mercantile Registry (*Registro Mercantil*).

As a result, 74,076,263 shares of Telefónica were cancelled, reducing the company's share capital by the same amount. Telefónica's share capital after the reduction, at such date, stood at €4,864,341,251 made up of an equal number of ordinary shares, all of a single series and with a nominal value of one (1) euro per share.

- On 29 July 2015, Telefónica entered into an agreement with Vivendi, S.A. pursuant to which Telefónica committed to deliver 46.0 million of its treasury shares, representing 0.95% of its share capital, to Vivendi, S.A. in exchange for 58.4 million preferred shares of Telefónica Brasil (which had been received by Vivendi, S.A. as partial consideration for GVT in the GVT Acquisition), representing 3.5% of the share capital of Telefónica Brasil, from Vivendi, S.A.

The execution of this agreement was approved by the CADE.

- On 4 August 2015, in relation to the long-term incentive plan consisting in the granting of shares of Telefónica – known as the Performance & Investment Plan ("**PIP**") -, the Company announced the number of shares to be delivered under PIP's Second Phase (2012-2015) to each of the beneficiaries of PIP in their positions as Executive Directors or Executives of Telefónica, and which amounts to 77% of the shares they were assigned originally.
- On 30 September 2015, the Executive Commission of Telefónica's Board of Directors agreed that the corporate resolutions required to carry out the free-of-charge capital increase related to the scrip dividend shareholder compensation scheme ("**Telefónica's Flexible Dividend**") approved by the Annual General Shareholder's Meeting held on 12 June 2015, should be adopted at the Executive Commission meeting scheduled for 13 November 2015. On 13 November 2014, the Executive Commission agreed the implementation of the aforementioned capital increase.
- On 28 October 2015, following a report of the Nominating, Compensation and Corporate Governance Committee, the Board of Directors of Telefónica approved, with regard to the second cycle (2015-2018) 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, 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 set forth in the plan, and of the maximum achievement of the Total Shareholder Return established in such plan.
- On 11 December 2015, Telefónica announced that, on 2 December 2015, the free-of-charge allotment rights trading period for the free-of-charge capital increase related to Telefónica's Flexible Dividend had ended. The holders of 20.01% of the free-of-charge allotment rights accepted the purchase commitment assumed by Telefónica. The gross amount paid by Telefónica for these rights amounted to €335,775,673.59. The Company waived the rights thus acquired, which were amortised.

The holders of 79.99% of the free-of-charge allotment rights were entitled, therefore, to receive new shares of Telefónica. Nevertheless, Telefónica waived the free-of-charge allotment rights that corresponded to its treasury shares at the record date (17 November 2015). Therefore, the final number of ordinary shares with a nominal value of one (1) euro issued in the capital increase was 110,857,946 (2.3% of Telefónica's share capital as of that date), totaling €110,857,946. As a result, the share capital of Telefónica after the capital increase, as registered on 11 December 2015 with the Commercial Registry of Madrid, was €4,975,199,197 (4,975,199,197 shares).

The new shares were admitted to listing on the Madrid, Barcelona, Bilbao and Valencia stock exchanges on 15 December 2015 and the ordinary trading of the new shares in Spain began on 16

December 2015. Applications were also made to the stock exchanges of London, Buenos Aires, New York and Lima.

Recent Developments

The following significant events have occurred since 31 December 2015:

- On 12 January 2016, DTS and Mediaproducción, S.L.U. reached an agreement for the broadcasting of the thematic pay TV channel called "BeIN Sports LaLiga" with contents of the Spanish National League Championship First and Second Division and the Copa del S.M. el Rey, corresponding to the three seasons 2016/17, 2017/18 and 2018/19.

The total value of the agreements relating to those channels amounted to €2,400 million.

Moreover, on 2 December 2015, DTS was awarded Package number 5 for the pay television broadcast of a live match of the First Division and a live match of the Second Division, on an exclusive basis (first selection), following the tender by the National Football League and publicly announced on 13 November 2015 for the three seasons 2016/17, 2017/18 and 2018/19.

- On 28 January 2016, Telefónica de España signed the 1st Collective Agreement of Related Companies, which was wholly backed by the largest trade unions. Telefónica Móviles España and Telefónica Soluciones were also parties to this agreement. The agreement contemplates, among other elements, an "Individual Employment Suspension Plan" for their respective employees, the implementation of which is entirely voluntary in the period from 2016-2017. All employees who fulfil the following criteria are eligible to participate in the Plan, namely: (i) employees must have been employed as of 1 January 2015, (ii) as of the date of the agreement, such employees must have worked for the Group 15 years or more, and (iii) as of 31 December 2017, such employees must be at least 53 years old. In relation to the aforementioned Plan:

- Telefónica has opened the registration period for employees to sign up to the Plan.
- The value of the expected expenses resulting from the Plan is estimated to be approximately €2,896 million.

- On 11 February 2016, Telefónica announced the creation of Telxius Telecom, S.A., a company which brings together certain infrastructure assets of the Group, which is intended to enable the management of the Telefónica Group's infrastructure on a global scale with a more specialised and focused approach, with the aim of increasing the services provided to other operators, improving the return on capital invested and allowing Telxius Telecom, S.A. to participate more actively in the growth opportunities that exist in the industry, including the possibility of incorporating third party assets.

- On 2 March 2016, the Company announced the decision to carry out an issue of cash-settled equity-linked bonds (the "**Bonds**") for placement among qualified investors in the international market. The Bonds were issued by Telefónica Participaciones, S.A.U., and guaranteed by Telefónica.

Concurrently with the issue of the Bonds, Telefónica purchased cash-settled call options on Telefónica's shares from one or several financial institutions in order to hedge Telefónica Participaciones, S.A.U. and Telefónica's exposure to any payments to be made under the Cash-Settlement Option.

The summary terms of the Bonds are as follows: (i) the final amount of the issue was €600 million, (ii) the issue price of the Bonds was 101.25% of their nominal value, (iii) the Bonds accrue interest at a rate of 0% per annum, and (iv) the Bonds include a cash-settled conversion option (the "**Cash-Settlement Option**"), which the holders may exercise from 9 November 2020 to the 33rd scheduled trading date before the final maturity date, or earlier in certain circumstances.

- On 16 March 2016, further to Relevant Events notices published on 2 March 2016 in relation to the issue by Telefónica of equity-linked bonds via its wholly-owned subsidiary Telefónica

Participaciones, S.A.U., the Company announced that the reference price of the Telefónica shares for the purpose of the Cash-Settlement Option (defined as Conversion Price in the terms of the Bonds) has been set at €11.9215.

- On 6 April 2016, Telefónica, S.A., through its wholly-owned subsidiary Telefónica Emisiones, S.A.U., under its Guaranteed Programme for the Issuance of Debt Instruments ("**EMTN Programme**") filed with the FCA in London on 5 June 2015, launched an issuance of Notes guaranteed by Telefónica, S.A. in the Euro market in an aggregate principal amount of €2,750 million.
- On 8 April 2016, the Board of Directors of Telefónica, S.A. resolved to adopt the following resolutions:
 - To propose to the next General Shareholders Meeting, the appointment of PricewaterhouseCoopers Auditores S.L. as statutory auditor for the Annual Accounts of Telefónica, S.A. and its Consolidated Group of Companies for the years 2017, 2018 and 2019.
 - To appoint Mr. José María Álvarez-Pallete López as Chairman of the Board of Directors and of the Executive Commission, replacing Mr. César Alierta Izuel.
 - To take formal note and record the voluntary resignation presented to their respective positions as members of the Board of Directors of Telefónica, S.A. by Mr. Carlos Colomer Casellas, Mr. Alfonso Ferrari Herrero, Mr. José Fernando de Almansa Moreno-Barreda and Mr. Santiago Fernández Valbuena.
 - Based on the proposal of the Nominating, Compensation and Corporate Governance Committee, to appoint Ms. Sabina Fluxà Thienemann, Mr. José Javier Echenique Landiribar, Mr. Peter Löscher and Mr. Juan Ignacio Cirac as Independent Directors of Telefónica, S.A.. The ratification of such resolutions will be proposed to the next General Shareholders Meeting.
 - To appoint as Coordinating Independent Director, Mr. Francisco Javier de Paz Mancho.
 - To appoint: (i) the Independent Director Mr. José Javier Echenique Landiribar as a member of the Executive Commission; (ii) the Independent Director Mr. José Javier Echenique Landiribar as Chairman of the Audit and Control Committee; (iii) the Independent Director Mr. Francisco Javier de Paz Mancho as a member and Chairman of the Nominating, Compensation and Corporate Governance Committee.

In addition, the Board of Directors agreed to call the Annual General Shareholders' Meeting which was held in Madrid, at the Recinto Ferial de la Casa de Campo, Pabellón de Cristal, Avenida de Portugal, sin número, at 1:00 p.m. on the second call on 12 May 2016.

- On 27 April 2016, the Board of Directors of Telefónica, S.A. resolved to adopt the following resolutions:
 - To appoint Ms. Sabina Fluxà Thienemann (Independent Director) as a member of the Nomination, Compensation and Corporate Governance Committee, and Mr. Javier de Paz Mancho (Independent Director) as a member of the Audit and Control Committee.
 - For Mr. Javier de Paz Mancho to cease as member of Service Quality and Customer Service Committee.
 - To reorganise the current Regulation and Institutional Affairs Committees so as to become a single Committee, under the name "Regulation of Institutional Affairs Committee".
 - To reorganise the current Strategy and Innovation Committees so as to become a single Committee, under the name "Strategy and Innovation Committee", and to appoint Mr.

Juan Ignacio Cirac Sasturain (Independent Director) and Mr. Peter Löscher (Independent Director) as members of such Committee.

- On 11 May 2016, Telefónica S.A. announced the decision of the European Commission to prohibit the potential acquisition by Hutchison Whampoa Group of the Telefónica subsidiary in the UK (O2 UK) under EU Merger Regulation.
- On 12 May 2016, further to Relevant Events notices published on 8 April 2016, Telefónica S.A. announced the holding of the Annual General Shareholders' Meeting of Telefónica S.A. at second call with the attendance, present or represented, of shareholders holding shares representing 56.13 % of the share capital of the Company, which approved by a majority of votes all the resolutions submitted by the Board of Directors for deliberation and vote by the General Shareholders' Meeting.

The meeting approved, among others, the following resolutions: the appointment of PricewaterhouseCoopers Auditores, S.L. as statutory auditor for the Annual Accounts of Telefónica, S.A. and its Consolidated Group of Companies for the years 2017, 2018 and 2019; the re-election as Director of Mr. Isidro Fainé Casas, Mr. Julio Linares López, Mr. Peter Erskine and Mr. Antonio Massanell Lavilla; and the ratification of the interim appointment as Director of each of Mr. Wang Xiaochu, Ms. Sabina Fluxà Thienemann, Mr. José Javier Echenique Landiribar, Mr. Peter Löscher and Mr. Juan Ignacio Cirac Sasturain.

Furthermore, the Company announced that, according to the shareholder remuneration policy, a dividend distribution was agreed, charged to Unrestricted Reserves, of a fixed gross amount of 0.40 Euro for each Company share issued, in circulation and carrying entitlement to such distribution. The payment of this dividend was executed on 19 May 2016.

- On 29 June 2016, following the European Commission's decision to prohibit the sale of O2 UK to the Hutchison Whampoa Group, the Board of Directors agreed that Telefónica will continue to explore different strategic alternatives for O2 UK, to be implemented when market conditions are deemed appropriate. Given that the execution of a transaction for sale is now less certain, Telefónica's operations in the United Kingdom have ceased to be presented as discontinued operations and its assets and liabilities are no longer classified as held for sale. Thus, items are presented line by line in the condensed consolidated interim financial statement and comparative figures have been presented accordingly. The impacts of this classification change are described in note 14 of the condensed consolidated interim financial statements.
- On 10 July 2016, Telefónica Internacional, S.A.U. (a 100% subsidiary of Telefónica, S.A.) proceeded with the sale of 361,794,559 shares of China Unicom (Hong Kong) Limited ("**China Unicom HK**"), representing 1.51% of the share capital of the company, by a block trade process, at a price of 7.80 Hong Kong dollars per share, for a total amount of 2,822 million Hong Kong dollars, approximately €322 million. Telefónica maintains a stake of close to 1% in China Unicom HK.
- On 5 September 2016, Telefónica, S.A. announced its intention to proceed with an offering (the "**Offering**") of shares of its telecommunications infrastructure subsidiary Telxius Telecom, S.A.U. ("**Telxius**"), addressed to qualified investors. The Offering is expected to take place during the second half of 2016, following receipt of the approval by the Comisión Nacional del Mercado de Valores of the Offering prospectus. Telxius intends to apply for the listing of its shares on the Barcelona, Bilbao, Madrid and Valencia stock exchanges, as well as their inclusion in the Spanish electronic trading system (Continuous Market). The free float of Telxius will be at least of 25%, the minimum legally required for the listing, and, at the same time, will enable Telefónica, S.A. to maintain a majority stake in Telxius immediately after the Offering.
- On 5 September 2016, Telefónica, S.A. announced that it is considering various strategic options with respect to Telefónica's United Kingdom subsidiary (O2 UK), (all of which would involve Telefónica maintaining a majority shareholding), including, among others, a potential Initial Public Offering. Preparatory work in connection with such strategic options has been initiated.

Business Overview

Highlights

Telefónica's total accesses totalled 347.5 million as of 30 June 2016. Group accesses decreased by 2.0% affected, in part, by prepaid disconnections in Telefónica Brazil (which resulted in the disconnection of 11.5 million accesses during 2015). In 2016, commercial activity increased based on high value customers, resulting in a sustained growth of the contract mobile segment (smartphones and LTE), fiber and Pay TV. Accesses in Telefónica Hispanoamérica (38.8% of the Group's total as of 30 June 2016) increased by 1.6% year-on-year and accesses in Telefónica United Kingdom (7.3% of the Group's total as of 30 June 2016) increased by 1.5% year-on-year and accesses in Telefónica Germany (14.0% of the Group's total as of 30 June 2016) increased by 1.2% year-on-year.

The below table shows the evolution of Group accesses in the first half of 2016 compared to the first half of 2015:

ACCESSES	June		(%)
	2015	2016	YoY
	<i>(thousands)</i>		
Fixed telephony accesses(1).....	40,400.0	39,262.1	(2.8%)
Internet and data accesses	21,249.6	21,641.4	1.8%
Broadband.....	20,775.2	21,195.9	2.0%
Fiber & VDSL	6,386.4	8,362.0	30.9%
Mobile accesses	278,414.0	272,596.8	(2.1%)
Prepay	177,429.1	165,619.6	(6.7%)
Contract	100,984.8	106,977.2	5.9%
M2M.....	10,681.6	12,988.2	21.6%
PayTV.....	8,030.3	8,422.0	4.9%
Final Clients Accesses	348,093.8	341,922.3	(1.8%)
Wholesale Accesses	6,401.0	5,591.7	(12.6%)
Total Accesses	354,494.8	347,514.0	(2.0%)

Notes:

- Accesses include Telefónica United Kingdom accesses since 2015 as the United Kingdom group has been classified as a continuing operation.
- (1) Includes "fixed wireless" and Voice over IP accesses.

The Group's strategy is based on capturing growth in its markets, especially on attracting high-value customers.

Mobile accesses totalled 272.6 million as of 30 June 2016, down 2.1% compared to 30 June 2015, affected mainly by the decrease in prepay accesses due to the disconnection of prepay accesses in Brazil (11.5 million accesses in 2015). Contract accesses, however, were up 5.9% year-on-year, continuing to increase their weight over total mobile accesses up to 39.2% (+3.0p.p. year-on-year).

Smartphone accesses maintained a strong growth rate (up 18.1% year-on-year), totalling 130.1 million accesses as of 30 June 2016 and reaching a penetration rate over total accesses of 51.1% (+9.0p.p. year-on-year), reflecting the Company's strategic focus on the growth of its data services.

Fixed broadband accesses stood at 21.2 million at 30 June 2016, up 2.0% year-on-year. Fiber accesses stood at 6.8 million at 30 June 2016.

TV accesses totalled 8.4 million as of 30 June 2016, up 4.9% year-on-year.

2016/2015 SEGMENT RESULTS

TELEFÓNICA SPAIN

The below table shows the evolution of accesses in Telefónica Spain over the first half of 2016 compared to the first half of 2015:

	June		%
	2015	2016	YoY
ACCESSES	<i>(thousands)</i>		
Fixed telephony accesses ⁽¹⁾	10,126.6	9,854.2	(2.7%)
Internet and data accesses.....	5,905.1	6,061.6	2.7%
Broadband	5,861.0	6,030.2	2.9%
Fiber	1,720.7	2,675.7	55.5%
Mobile accesses.....	17,330.7	17,094.4	(1.4%)
Prepay.....	2,989.1	2,579.7	(13.7%)
Contract.....	14,341.6	14,514.7	1.2%
M2M	1,726.5	1,890.5	9.5%
Pay TV	3,595.7	3,755.0	4.4%
Final Clients Accesses	36,958.2	36,765.2	(0.5%)
Wholesale Accesses	5,286.7	4,693.3	(11.2%)
Total Accesses.....	42,244.9	41,458.6	(1.9%)

Notes

⁽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.

During 2016 the commercial activity of Telefónica continues to leverage on its differentiated assets which, in the second half of 2015, were strengthened by the convergent offer "Movistar Fusión+" launched in July 2015. During the first half of 2016 the tariffs of the consumer segment, fundamentally broadband, postpaid mobile and "Fusion" have been revised, maintaining the positive trend aligned with the new cycle of growth.

Churn evolution has been positive during the first half of 2016, especially taking into account the elimination of "Fusión" long-term contracts on 1 August 2015.

In the first half of 2016, the **retail broadband accesses** increased their growth up to 2.9%, with positive net adds of 68 thousand in the first half of 2016, due to churn improvement in this period and online non convergent broadband promotions. The fiber net adds grew by 12.1%, mobile contract net adds grew by a further 0.2 million customers year-on-year. There has also been a positive evolution of the second mobile line included in "Fusión+ Contigo" since its launch on 1 June 2016. Fixed accesses decreased its net loss by 52.9% year-on-year.

Telefónica Spain had 41.5 million **accesses** as of 30 June 2016, down 1.9% compared to 30 June 2015, explained by the decrease in mobile accesses and fixed telephony accesses with retail accesses down 0.5% year-on-year.

Consumer "Movistar Fusión", with a customer base of 4.3 million with 2.1 million additional wireless lines to the base offer as of 30 June 2016, maintained a solid year-on-year growth (+10% and +9% respectively year-on-year) and contributed 82% of the fixed retail broadband customer base (+5p.p. year-on-year) and 70% of the wireless contract customer base (+6p.p. year-on-year). There was significant growth in the penetration of the high value services of "Movistar Fusión", with 32% of the customer base already using 100 Mb or 300 Mb ultra-fast broadband (+7 p.p. year-on-year) and 67% of the customer base with Pay-TV as of 30 June 2016 (+15p.p. year-on-year).

Fixed accesses decreased 3% year-on-year, with a net loss of 151 thousand accesses in the first half of 2016. This decrease was mainly due to a lower fixed access market.

Retail broadband accesses totalled 6.0 million and grew 2.9% year-on-year as at 30 June 2016, with net adds of 68 thousand accesses, due to the lower churn (1.4% as of 30 June 2016, -0.05p.p. year-on-year) and on-line non convergent broadband promotions.

Fiber accesses reached 2.7 million customers (1.6 times compared to 30 June 2015), representing 44% of total broadband customers (+15p.p. year-on-year) with net adds of 453 thousand accesses in the first half of 2016. Ultra speed fiber accesses, with 100 or 300 Mb (with additional ARPU of 10 euros, including VAT) reached 1.7 million accesses (65% of total fiber accesses). At 30 June 2016 the fiber deployment had reached 15.7 million premises, 3.2 million more than at 30 June 2015, and continues to be the largest in Europe.

Total **mobile accesses** stood at 17.1 million as of 30 June 2016, down 1.4% compared to 30 June 2015 as a result of the decrease in prepay accesses. The contract access base accelerated its growth during the first half of 2016, growing by 1.2% year-on-year. Smartphone penetration as of 30 June 2016 stood at 68.3% of the mobile voice base (+4.3p.p. compared to 30 June 2015) and significantly boosted data traffic growth to 49% year-on-year due to the higher number of customers with the renewed portfolio containing superior data packages.

LTE network rollout continued to progress well and coverage reached (based on Telefónica's estimates) approximately 86% of the population at 30 June 2016, up 24 percentage points compared to 30 June 2015, due to the deployment of the 800 MHz. As a result, the LTE customer base reached 5.0 million customers as of 30 June 2016, doubling the customer base at 30 June 2015, while the penetration reached 33% (+17p.p. year-on-year).

Pay-TV accesses reached 3.7 million at 30 June 2016, up by 4.4% year-on-year, including 750 thousand satellite TV accesses from DTS.

Fusion ARPU was 79 euros in the first six months of 2016, up 12.9% year-on-year in reported terms, boosted by the demand of higher value packages and the tariff revisions in May 2015 and February 2016

	June		%
	2015	2016	YoY
TELEFÓNICA SPAIN			
Voice Traffic (millions of minutes)	84,018	78,015	(7.1%)
ARPU Fusión (EUR)	70.0	79.0	12.9%
% non-SMS over data revenues	95.5%	95.3%	(0.2 p.p.)

TELEFÓNICA UNITED KINGDOM

The below table shows the evolution of accesses in Telefónica United Kingdom of the first half of 2016 compared to the first half of 2015:

	June		%
	2015	2016	YoY
ACCESSES	<i>(thousands)</i>		
Fixed telephony accesses ⁽¹⁾	235.4	257.7	9.5%
Internet and data accesses	20.4	22.3	9.8%
Broadband	20.4	22.3	9.8%
Mobile accesses	24,816.5	25,172.5	1.4%
Prepay ⁽²⁾	10,793.1	9,745.8	(9.7%)
Contract	14,023.4	15,426.7	10.0%
M2M ⁽³⁾	2,234.2	3,176.8	42.2%
Final Clients Accesses	25,072.2	25,452.6	1.5%
Total Accesses	25,072.2	25,452.6	1.5%

Notes:

⁽¹⁾ Includes "fixed wireless" and Voice over IP accesses.

⁽²⁾ Includes the disconnection of 720 thousand inactive prepay customers in the first half of 2016.

⁽³⁾ Includes 720 thousand M2M accesses on the Jasper platform since the first half of 2016.

During the first six months of 2016 Telefónica United Kingdom maintained market momentum which has been underpinned by the strength of the O2 brand, successful commercial propositions and customer loyalty, factors that allowed Telefónica to deliver continued strong customer growth in a competitive market.

Total accesses increased by 1.5% year-on-year to 25.4 million as of 30 June 2016, mainly boosted by a 1.4% growth in the mobile customer base (25.2 million).

Contract **mobile accesses** increased by 10,0% year-on-year to 15.4 million by the end of June 2016 increasing their proportion over the total mobile accesses to 61.3% driven by the inclusion of 720 thousand M2M accesses from the Global platform that have not previously been accounted. Net mobile adds in the first half of 2016 reached 154 thousand accesses driven by the solid contribution of the postpay segment. Smartphone penetration (as a percentage of mobile internet data tariff over total mobile customers) rose 12.5 percentage points year-on-year to 62.4%, triggered by the continued expansion of LTE customers base (64% year-on-year growth and 9.5 million by 30 June 2016). LTE penetration now represents 43% of the mobile base.

Prepay accesses decreased by 9.7% year-on-year to 9.7 million customers by the end of June 2016 including the disconnection of 720 thousand inactive accesses during the first six months of 2016.

Mobile **ARPU** fell by 7.7% year-on-year in reported terms mainly due to the depreciation of the pound sterling. In organic terms, ARPU decreased by 1,8% negatively affected by the "Refresh" model despite the fact that the Data ARPU grew by 0.7% year-on-year, driven by the increase in the smartphone penetration. Revenues from the "Refresh" model are not recognised as mobile service revenues, and are instead recognised under the item line revenues from hardware sales, for which reason smartphone sales are not reflected in ARPU.

	June		% Organic
	2015	2016	YoY
TELEFÓNICA UNITED KINGDOM			
Voice Traffic (millions of minutes)	45,132	46,389	2.8%
ARPU (EUR)	19.2	17.7	(1.8%)
Prepay	7.5	7.7	9.9%
Contract (1)	33.3	29.9	(4.8%)
Data ARPU (EUR)	11.2	10.6	0.7%
% non-SMS over data revenues	58.9%	60.4%	1.5p.p.

Notes:

(1) Excludes M2M

TELEFÓNICA GERMANY

The below table shows the evolution of accesses in Telefónica Germany of the first half of 2016 compared to the first half of 2015:

ACCESSES	June 2015	June 2016	% YoY
Thousands of accesses			
Fixed telephony accesses ⁽¹⁾	2,009.7	2,007.4	(0.1%)
Internet and data accesses	2,354.7	2,329.8	(1.1%)
Broadband	2,115.2	2,103.9	(0.5%)
VDSL	379.8	669.3	76.2%
Mobile accesses	42,617.0	43,417.8	1.9%
Prepay	23,500.9	23,814.2	1.3%
Contract ⁽²⁾	19,116.1	19,603.6	2.6%
M2M	506.2	704.3	39.1%
Final Clients Accesses	46,981.4	47,754.9	1.6%
Wholesale Accesses	1,059.3	850.1	(19.7%)
Total Accesses	48,040.7	48,605.0	1.2%

Notes:

(1) Includes "fixed wireless" and Voice over IP accesses.

(2) In the fourth quarter of 2015, 400 thousand inactive customers were disconnected.

In the first half of 2016, Telefónica Germany maintained market momentum and continues to grow its customer base in an environment of intense mobile market competition, with aggressive pricing in non-premium products.

The **total access** base grew 1.2% year-on-year and stood at 48.6 million at the end of June 2016, mainly driven by a 1.9% increase in the mobile base (which reached 43.4 million).

The **contract mobile customer base** grew 2.6% year-on-year and reached 19.6 million accesses, increasing the share over the total mobile base up to 45.2%. Net adds reached 520 thousand accesses due to the solid contribution of partners (second brands). Smartphone penetration reached 56.2% of the total mobile access base, up 5.0 percentage points year-on-year driven by the continued growth of LTE customers (+54.0% year-on-year reaching 9.4 million at the end of June 2016). LTE penetration reached 22.0% of the total mobile access base.

The **prepay access** base increased 1.3% year-on-year to 23.8 million. Prepay posted a net loss of 165 thousand customers in the first half of 2016, mainly due to disconnections in the first few months of the year.

The **retail broadband accesses** grew by 6,000 accesses in the first half of the year, changing the trend of previous years. VDSL was once again the main growth engine of fixed performance with 152 thousand net additions (+23.6% year-on-year) in the first half of 2016.

Mobile ARPU was 10.3 euros (-3.5% year-on-year), while contract ARPU stood at 16.1 euros (-4.2% year-on-year), as a result of the higher share of second brands in the customer base. Data ARPU was 5.7 euros (+3.7% year-on-year), as a result of the steady increase of non-SMS data revenues.

	June		%
	2015	2016	YoY
TELEFÓNICA GERMANY			
Voice Traffic (millions of minutes)	60,103	58,251	(3.1%)
ARPU (EUR)	10.7	10.3	(3.5%)
Prepay	5.8	5.7	(0.8%)
Contract ⁽¹⁾	17.2	16.6	(3.5%)
Data ARPU (EUR)	5.5	5.7	3.5%
% non-SMS over data revenues	71.0%	76.1%	5.1p.p.

⁽¹⁾ Excludes M2M.

TELEFÓNICA BRAZIL

The below table shows the evolution of accesses in Telefónica Brazil for the first half of 2016 compared to the first half of 2015:

ACCESSES	June		%
	2015	2016	YoY
	<i>(thousands)</i>		
Fixed telephony accesses ⁽¹⁾	14,869.6	14,742.1	(0.9%)
Internet and data accesses	7,224.0	7,321.8	1.4%
Broadband.....	7,092.4	7,263.5	2.4%
Fiber.....	3,640.8	3,983.6	9.4%
Mobile accesses	82,648.6	73,296.1	(11.3%)
Prepay	53,068.7	41,669.4	(21.5%)
Contract	29,580.0	31,626.7	6.9%
M2M.....	3,935.2	4,590.3	16.6%
Pay TV.....	1,785.9	1,761.4	(1.4%)
Final Clients Accesses	106,528.1	97,121.4	(8.8%)
Wholesale Accesses	23.6	20.7	(12.1%)
Total Accesses	106,551.7	97,142.1	(8.8%)

⁽¹⁾ Includes "fixed wireless" and Voice over IP accesses.

Results for the first half of 2016 were adversely affected by the interconnection tariff reduction implemented on 24 February 2016 in the mobile business (-33.8%), fixed-mobile tariff (-20.6%), fixed-local (-65.9%) and fixed interurban (-21.3%).

Telefónica Brazil reached 97.1 million **accesses** at 30 June 2016, down 8.8% compared to 30 June 2015 due mainly to a more restrictive calculation of prepaid customer base from 2015, resulting in a decrease of 11.3% year-on-year.

In the **mobile business**, the strategic focus remained on gaining and retaining high value customers, reaching a market share of 42.3% in the contract segment as of 31 May 2016 (latest data available; Source: ANATEL). Telefónica Brazil maintained its market leadership in terms of total accesses with a market share of 28.7% as of 31 May 2016 (latest data available; Source: ANATEL). The commercial offer in the contract segment included a higher data volume, more minutes of voice traffic and innovative products such as "Vivo Bis" (pursuant to which the data not consumed in a month is automatically added to data available for the following month). The contract growth was partially offset by the disconnection of 11.5 million prepaid accesses.

In the **fixed business**, Telefónica Brazil maintained its strategic focus on fiber deployment, with 16.1 million premises passed with FTTx at 30 June 2016 and 4.0 million homes connected, which together with the fixed-mobile substitution resulted in a decrease of 3.5 % in fixed telephony accesses. Retail broadband customers totalled 7.3 million customers in the first half of 2016, up 2.4% year-on-year. Of the 7.3 million customers at the end of June 2016, 55.0% were connected with FTTC. Pay TV customers stood at 1.8 million as of 30 June 2016, decreasing 1.4% year-on-year due to a higher penetration of high value and IPTV customers. IPTV accesses increased their relevance, representing 11% of total Pay-TV accesses.

The **mobile ARPU** decreased by 7.9% year-on-year in reported terms due mainly to the depreciation of the Brazilian real. In organic terms, mobile ARPU increased by 16.1% year-on-year as a consequence of the higher data ARPU which offset the negative impact of the reduction in the mobile termination rates. The high quality of the customer base is reflected in an increase in the outbound ARPU and the 39% growth in data ARPU.

	June		%	% Local Currency
	2015	2016	YoY	YoY
TELEFÓNICA BRAZIL				
Voice Traffic (millions of minutes)	189,485	186,804	(1.4%)	(1.4%)
ARPU (EUR)	6.9	6.4	(7.1%)	16.1%
Prepay	3.5	3.3	(5.7%)	18.0%
Contract ⁽¹⁾	14.7	12.0	(18.2%)	2.2%
Data ARPU (EUR)	3.0	3.3	11.4%	39.0%
% non-SMS over data revenues	82.1%	86.5%	4.4p.p.	4.2p.p.

⁽¹⁾ Excludes M2M.

TELEFÓNICA HISPANOAMÉRICA

The below table shows the evolution of accesses in Telefónica Hispanoamérica of the first half for 2016 compared to the first half of 2015:

	June		%
	2015	2016	YoY
ACCESSES	<i>(thousands)</i>		
Fixed telephony accesses ⁽¹⁾	13,158.7	12,400.6	(5.8%)
Internet and data accesses	5,573.4	5,772.1	3.6%
Broadband	5,514.1	5,642.2	2.3%
Mobile accesses	110,866.4	113,344.0	2.2%
Prepay	87,077.4	87,810.5	0.8%
Contract	23,789.1	25,533.6	7.3%
M2M	2,144.8	2,354.3	9.8%
Pay TV	2,648.6	2,905.6	9.7%
Final Clients Accesses	132,247.2	134,422.4	1.6%
Wholesale Accesses	31.4	27.5	(12.3%)
Total Accesses T. Hispanoamérica	132,278.6	134,449.9	1.6%

⁽¹⁾ Includes "fixed wireless" and Voice over IP accesses.

Total accesses in Telefónica Hispanoamérica reached 134.4 million at 30 June 2016 (+1.6% year-on-year).

Mobile accesses totalled 113.3 million and grew by 2.2%, highlighting the increase of the quality of the customer base.

- The contract segment grew by 7.3% year-on-year. Growth was particularly strong in Peru (+11.5% year-on-year), Mexico (+24.4% year-on-year) and Chile (+8.5% year-on-year). Net adds at 30 June 2016 reached 564 thousand accesses, primarily due to Peru (+210 thousand net adds) and Chile (+165 thousand net adds), both benefiting from a successful migration strategy (from prepay to contract) and a higher volume in net adds. Colombia also showed positive net adds (+110 thousand accesses) due to higher commercial activity.
- The prepay accesses grew by 0.8% year-on-year, with net loss of 522 thousand customers. This decrease was driven mainly by Argentina (-583 thousand customers), Chile (-845 thousand customers) and Peru (-785 thousand customers), explained by the competitive environment in the prepay segment, which was not followed by Movistar to avoid damaging the quality of the network (preventing low price offers), and the focus on value customers that allowed the acceleration of the migration processes from prepay to contract. The positive net adds of Mexico (+1.0 million accesses) were not enough to offset the total negative net adds.
- Smartphone base grew (+21.6% year-on-year), totalling 43.1 million accesses in June 2016, with a penetration over mobile accesses of 39.3% (+6.2p.p. year-on-year), mainly related to the growth in all the countries in the region except for Chile. At the same time, the 4G handsets also continued to grow, reaching 11 million accesses as of 30 June 2016.

Traditional **fixed business accesses** stood at 12.4 million at 30 June 2016 (-5.8% year-on-year), with negative net adds of 429 thousand customers, affected by the erosion of traditional fixed business in the region, including Mexico (-19.4% year-on-year), Chile (-6.4% year-on-year), Peru (-4.4% year-on-year), Colombia (-3.3% year-on-year) and Argentina (-2,5% year-on-year).

Broadband accesses totalled 5.6 million at 30 June 2016 (+2.3% year-on-year), due mainly to access growth in Peru (+6.1%), Chile (+1.0%) and Colombia (+1.2%). The penetration of fixed broadband accesses over traditional fixed business accesses was 45.5% at 30 June 2016 (+3.6p.p. year-on-year). There was progressive migration towards data plans with higher speeds, with 56.2% of broadband accesses having a speed over 4Mb at 30 June 2016 (+5p.p. year-on-year).

Pay TV accesses totalled 2.9 million (+9.7% year-on-year), with net adds of 93 thousand accesses as a result of a higher customer base in all countries in the region that offer the service. Growth was particularly positive in Peru (+14.7%), Colombia (+17.1%) and Chile (+3.5%).

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 SMS and 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 and Germany). Telefónica also offers VoIP services in some markets.
- *Data and business-solutions services:* The data and business-solutions services principally include leased lines; virtual private network, or VPN, services; fiber optics services; the

provision of hosting and application, or ASP, service, including web hosting, managed hosting, content delivery and application, and security services; outsourcing and consultancy services, including network management, or CGP; and desktop services and system integration and professional services.

- *Wholesale services for telecommunication operators:* The wholesale services for telecommunication operators principally include domestic interconnection services; international wholesale services; leased lines for other operators' network deployment; and local loop leasing under the unbundled local loop regulation framework). It also includes bit stream services, bit stream naked, wholesale line rental accesses and leased ducts for other operators' fiber deployment.

Digital services

The main highlights in services developed by Telefónica Digital are:

- *Video/TV services:* IPTV services (Internet protocol), over-the-top network television services, and cable and satellite TV. In certain markets, advanced Pay-TV services are offered, such as high-definition TV (HDTV), Multiroom (allowing clients to watch different TV channels in different rooms) and Digital Video Recording (DVR).
- *Internet of Things ("IoT") Portfolio:* includes IoT horizontal solutions (managed connectivity, managed data and managed devices). In this space, "Smart M2M" is Telefónica's own platform and a key asset. Additionally, Telefónica offers key core end to end solutions in the fields of Smart Mobility, Smart Cities, Smart Retail and Smart Energy, and new businesses like Smart Industry, Smart Health, among others. In these spaces Telefónica offers full end to end solutions: "device + connectivity + application".
- *e-Health services or telecare:* A set of services intended to help to support usual healthcare practice through electronic and communication processes, that are aimed at leading to healthcare sector costs and time optimisation for all agents involved, workers and patients. They include remote chronic patient management, telecare services allowing tele-assistance through connectivity services, emergencies and medical appointments management and Digital Imaging.
- *Financial services and other payment services:* These services allow merchants and financial institutions to make and receive payments.
- *Security services:* A broad set of facilities and services (Managed Security, Cloud and Comms Security, Cybersecurity (threats, vulnerabilities and antifraud platforms)) which aim to protect information stored in different end customers' devices and networks from unauthorised access, use, disclosure, disruption or destruction, and including 11Paths developed services such as Latch, FaasT, Metashield or Tacyt.
- *Cloud computing services:* Telefónica offers a broad set of products and services to large enterprises which are focused on "Managed Cloud Services" and aims to build fully managed infrastructure environments and manage the complex tools and applications that run on top of the IT infrastructure, and small and medium-sized businesses including different SaaS bundles services with communications services that aim to expand customer digital presence and increase the employees' productivity and collaboration.
- *Advertising:* A portfolio of marketing channels that third party brands can use to acquire and engage with customers. Traditional channels such as messaging may be utilised alongside new channels like programmatic display and sponsored connectivity. These are powered by Telefónica's in-house technologies; SMS, bulk SMS, mobile portals- and fuelled by its customer data.
- *Big Data:* Includes the product "Smart Steps" which helps retailers, municipalities and public security bodies to understand the influx of people. Anonymous mobile data network and aggregates are used to calculate the influx of people in an area. Telefónica also offers B2B opt-in services to the financial sector (Risk Management) for improving fraud prevention and credit

scoring in Brazil, United Kingdom and Chile. Recently a Smart Steps joint venture has been launched with China Unicom based out of Beijing to sell data insights in China.

- *Future Communications*: Includes "TU Go", Movistar's exclusive application that lets clients have the same number on all their devices and communicate among such devices via Wi-Fi.

Sales and Marketing

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

Competition

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

Telefónica competes in its markets on the basis of the price of its services; the quality and range of features; the added value Telefónica endeavours to offer with its service; additional services associated with those main services; the reliability of its network infrastructure and its technological attributes; and the desirability of its offerings, including bundled offerings of one type of service with another and, in the case of the mobile industry, in most of the markets offerings that include 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 Company may not be able to adequately foresee and respond to technological changes and sector trends"*.

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 Telefónica increased its voting interest in the share capital of China Unicom to 8.06% and China Unicom obtained 0.87% voting interest in Telefónica's 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 initial term of the strategic alliance agreement between Telefónica and China Unicom terminated on 6 September 2012 and it is subject to automatic annual renewals, 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 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 in control of China Unicom.

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

On 10 June 2012, Telefónica S.A., through its 100% subsidiary, Telefónica Internacional, S.A.U., and China United Network Communications Group Company Limited through a 100% owned subsidiary, signed an agreement for the acquisition by the latter company of 1,073,777,121 shares of China Unicom HK, 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.

On 10 November 2014, Telefónica, through its 100% subsidiary, Telefónica Internacional, S.A.U., sold 597,844,100 shares of China Unicom, representing 2.5% of the share capital of the company, by means of a block trade, 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 continues to maintain its commitment to the strategic alliance with China Unicom.

Recently a Smart Steps joint venture has been launched with China Unicom based in Beijing to sell data insights in China.

On 10 July 2016, Telefónica Internacional, S.A.U. (100% subsidiary of Telefónica, S.A.) proceeded with the sale of 361,794,559 shares of China Unicom HK, representing 1.51% of the share capital of the company via a block trade process, at a price of 7.80 Hong Kong dollars per share, for a total amount of 2,822 million Hong Kong dollars (approximately €322 million). After the reclassification of losses included in other comprehensive income, the sale will have a negative impact in the consolidated profit for the year in the amount of €123 million.

As of the date of this Prospectus, Telefónica's shareholding in China Unicom amounts to close to 1% of its capital stock. Furthermore, Mr. César Alierta, chairman of Telefónica, is a member of the Board of Directors of China Unicom while Mr. Wang Xiaochu, chairman of China Unicom, is a member of the Board of Directors of Telefónica.

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 they are present.

Based on the advice of its legal counsel, Telefónica believes it is reasonable to assume that these legal proceedings will not materially affect its financial condition or solvency, regardless of the outcome.

Telefónica highlights the following unresolved legal proceedings or those underway in 2015 (see Note 17 to the 2015 Consolidated Financial Statements for details of tax-related cases).

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 legal process ended on 25 June 2015, when the German Federal Constitutional Court dismissed the appeal lodged by Quam against the decision to reverse the UMTS licence issued by the regulatory authority and endorsed by the courts in their different instances.

This judgment is not subject to appeal.

Appeal against the decision by ANATEL regarding the inclusion of interconnection and network usage revenues in the Fundo de Universalização de Serviços de Telecomunicações

Vivo Group operators (currently Telefônica de Brasil), together with other cellular operators, appealed ANATEL's decision of 16 December 2005, to include interconnection and network usage revenues and expenses in the Fund for Universal Access to Telecommunications Services ("FUST") calculation of the amounts payable into the FUST – a fund which covers 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 favor 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, which was dismissed. ANATEL filed an appeal against this resolution.

At the same time, Telefônica Brasil and Telefónica Empresas, S.A., together with other wireline operators through *Associação Brasileira de Concessionárias de Serviço Telefônico Fixo Comutado ("ABRAFIX")* 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, which was dismissed by a decision of 10 May 2016. ANATEL filed an appeal against this decision.

The wireline fixed operators have filed an appeal for clarification that the FUST cannot be collected on income earned by Interconnection and Operating Leased Line Connection. They have also asked the Court to rule on two legal foundations that were not analysed in the judgment: that the FUST has become obsolete, among other reasons, because of the advance of mobile telephony; and what is collected does not apply to the purpose for which it was created, as only a very small percentage of the amount collected by the FUST is used in financing fixed telephony.

The amount of the claim is quantified at 1% of the interconnection revenues.

Public civil procedure by the São Paulo government against Telefônica Brasil for alleged reiterated malfunctioning in services provided

This proceeding was filed by the Public Ministry of the State of São Paulo for alleged reiterated malfunctioning in the services provided by Telefônica Brasil, seeking compensation for damages to the customers affected. A general claim was filed by the Public Ministry of the State of São Paulo, for 1 billion Brazilian reais (approximately €225 million), calculated on the company's revenue base over the last five years.

In April 2010, a ruling against the Telefónica Group was issued in the first instance. The full impact of this proceeding will not be known until there is a final ruling, and the total amount of persons affected by and party to the proceeding is known. At that moment, the amount of the indemnity will be established, ranging between 1 billion and 60 million reais (approximately, between €225 and €13 million), depending on the number of parties. On 5 May 2010, Telefônica Brasil filed an appeal before the São Paulo Court of Justice, suspending the effect of the ruling.

On 13 April 2015, the appeal was judged in favour of Telefonica, by unanimous vote, reversing the earlier decision in first instance.

The Public Prosecutor filed an extraordinary petition for review at the High Court of Brasilia, who dismissed the appeal on the basis of the absence of necessary legal requirements for filing. Against this resolution, a new appeal can be filed.

Appeal against the decision of 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 European Commission initiated formal proceedings to investigate whether Telefónica S.A. and Portugal Telecom SGPS, S.A. ("**Portugal Telecom**") had infringed 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 which was the owner of the Brazilian company Vivo.

On 23 January 2013, the European Commission passed a ruling on the formal proceedings. The ruling imposed a fine on Telefónica of €67 million, as the European Commission ruled that Telefónica and Portugal Telecom committed an infraction of 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 referred to above.

On 9 April 2013, Telefónica filed an appeal for annulment of this ruling with the European Union General Court. On 6 August 2013, the European Union General Court notified Telefónica of the response issued by the European Commission, in which the European Commission reaffirmed the main arguments of its ruling and, specially, that Clause Nine includes a competition restriction. On 30 September 2013, Telefónica filed its reply. On 18 December 2013, the European Commission filed its appeal.

On 28 June 2016, the European Union General Court published its Decision on such appeal, in which, although it declared the existence of an infringement of competition law, it annulled Article 2 of the contested Decision, which determined the amount of the fine, and required the Commission to reassess the amount. The General Court determined that the Commission had not disproved the allegations or the evidence provided by Telefónica in its appeal concerning services where there was no potential competition or services that were outside the scope of the relevant provision. Telefónica believes that the sanctions are not consistent with the relevant legislation and therefore intends to file a further appeal before the Court of Justice of the European Union, within two months of notification of the abovementioned decision.

Judicial appeals against the decisions by the CADE regarding the acquisition by Telefónica, of stakes in Portugal Telecom and Telco

On 4 December 2013, the Brazilian Antitrust Regulator, CADE, announced the two following decisions:

Firstly, CADE approved, with the restrictions described further 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**").

This transaction had previously been approved by ANATEL and its closing (which did not require CADE's prior approval at the time), occurred immediately after ANATEL's approval was granted on 27 September 2010.

This decision was granted by CADE subject to the following conditions:

- (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.

Due to the fulfilment of the conditions set forth in the authorisations granted by ANATEL (on 22 December 2014 and 12 March 2015) and CADE (on 25 March 2015) for the acquisition by Telefônica Brasil of GVT, and for the demerger of Telco, the previously mentioned decision of CADE on 4 December 2013 was overridden due to Telefónica's divestment of its total shareholding in Telecom Italia.

In this regard, Telefónica, S.A. delivered 1,110 million ordinary shares of Telecom Italia (representing 8.2% of its ordinary shares) to Vivendi, S.A. in exchange for 4.5% of the total share capital of Telefónica Brasil and sold, by means of an agreement with a financing institution, 872 million ordinary shares of Telecom Italia, representing 6.5% of the ordinary shares of this company, for approximately €1,025 million.

Telefónica also arranged several hedging instruments to allow Telefónica to repurchase the shares of Telecom Italia that may be required to meet its exchange obligations under the mandatory exchangeable bonds for shares of Telecom Italia issued by Telefónica, S.A. in July 2014.

Telefónica has therefore completed the divestment process of its entire stake in Telecom Italia, in accordance with its regulatory and anti-trust commitments.

Secondly, CADE imposed a fine on Telefónica of 15 million Brazilian reais, for having allegedly breached the spirit and the purpose 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 and payment for non-voting shares of Telco in the capital increase carried out in accordance with the agreement dated 24 September 2013. This decision also requires Telefónica to divest such non-voting shares of Telco. As indicated above, the divestment by Telefónica of its entire stock participation in Telco and consequently in Telecom Italia has been completed.

On 9 July 2014, Telefónica filed a judicial appeal against the abovementioned decision to impose a fine on Telefónica.

Decision by the High Court regarding the acquisition by Telefónica of shares in Český Telecom by way of tender offer

Venten Management Limited ("**Venten**") and Lexburg Enterprises Limited ("**Lexburg**"), were minority shareholders of CESKY TELECOM. In September 2005 both companies sold their shares to Telefónica in a mandatory tender offer. Subsequently Venten and Lexburg, in 2006 and 2009, respectively, filed actions against Telefónica claiming a higher price than the price for which they sold their shares in the mandatory tender offer.

On 5 August 2016 the hearing before the High Court took place in order to decide the appeal against the second decision of the Municipal Court, which had been favourable to Telefónica's position (as was also the case with the first decision of the Municipal Court). At the end of the hearing, the High Court announced the Second Appellate Decision by which it reversed the second decision of the Municipal Court and ordered Telefónica to pay CZK 644,280,000 (ca. EUR 23,862,222) to Venten and CZK 227,760,000 (ca. EUR 8,435,555) to Lexburg, in each case plus interest. Now the Decision must be written and delivered to the parties, which is expected to happen in the second half of September 2016. Once delivered, an extraordinary appeal by the Company may be filed against the Second Appellate Decision.

Claim of consumers association "FACUA" against Telefónica de España In connection with the raising of the price of Movistar Fusión.

On 5 September 2016, notification was given to Telefónica de España of a claim against it filed by the consumers association "FACUA".

Through such claim, the association exercises an action to protect consumers' and users' collective interests stipulated in articles 11 of the Civil Procedure Act (*Ley de Enjuiciamiento Civil*) and 24.1 of the Consumer and Users Protection Act (*Ley General de Defensa de los Consumidores y Usuarios*) on the basis of alleged disloyalty towards the consumers, arising from the raising of the prices of the product "Movistar Fusión" from 5 May 2015 by an amount of 5 euros per month.

The claim exposes a first declaratory statement, stating that disloyalty is declared due to misleading advertising regarding the price rise, a second head claim of prohibitory injunction, requesting that Telefónica de España be ordered to discontinue the use of such price rise and to prohibit its future application to all customers who became customers of Movistar Fusion prior to 5 May 2015. It contains a third statement, requesting Telefónica de España to be condemned to repay the excess amounts collected as a result of the rise in prices for those customers who have chosen to maintain the service contracted, together with accrued interest on such amount.

The claim has been filed for an undetermined amount, given the impossibility of determining *a priori* the total amount of the claim. As of the date of this Prospectus, and without prejudice to the ongoing procedures, it should be noted that in the past few months many Courts of First Instance have provided rulings in similar cases, filed by clients on an individual basis, although promoted by FACUA, the majority of which have rejected such claims on the basis of a lack of justification of the intended invariance of the price and the legal raising of the prices agreed by the existing contracts (as of the date of this Prospectus, 21 decisions have rejected those claims).

Other Contingencies

Telefónica is currently conducting an internal investigation regarding possible violations of applicable anti-corruption laws. Telefónica has been in contact with governmental authorities about this matter and intends to cooperate with those authorities as the investigation continues. It is not possible at this time to predict the scope or duration of this matter or its likely outcome.

Tax Proceedings

Tax inspections in the tax group in Spain

With regard to the tax inspection for the years 2001 to 2004, the Supreme Court issued a ruling in 2015, accepting the tax losses incurred by the Group in relation to the transfer of certain interests in TeleSudeste, Telefónica Móviles México and Lycos as tax deductible, rejecting the other contentions, and therefore the contingencies related to this process disappeared. This has resulted in recognition of a tax expense of €49 million in the 2015 financial statements. However, this did not require payment of any additional tax because Telefónica applied unused tax loss carryforwards to offset the effect of these adjustments, at the corresponding tax rate for each period.

In 2012, tax inspections for all taxes for the years 2005 to 2007 were completed, with Telefónica signing off a corporate income tax assessment of €135 million, which was paid in 2012, whilst disputing other adjustments with which it disagreed. However, the settlement agreement for the disputed tax assessment did not give rise to any tax payment, since the adjustments proposed were offset by unused tax loss carryforwards, Telefónica filed an appeal with the Central Economic-Administrative Court against these adjustments in May 2015, regarding the tax treatment of the "juros sobre el capital propio" (interest on own capital) as dividends.

In July 2015, tax inspections for all taxes for the years 2008 to 2011 were completed, with Telefónica signing off certain corporate income tax assessments and disputing others. This resulted in an expense amounting to €206 million. However, this did not require any tax payment, as the adjustments arising from the inspection were offset by unused tax loss carryforwards, at the corresponding tax rate for each period.

Although the settlement agreement for the disputed tax assessment did not give rise to any tax payment, in July 2015 the company filed an appeal with the Central Economic-Administrative Court against the adjustments it disputes, regarding the tax treatment of the "juros sobre el capital propio" (interest on own capital) as dividends, and the criteria to use tax loss carryforwards in the years subject to settlement.

As at 31 December 2015, it was not expected that there would be any need to recognise additional liabilities for the outcome of this litigation.

Telefônica Brasil

The Telefónica Group is involved in a range of tax litigation in Brazil over direct and indirect taxes (including those relating to GVT). This includes a number of appeals relating to ICMS tax (a tax similar to VAT, levied on telecommunications services). There is a dispute with the Brazilian tax authorities over which services should be subject to settlement of this tax. In 2015 the tax authorities embarked upon a new round of inspections in this regard.

To date the most significant issues have focused on the requirement to collect ICMS on penalties charged to customers for non-compliance, Internet advertising services, and complementary or additional services to the basic telecommunications services such as value-added services and modem rental.

All related procedures are being contested in all instances (administrative and court proceedings). The aggregate amount of these assessments, updated to take into account interest, fines and other items, is approximately 11,900 million Brazilian reais (€2,750 million). No provisions have been set aside for these matters, as the risk of them giving rise to liabilities is not probable. Telefônica Brasil has obtained independent expert reports supporting its position, i.e. that the aforesaid services are not subject to ICMS.

Telefónica del Perú

With regard to tax matters in Peru, litigation continues over corporate income tax for 2000 and 2001, payments on account in respect of the year 2000, recoverable balances for 1998 and 1999, and the interest and penalties that should apply to these.

In August 2015, the court of second instance handed down a ruling partially upholding the position of Telefónica del Perú, ruling in its favor on three of the five objections filed by the tax authorities and appealed against to the courts, relating, inter alia, to corporate income tax for 2000-2001. This dispute accounts for more than 75% of the total amount under litigation, with the objections relating to insolvency provisions, interest on borrowing and leases of space for public telephones. Both the tax authorities and the company have filed appeals against the decision in higher courts.

At the date of this Prospectus, the settlements carried out by Superintendencia Nacional de Aduanas y de Administración Tributaria for 2000 and 2001 are in the final instance of the legal process (under review by the Supreme Court).

In general, the discussions over this litigation are taking place before the courts (not only through the current contentious-administrative appeals but also through constitutional protection suits, which are being heard in all instances in both cases). In connection with these proceedings in Peru, the Group and its legal advisors consider that the Group's position is based on robust legal arguments.

In parallel to the aforementioned court proceedings, the tax authorities proceeded to collect corporate income tax due for the years 2000-2001 and payments on account of corporate income tax in respect of the year 2000. There were successive reductions to the sums claimed in the two cases following appeals filed by Telefónica del Perú against the settlements and due to the precautionary measures imposed. The company paid out 286 million Peruvian soles (approximately, €80 million) in 2012 and 2013 pending the final rulings.

In the context of these execution processes, in June 2015, the tax authorities issued Compliance Resolutions demanding payment of 1,521 million Peruvian soles (approximately €431 million). An appeal has been filed against this with the Tax Court, and the adoption of precautionary suspension measures duly requested from the legal authorities (as a definitive court ruling on these cases is currently pending).

Given the sentences and rulings handed down in June and August 2015, the Group decided to recognise a provision in the accompanying 2015 Consolidated Financial Statements of €431 million (see Note 15 to the 2015 Consolidated Financial Statements).

In the first half of 2016 there were no new court rulings in connection with these proceedings. The Group and its legal advisors considers there are legal arguments that support their position.

Years Open for Inspection

The years open for review by the tax inspection authorities for the main applicable taxes vary from one consolidated company to another, based on each country's tax legislation, taking into account their respective statute-of-limitations periods. In Spain, following the tax audit completed in 2015, the taxes from 2012 onwards are open to inspection with respect to the main companies of the Spanish tax group.

In the other countries in which the Telefónica Group has a significant presence, the years open for inspection by the relevant authorities are generally as follows:

- The last twelve years in Germany.
- The last eight years in the United Kingdom.

- The last seven years in Argentina.
- The last five years in Brazil, Mexico, Uruguay, Colombia and the Netherlands.
- The last four years in Venezuela, Peru, Guatemala, Nicaragua and Costa Rica.
- The last three years in Chile, Ecuador, El Salvador, the United States and Panama.

The tax inspection of the open years is not expected to give rise to additional material liabilities for the Group.

Major Shareholders

At 26 February 2016, Telefónica had 4,975,199,197 shares outstanding, each having a nominal value of €1.00 per share. All outstanding shares have the same rights.

At 26 February 2016, according to information provided to us or to the Spanish National Securities Commission (*Comisión Nacional de Mercado de Valores*), beneficial owners of 3% or more of Telefónica's voting stock were as follows:

Name of Beneficial Owner	Number of Shares		Percent
	Direct	Indirect	
Banco Bilbao Vizcaya Argentaria, S.A. ⁽¹⁾	302,205,736	—	6.07%
Fundación Bancaria Caixa d' Estalvis i Pensions de Barcelona (" la Caixa ") ⁽²⁾ ...	—	249,501,612	5.01%
Blackrock, Inc. ⁽³⁾	—	253,632,799	5.09%

⁽¹⁾ Based on the information provided by Banco Bilbao Vizcaya Argentaria, S.A. as at 31 December 2015 for the 2015 Annual Report on Corporate Governance.

⁽²⁾ Based on information provided by la Caixa as at 31 December 2015 for the 2015 Annual Report on Corporate Governance. The indirect shareholding is held by Caixabank, S.A. which owns 249,482,489 shares and by Vidacaixa, S.A. de Seguros y Reaseguros which owns 19,123 shares.

⁽³⁾ According to the form on Schedule 13G filed on 9 February 2016 with the SEC. Though the reported beneficial ownership is 5.09%, Blackrock, Inc. has sole voting power with respect to 233,260,845 shares (representing 4.68% of Telefónica's share capital as of the date of such filing).

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.

Management of Telefónica

During 2015, the Board of Directors met 15 times. As at the date of this Prospectus, the Board of Directors had met eight times during 2016. As at 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. José María Álvarez - Pallete López ⁽¹⁾	12/12/1963	52	2006	2017
Vice-chairmen				
Mr. Isidro Fainé Casas ⁽¹⁾⁽²⁾	10/07/1942	74	1994	2020
Mr. José María Abril Pérez ⁽¹⁾⁽³⁾⁽⁶⁾	19/03/1952	64	2007	2018
Mr. Julio Linares López ⁽⁵⁾⁽⁸⁾	26/12/1945	70	2005	2020
Members (vocales)				
Mr. César Alierta Izuel	05/05/1945	71	1997	2017
Ms. María Eva Castillo Sanz ⁽⁵⁾⁽⁶⁾⁽⁸⁾	23/11/1962	53	2008	2018
Mr. Juan Ignacio Cirac Sasturain ⁽⁶⁾	11/10/1965	50	2016	2020
Mr. José Javier Echenique Landiribar ⁽¹⁾⁽⁴⁾	20/11/1951	64	2016	2020
Mr. Peter Erskine ⁽¹⁾⁽⁶⁾⁽⁷⁾	10/11/1951	64	2006	2020
Ms. Sabina Fluxà Thienemann ⁽⁷⁾	26/04/1980	36	2016	2020
Mr. Luiz Fernando Furlán	29/07/1946	70	2008	2018
Mr. Gonzalo Hinojosa Fernández de Angulo ⁽¹⁾⁽⁴⁾⁽⁵⁾⁽⁶⁾⁽⁷⁾⁽⁸⁾	10/07/1945	71	2002	2017
Mr. Pablo Isla Álvarez de Tejera ⁽⁷⁾	22/01/1964	52	2002	2017
Mr. Peter Löscher ⁽⁶⁾	17/09/1957	58	2016	2020
Mr. Antonio Massanell Lavilla ⁽²⁾⁽⁴⁾⁽⁵⁾⁽⁶⁾⁽⁸⁾	24/09/1954	61	1995	2020
Mr. Ignacio Moreno Martínez ⁽³⁾⁽⁴⁾⁽⁵⁾⁽⁸⁾	30/07/1957	59	2011	2017
Mr. Francisco Javier de Paz Mancho ⁽¹⁾⁽⁴⁾⁽⁵⁾⁽⁷⁾	24/07/1958	58	2007	2018
Mr. Wang Xiaochu ⁽⁹⁾	24/08/1958	58	2015	2020

Note

- (1) Member of the Executive Commission of the Board of Directors.
- (2) Nominated by Fundació Bancaria Caixa d'Estalvis i Pensions de Barcelona ("La Caixa").
- (3) Nominated by Banco Bilbao Vizcaya Argentaria, S.A.
- (4) Member of the Audit and Control Committee of the Board of Directors.
- (5) Member of the Regulation and Institutional Affairs Committee.
- (6) Member of the Strategy and Innovation Committee.
- (7) Member of the Nominating, Compensation and Corporate Governance Committee.
- (8) Member of the Service Quality and Customer Service Committee.
- (9) 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
José María Álvarez Pallete López José María Abril Pérez Isidro Fainé Casas	Executive Chairman of Telefónica, S.A. Vice Chairman of Telefónica, S.A. Vice Chairman of Telefónica, S.A.	Chairman of Fundación Bancaria Caixa d' Estalvis i Pensions de Barcelona ("la Caixa") Chairman of Criteria Caixa, S.A.U. Director of Gas Natural SDG, S.A. Chairman of the Spanish Confederation of Savings Banks (" <i>Confederación Española de Cajas de Ahorros</i> ", CECA) First Vice Chairman of Repsol, S.A. Director of Banco Portugués de Investimento, S.A. (BPI) Chairman of European Savings Bank Group (ESGB) Deputy Chairman of the World Savings Bank Institute (WSBI) Director of the Bank of East Asia (BEA) Director of Suez Environnement Company. Chairman of the Spanish Confederation of Directors and Executives (" <i>Confederación Española de Directivos y Ejecutivos</i> ", "CEDE") Chairman of the Spanish Chapter of the Club of Rome and the Circulo Financiero Member of the Business Council for Competitiveness (" <i>Consejo Empresarial de la Competitividad</i> ")
Julio Linares López	Vice Chairman of Telefónica, S.A. Trustee of Telefónica Foundation	Member of the GSM Association board and Executive Committee and Chairman of its Strategic Committee Member of the Executive Committee and the Board of the Spanish Confederation of Employers' Organisations (" <i>Confederación Española de Organizaciones Empresariales</i> ", "CEOE") Trustee of the Mobile World Capital Barcelona Foundation Trustee of CEDE Foundation Member of the Board of GSMA Ltd. Member of the Governing Council of the Association for the Advancement of Management Member of the Social Council of the Complutense University in Madrid Member of the Advisory Council of AMETIC Member of the Advisory Council of Official College of Telecommunications Engineering (COIT) Member of the Spanish Association of Telecommunications Engineers (AEIT) Member of the Advisory council of the Higher Technical School of Engineers Telecommunications
César Alierta Izuel	Director of Telefónica, S.A. Chairman of Telefónica Foundation Director of DTS, Distribuidora de Televisión Digital, S.A.U.	Director of China Unicom (Hong Kong) Limited Chairman of the Business Competitiveness Council (" <i>Consejo Empresarial de la Competitividad</i> ") Trustee of Bancaria Caixa d' Estalvis i Pensions de Barcelona Foundation ("la Caixa") Chairman of the Social Board of the UNED Member of the Columbia Business School Board of Overseers
María Eva Castillo Sanz	Director of Telefónica, S.A. Chairwoman of Supervisory Board of Telefónica Deutschland Holding, A.G.Trustee of Telefónica Foundation	Director of Bankia, S.A. Director of Visa Europe Member of the Board of the Comillas-ICAI Foundation
Juan Ignacio Cirac Sasturain	Director of Telefónica, S.A.	Member of the Board of Entreculturas Foundation Member of the Advisory Board of the Institute for the Interdisciplinary Information Sciences, Tsinghua University Member of the Advisory Board of the Russian Quantum Center Member of the Advisory Board of Annalen der Physik Member of the Review Panel, QSIT Swiss National Science Foundation Member of the Scientific Committee of BBVA

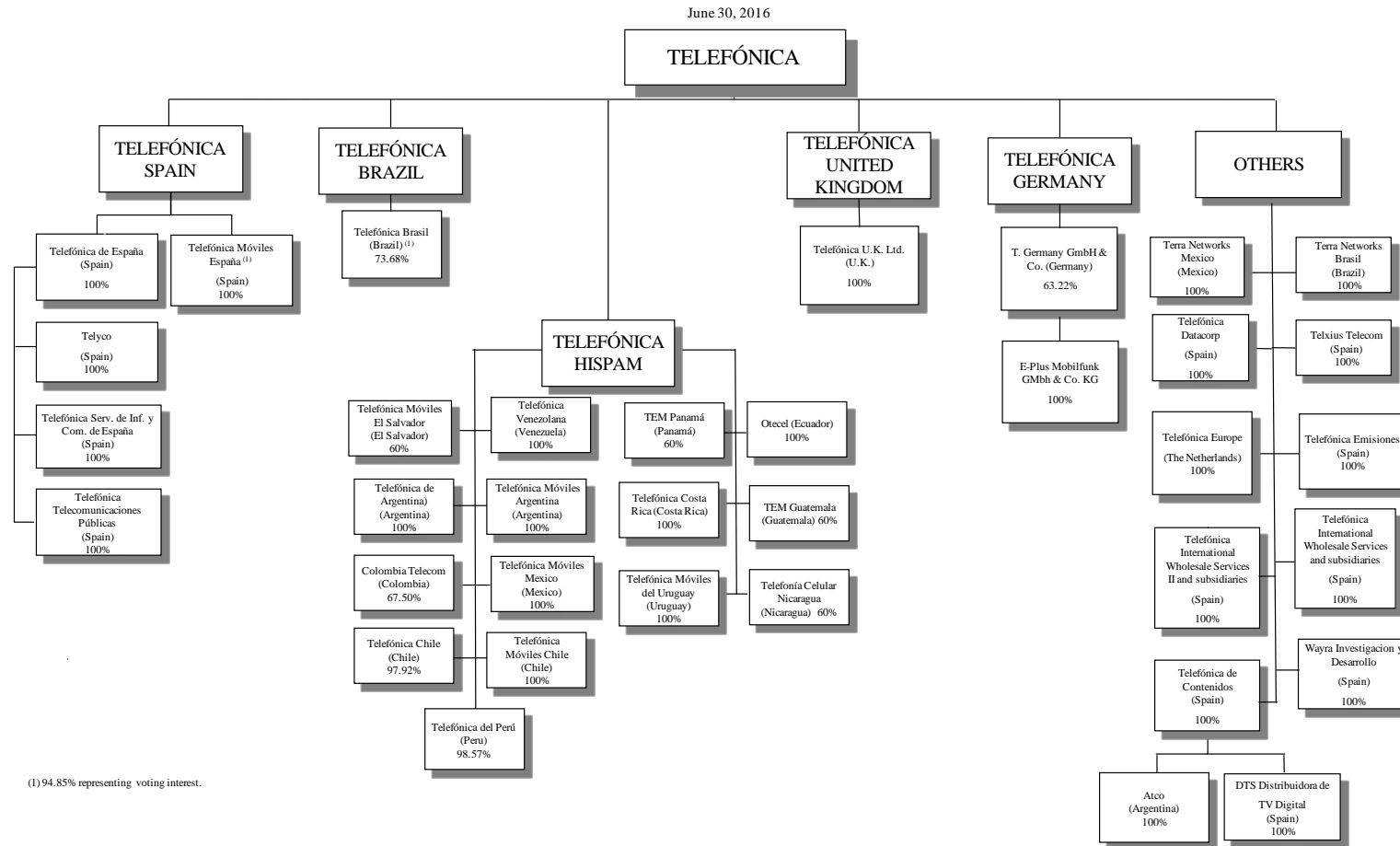
Name	Principal activities inside the Group	Principal Activities outside the Group
José Javier Echenique Landiribar	Director of Telefónica, S.A.	Foundation Vice-chairman of Banco de Sabadell, S.A. Director of Repsol, S.A. Director of ACS Actividades de Construcción y Servicios, S.A. Director of ACS Servicios, Comunicaciones y Energía, S.L. Director of Ence Energía y Celulosa, S.A. Trustee of Novia Salcedo Foundation Member of the Board of Deusto Business School Member of the Basque Businessmen Circle
Peter Erskine	Director of Telefónica, S.A. Member of the Supervisory Board of Telefonica Deutschland Holding AG	Chairman of the Henley Business School Strategy Board Member of the Council of Reading University Member of the University's Strategy and Finance Committee
Sabina Fluxà Thienemann	Director of Telefónica, S.A.	Co-Vice Executive President and CEO of Iberostar Group Member of the Regional Advisory Board of BBVA Member of the Board of Directors of APD Illes Balears Trustee of Iberostar Foundation Trustee of Eneavor Foundation Chairman of Amazonas Sustainability Foundation Director of Brasil Food, S.A. (BRF) Director of AGCO Corporation Member of the Global Ocean Commission
Luiz Fernando Furlán	Director of Telefónica, S.A. Director of Telefônica Brasil, S.A.	Chairman of Amazonas Sustainability Foundation Director of Brasil Food, S.A. (BRF) Director of AGCO Corporation 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 Álvarez de Tejera	Director of Telefónica, S.A.	Chairman and CEO of Inditex, S.A.
Peter Löscher	Director of Telefónica, S.A.	Chairman of the Supervisory Board of Sulzer AG Chairman of the Supervisory Board of OMV Member of the Supervisory Board of Deutsche Bank
Antonio Massanell Lavilla	Director of Telefónica, S.A.	Vice Chairman of CaixaBank, S.A. Director of Sociedad de Gestión de Activos Inmobiliarios procedentes de la Reestructuración Bancaria (SAREB). Non-Executive Chairman of Cecabank Member of the Supervisory Board of ERSTE Group Bank Director of Mediterranean Beach & Golf Community, S.A. Member of the Plenary of the Chamber of Commerce of Barcelona Vice-Chairman of the Board of Trustees of COTEC Foundation Member of the Euro Retail Payments Board (ERPB) Chairman of the Barcelona Centre Financer European association
Ignacio Moreno Martínez	Director of Telefónica, S.A.	Chief Executive Officer of Metrovacesa, S.A. Representative of Cardomana Servicios y Gestiones, S.L. on the Board of Directors of Secuoya Grupo de Comunicación, S.A.
Francisco Javier de Paz Mancho	Director of Telefónica de Argentina, S.A. Director of Telefônica Brasil, S.A.	
Wang Xiaochu	Director of Telefónica, S.A.	Chairman of China United Network Communications Group Company Limited Chairman, Executive Director and CEO of China Unicom (Hong Kong) Limited

Conflicts of Interest

As at the date of this Prospectus, there are 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 June 2016, including their jurisdictions of incorporation and Telefónica's ownership interest:



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 of 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; and
- (ii) a holder of Securities is not a pension fund or otherwise not a taxpayer or exempt for tax purposes.

Generally speaking, an individual has a substantial interest in a company if (a) such individual, either alone or together with his partner, directly or indirectly has, or is deemed to have or (b) certain relatives of such individual or his partner directly or indirectly have or are deemed to have (i) the ownership of, a right to acquire the ownership of, or certain rights over, shares representing 5 per cent or more of either the total issued and outstanding capital of such company or the issued and outstanding capital of any class of shares of such company, or (ii) the ownership of, or certain rights over, profit participating certificates (*winstbewijzen*) that relate to 5 per cent or more of either the annual profit or the liquidation proceeds of such company

Generally speaking, a non-resident entity has a substantial interest in a company if such entity, directly or indirectly has (i) the ownership of, a right to acquire the ownership of, or certain rights over, shares representing 5 per cent or more of either the total issued and outstanding capital of such company or the issued and outstanding capital of any class of shares of such company, or (ii) the ownership of, or certain rights over, profit participating certificates (*winstbewijzen*) that relate to 5 per cent or more of either the annual profit or the liquidation proceeds of such company. An entity has a deemed substantial interest in a company if such entity has disposed of or is deemed to have disposed of all or part of a substantial interest on a non-recognition basis.

For the purpose of this summary, the term "entity" means a corporation as well as any other person that is taxable as a corporation for Dutch corporate tax purposes.

Where this summary refers to a holder of Securities, an individual holding Securities or an entity holding Securities, such reference is restricted to an individual or entity holding legal title to as well as an economic interest in the Securities or otherwise being regarded as owning Securities for Dutch tax purposes. It is noted that for purposes of Dutch income, corporate, gift and inheritance tax, assets legally owned by a third party such as a trustee, foundation or similar entity, may be treated as assets owned by the (deemed) settlor, grantor or similar originator or the beneficiaries in proportion to their interest in such arrangement.

Where the summary refers to "The Netherlands" or "Dutch" it refers only to the European part of the Kingdom of The Netherlands.

Investors should consult their professional advisers on the tax consequences of their acquiring, holding and disposing of Securities.

1. WITHHOLDING TAX

All payments made by the Issuer of interest and principal under the Securities can be made free of withholding or deduction of any taxes of whatever nature imposed, levied, withheld or assessed by The Netherlands or any political subdivision or taxing authority thereof or therein.

2. TAXES ON INCOME AND CAPITAL GAINS

Residents

Resident entities

An entity holding Securities which is, or is deemed to be, resident in The Netherlands for corporate tax purposes and which is not tax exempt, will generally be subject to corporate tax in respect of income and capital gains derived from the Securities at a rate of 20% with respect to taxable profits up to €200,000 and 25% with respect to taxable profits in excess of that amount.

Resident individuals

An individual holding Securities who is, or is deemed to be, 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 securities are attributable to an enterprise from which the holder of the securities derives a share in the profits, whether as an entrepreneur (*ondernemer*) or as a person who has a co-entitlement to the net worth (*mede-gerechtigde tot het vermogen*) of such enterprise, (other than as a shareholder); or
- (ii) the benefits derived from the securities qualify as income from miscellaneous activities (*belastbaar resultaat uit overige werkzaamheden*) as defined in the Income Tax Act (*Wet inkomstenbelasting 2001*), or the holder of the securities is considered to perform 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). As of 1 January 2017, the rate of 4 per cent. will be replaced by variable progressive rates. For 2017 these rates have been set from 2.9 to 5.5 per cent. The applicable rates will be updated annually on the basis of historic market yields. 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, and is not deemed to be, 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 securities are attributable to an enterprise or deemed 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*) taxable in The Netherlands; or
- (ii) the holder is an individual and the income and capital gains derived from the securities qualify 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 the First Additional Provision 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 the First Additional Provision 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, 19 per cent.) 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 the First Additional Provision 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 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, 19 per cent.) 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 the First Additional Provision 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.

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**"). However, Estonia has since stated that it will not participate.

The Commission's Proposal has very broad scope and could, if introduced, apply to certain dealings in 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 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.

However, the FTT proposal remains subject to negotiation between participating Member States and it may therefore be altered prior to any implementation, the timing of which remains unclear. Additional EU Member States may decide to participate.

Prospective holders of Securities are strongly advised to seek their own professional advice in relation to the FTT.

SUBSCRIPTION AND SALE

BNP Paribas, Citigroup Global Markets Limited, Commerzbank Aktiengesellschaft, Merrill Lynch International, Société Générale, The Royal Bank of Scotland plc and UniCredit Bank AG (the "**Joint Bookrunners**") have, in a subscription agreement dated 9 September 2016 (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, US 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 US 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 US 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, US 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, US 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 35 of the Spanish Securities Market Law approved by legislative Royal Decree 4/2015, of 23 October (*Real Decreto Legislativo 4/2015, de 23 de octubre, por*

el que se aprueba el texto refundido de la Ley 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 1 September 2016. 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 29 July 2015, 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 18 of this Prospectus, and under "Description of the Guarantor - Legal Proceedings" and "Description of the Guarantor – Tax Proceedings" on pages 81-87 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 2015 there has been no material adverse change in the prospects of the Issuer, and there has been no significant change in the financial or trading position of the Issuer. Since 31 December 2015 there has been no material adverse change in the prospects of the Guarantor and the Group, and since 30 June 2016 there has been no significant change in the financial or trading position of the Guarantor and the Group, save for: (i) on 7 July 2016, the Guarantor drew down €500 million under its €3,000 million syndicated credit facility signed on 17 November 2015 and maturing in 2018; and (ii) on 8 September 2016, the Guarantor redeemed €500 million of its €3,000 million syndicated credit facility signed on 17 November 2015 and maturing in 2018.

Auditors

4. The consolidated financial statements of the Guarantor have been audited without qualification for the years ended 31 December 2015 and 2014 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 2015 and 2014 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 by-laws 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 2015 and 2014; and

- (e) the audited consolidated financial statements of the Guarantor for the years ended 31 December 2015 and 2014 and the unaudited interim consolidated financial information of the Guarantor for the 6 months ended 30 June 2016 (set out in the document entitled "*Results January – June 2016*").

Each of the translations into English of the Issuer's articles of association and of the by-laws 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 3.753% 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 14 September 2016, 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 XS1490960942 and the common code is 149096094.

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