

TELEFONICA S A  
Form 20-F  
April 30, 2009

As filed with the Securities and Exchange Commission on April 30, 2009

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UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549

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FORM 20-F

(Mark One)

- REGISTRATION STATEMENT PURSUANT TO SECTION 12(b)  
OR (g) OF THE SECURITIES EXCHANGE ACT OF 1934  
OR
- ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d)  
OF THE SECURITIES EXCHANGE ACT OF 1934  
for the fiscal year ended December 31, 2008  
OR
- TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d)  
OF THE SECURITIES EXCHANGE ACT OF 1934  
OR
- SHELL COMPANY REPORT PURSUANT TO SECTION 13 OR 15(d)  
OF THE SECURITIES EXCHANGE ACT OF 1934  
for the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission file number: 001-09531

TELEFÓNICA, S.A.  
(Exact name of Registrant as specified in its charter)

KINGDOM OF SPAIN  
(Jurisdiction of incorporation or organization)

Distrito C, Ronda de la Comunicación, s/n  
28050 Madrid, Spain  
(Address of principal executive offices)

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(Name, Telephone, E-Mail and/or Facsimile number and Address of Company Contact Person)

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Securities registered or to be registered pursuant to Section 12(b) of the Act:

| Title of each class   | Name of each exchange on which registered |
|---|---|
| Ordinary Shares, nominal value €1.00 per share*   | New York Stock Exchange                   |
| American Depositary Shares, each representing three Ordinary Shares   | New York Stock Exchange                   |
| Guarantees** by Telefónica, S.A. of the \$1,000,000,000 Floating Rate Guaranteed Senior Notes Due 2009; \$1,000,000,000 Fixed Rate Guaranteed Senior Notes Due 2011; \$1,250,000,000 Fixed Rate Guaranteed Senior Notes Due 2016; \$2,000,000,000 Fixed Rate Guaranteed Senior Notes Due 2036; \$850,000,000 Floating Rate Guaranteed Senior Notes Due 2013; \$750,000,000 Fixed Rate Guaranteed Senior Notes Due 2013; and \$700,000,000 Fixed Rate Guaranteed Senior Notes Due 2017, each of Telefónica Emisiones, S.A.U. | New York Stock Exchange                   |

\*Not for trading, but only in connection with the listing of American Depositary Shares, pursuant to the requirements of the New York Stock Exchange.

\*\*Not for trading, but only in connection with the listing of the \$1,000,000,000 Floating Rate Guaranteed Senior Notes Due 2009; \$1,000,000,000 Fixed Rate Guaranteed Senior Notes Due 2011; \$1,250,000,000 Fixed Rate Guaranteed Senior Notes Due 2016; \$2,000,000,000 Fixed Rate Guaranteed Senior Notes Due 2036; \$850,000,000 Floating Rate Guaranteed Senior Notes Due 2013; \$750,000,000 Fixed Rate Guaranteed Senior Notes Due 2013; and \$700,000,000 Fixed Rate Guaranteed Senior notes Due 2017 each of Telefónica Emisiones, S.A.U. (a wholly-owned subsidiary of Telefónica, S.A.).

Securities registered or to be registered pursuant to Section 12(g) of the Act: None

Securities for which there is a reporting obligation pursuant to Section 15(d) of the Act: None

The number of outstanding shares of each class of capital stock of Telefónica, S.A. at December 31, 2008 was:

Ordinary Shares, nominal value €1.00 per share: 4,704,996,485

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

Yes  No

If this report is an annual or transition report, indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 15 (d) of the Securities Exchange Act of 1934.

Yes  No

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports) and (2) has been subject to such filing requirements for the past 90 days.

Yes  No

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Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of “accelerated filer” and “large accelerated filer” in Rule 12b-2 of the Exchange Act.

Large accelerated filer  Accelerated filer  Non-accelerated filer

Indicate by check mark which basis of accounting the registrant has used to prepare the financial statements included in this filing:

U.S. GAAP  International Financial Reporting Standards as Issued by the international Accounting Standards Board  Other

If “Other” has been checked in response to the previous question, indicate by check mark which financial statement item the registrant has elected to follow.

Item 17  Item 18

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes  No

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CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING STATEMENTS

This Annual Report contains statements that constitute forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, Section 21E of the Securities Exchange Act of 1934, as amended, and the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. The forward-looking statements in this Annual Report can be identified, in some instances, by the use of words such as “expect”, “aim”, “hope”, “anticipate”, “intend”, “believe” and similar language or the negative thereof or by the forward-looking nature of discussions of strategy, plans or intentions. These statements appear in a number of places in this Annual Report including, without limitation, certain statements made in “Item 3. Key Information—Risk Factors”, “Item 4. Information on the Company”, “Item 5. Operating and Financial Review and Prospects” and “Item 11. Quantitative and Qualitative Disclosures About Market Risk” and include statements regarding our intent, belief or current expectations with respect to, among other things:

- the effect on our results of operations of competition in the Spanish telecommunications market and our other principal markets;
  - trends affecting our financial condition or results of operations;
  - acquisitions or investments which we may make in the future;
    - our capital expenditures plan;
    - our estimated availability of funds;
  - our ability to repay debt with estimated future cash flows;
  - our shareholder remuneration policies;
- supervision and regulation of the Spanish telecommunications sector and of the telecommunications sectors in other countries where we have significant operations;
  - our strategic partnerships; and
- the potential for growth and competition in current and anticipated areas of our business.

Such forward-looking statements are not guarantees of future performance and involve numerous risks and uncertainties, and actual results may differ materially from those anticipated in the forward-looking statements as a result of various factors. The risks and uncertainties involved in our business that could affect the matters referred to in such forward-looking statements include but are not limited to:

- changes in general economic, business or political conditions in the domestic or international markets (particularly in Latin America) in which we operate or have material investments that may affect demand for our services;
- changes in currency exchange rates, interest rates or in credit risk in our treasury investments or in some of our financial transactions;
  - general economic conditions in the countries in which we operate;
  - existing or worsening conditions in the international financial markets;

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- failure to maintain satisfactory working relationships with our joint venture partners;
  - the actions of existing and potential competitors in each of our markets;
- the impact of current, pending or future legislation and regulation in countries where we operate;



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- failure to renew or obtain the necessary licenses, authorizations and concessions to carry out our operations;
  - the potential effects of technological changes;
  - unanticipated service network interruptions;
  - the impact of limitations in spectrum capacity;
- failure of suppliers to provide necessary equipment and services on a timely basis;
  - the impact of unanticipated network interruptions;
- the effect of reports suggesting that radio frequency emissions cause health problems;
- the impact of impairment charges on our goodwill and assets as a result of changes in the regulatory, business or political environment; and
  - the outcome of pending litigation.

Readers are cautioned not to place undue reliance on those forward-looking statements, which speak only as of the date of this Annual Report. We undertake no obligation to release publicly the result of any revisions to these forward-looking statements which may be made to reflect events or circumstances after the date of this Annual Report including, without limitation, changes in our business or acquisition strategy or planned capital expenditures, or to reflect the occurrence of unanticipated events.

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CERTAIN TERMS AND CONVENTIONS

Our ordinary shares, nominal value €1.00 per share, are currently listed on each of the Madrid, Barcelona, Bilbao and Valencia stock exchanges and are quoted through the Automated Quotation System under the symbol “TEF”. They are also listed on various foreign stock exchanges such as the London, Buenos Aires and Tokyo stock exchanges. Our American Depositary Shares (“ADSs”) are listed on the New York Stock Exchange and on the Lima Stock Exchange. ADSs, each representing the right to receive three ordinary shares, are issued under a Deposit Agreement with Citibank, N.A., as depositary in the form of certificated ADSs (American Depositary Receipts, or ADRs) or uncertificated ADSs. Brazilian Depositary Shares (“BDSs”), each representing the right to receive one ordinary share, are listed on the São Paulo Stock Exchange. BDSs are evidenced by Brazilian Depositary Receipts (“BDRs”) issued under a Deposit Agreement with Banco Bradesco, S.A., as depositary.

We delisted our shares from the Paris and Frankfurt stock exchanges in the first quarter of 2008.

As used herein, “Telefónica”, “Telefónica Group”, “Group” and terms such as “we”, “us” and “our” mean Telefónica, S.A. and its consolidated subsidiaries, unless the context requires otherwise.

As used herein, “Atento” means Atento Holding, Inversiones y Teleservicios, S.A. and its consolidated subsidiaries, unless the context requires otherwise.

As used herein, “O2 Group” means Telefónica O2 Europe Plc and its consolidated subsidiaries, “Telefónica O2 UK” means O2 (UK) Ltd. and its consolidated subsidiaries and “Telefónica O2 Germany” means O2 (Germany) GmbH & Co OHG and its consolidated subsidiaries, unless the context requires otherwise.

Below are definitions of certain technical terms used in this Annual Report:

- “Access” refers to a connection to any of the telecommunications services offered by the Telefónica Group. We present our customer base using this model because the integration of telecommunications services in bundled service packages has changed the way residential and corporate customers contract or purchase our services. Because a single customer may contract for multiple services, we believe it is more accurate to count the number of accesses, or services a customer has contracted for, as opposed to only counting the number of our customers. For example, a customer that has fixed line telephony service and broadband service represents two accesses rather than a single customer. In addition, we fully count the accesses of all companies over which we exercise control or joint control. The following are the main categories of accesses:
  - o Fixed telephony accesses: includes public switched telephone network, or PSTN, lines (including public use telephony), and integrated services digital network, or ISDN, lines and circuits. For purposes of calculating our number of fixed line accesses, we multiply our lines in service as follows: PSTN (x1); basic ISDN (x1); primary ISDN (x30, x20 or x10); 2/6 digital accesses (x30).
  - o Internet and data accesses: includes broadband accesses (retail asymmetrical digital subscriber line, or ADSL, satellite, fiber optic and circuits over 2 Mbps), narrowband accesses (Internet service through the PSTN lines) and other accesses, including the remaining non-broadband final client circuits.
  - o Pay TV: includes cable TV, direct to home satellite TV, or DTH, and Internet Protocol TV, or IPTV.
    - o Mobile accesses: includes contract and pre-pay mobile telephony.

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 UL) or only DSL service (shared unbundled loop, or shared UL).

o Wholesale ADSL: means wholesale asymmetrical digital subscriber line.

o Other: includes other circuits for other operators.

Certain technical terms used with respect to our business are as follows:

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- “ARPU” is the average revenue per user per month. ARPU is calculated by dividing total service revenue (excluding inbound roaming revenue) from sales to customers for the preceding 12 months by the weighted average number of customers for the same period, and then divided by 12 months. ARPU is calculated using gross service revenue before deduction of wholesale discounts.
  - “CDMA” means Code Division Multiple Access, which is a type of radio communication technology.
- “Commercial activity” includes the addition of new lines, replacement of handsets and changes in types of contracts.
  - “Customer revenue” means service revenue less interconnection revenue.
- “Duo bundle” means broadband plus voice service. We measure “Duo bundles” in terms of units, where each bundle of broadband and voice service counts as one unit.
  - “Final clients accesses” means accesses provided to residential and corporate clients.
  - “Gross adds” means the gross increase in the number of accesses in a period.
- “HSDPA” means High Speed Downlink Packet Accesses, which is a 3G mobile telephony communications protocol in the High-Speed Packet Access (HSPA) family, which allows networks based on UMTS to have higher data transfer speeds and capacity.
- “Interconnection revenue” means revenues received from other operators which use our networks to connect to our customers.
  - “ISP” means Internet service provider.
  - “LMDS” means local multipoint distribution service.
- “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.
- “MOU”, or minutes of use per month, is calculated by dividing the total number of voice minutes for the preceding 12 months by the weighted average number of mobile accesses for the same period, and then divided by 12 months.
- “MVNO” means mobile virtual network operator, which is a mobile operator that is not entitled to use spectrum for the provision of mobile services. Consequently, an MVNO must subscribe to an access agreement with a mobile network operator in order to provide mobile access to their customers. An MVNO pays such mobile network operator for using the infrastructure to facilitate coverage to their customers. There are two types of MVNOs: (i) “pure MVNOs”, which are typically telecommunications companies without licensed frequency allocation and want to complete their telecommunications service portfolio (for example, ONO in Spain); and (ii) “reseller MVNOs”, which are companies that purchase wholesale mobile minutes and resell to end-users, and use their brand and distribution channel (for example, Carrefour in Spain).
- “Net adds” means the difference between the number of accesses at the end of the period and the beginning of a period.
  - “Revenues” means net sales and rendering of services.

- “Service revenues” means revenues less revenues from handset sales.
- “Trio bundle” means broadband plus voice service plus IPTV. We measure “Trio bundles” in terms of units, where each bundle of broadband, voice service and IPTV counts as one unit.
  - “UMTS” means Universal Mobile Telecommunications System.

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- “VoIP” means voice over Internet protocol.
- “Wholesale accesses” means accesses we provide to our competitors, who then sell such accesses to their residential and corporate clients.

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PRESENTATION OF CERTAIN FINANCIAL INFORMATION

In this Annual Report, references to “U.S. dollars”, “dollars” or “\$”, are to United States dollars, references to “pounds sterling”, “sterling” or “£” are to British pounds sterling, references to “reais” refer to Brazilian reais and references to “euro” or “€” are to the single currency of the participating member states in the Third Stage of the European Economic and Monetary Union pursuant to the treaty establishing the European Community, as amended from time to time.

Our consolidated financial statements as of December 31, 2007 and 2008, and for the years ended December 31, 2006, 2007 and 2008 included elsewhere in this Annual Report including the notes thereto (the “Consolidated Financial Statements”), are prepared in conformity with International Financial Reporting Standards (“IFRS”) as issued by the International Accounting Standards Board (“IASB”), which do not differ from IFRS as adopted by the European Union.

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PART I

Item 1. Identity of Directors, Senior Management and Advisors

A. Directors and Senior Management

Not applicable.

B. Advisers

Not applicable.

C. Auditors

Not applicable.

Item 2. Offer Statistics and Expected Timetable

Not applicable.

Item 3. Key Information

A. Selected Financial Data

The following table presents our selected consolidated financial data. It is to be read in conjunction with “Item 5. Operating and Financial Review and Prospects” and the Consolidated Financial Statements. The consolidated income statement and cash flow data for the years ended December 31, 2006, 2007 and 2008 and the consolidated balance sheet data as of December 31, 2007 and 2008 set forth below are derived from, and are qualified in their entirety by reference to, the Consolidated Financial Statements. The consolidated income statement and cash flow data for the years ended December 31, 2004 and 2005 and the consolidated balance sheet data as of December 31, 2004, 2005 and 2006 set forth below are derived from Telefónica, S.A.’s consolidated financial statements for such years, which are not included herein.

Our Consolidated Financial Statements have been prepared in accordance with IFRS as issued by the IASB.

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The basis of presentation and principles of consolidation are described in detail in Notes 2 and 3.q., respectively, to our Consolidated Financial Statements.

|   | As of or for the year ended December 31,  |           |           |           |           |
|---|---|-----------|-----------|-----------|-----------|
|   | 2004(1)                                   | 2005(1)   | 2006(1)   | 2007      | 2008      |
|   | (in millions of euros, except share data) |           |           |           |           |
| Revenues  | 29,809                                    | 37,383    | 52,901    | 56,441    | 57,946    |
| Other income  | 1,134                                     | 1,416     | 1,571     | 4,264     | 1,865     |
| Supplies  | (7,577)                                   | (9,999)   | (16,629)  | (17,907)  | (17,818)  |
| Personnel expenses  | (4,976)                                   | (5,532)   | (7,622)   | (7,893)   | (6,762)   |
| Other expenses  | (6,373)                                   | (8,212)   | (11,095)  | (12,081)  | (12,312)  |
| Depreciation and amortization   | (5,642)                                   | (6,693)   | (9,704)   | (9,436)   | (9,046)   |
| Operating income  | 6,375                                     | 8,363     | 9,422     | 13,388    | 13,873    |
| Share of profit (loss) of associates  | (50)                                      | (128)     | 76        | 140       | (161)     |
| Net financial expenses  | (1,456)                                   | (1,790)   | (2,795)   | (2,851)   | (2,821)   |
| Net exchange differences  | (177)                                     | 162       | 61        | 7         | 24        |
| Net financial income (expense)  | (1,633)                                   | (1,628)   | (2,734)   | (2,844)   | (2,797)   |
| Profit before taxes from continuing operations  | 4,692                                     | 6,607     | 6,764     | 10,684    | 10,915    |
| Corporate income tax  | (1,451)                                   | (1,904)   | (1,781)   | (1,565)   | (3,089)   |
| Profit for the year from continuing operations  | 3,241                                     | 4,703     | 4,983     | 9,119     | 7,826     |
| Profit from discontinued operations after taxes   | 245                                       | 124       | 1,596     | —         | —         |
| Profit for the year   | 3,486                                     | 4,827     | 6,579     | 9,119     | 7,826     |
| Minority interests  | (310)                                     | (381)     | (346)     | (213)     | (234)     |
| Profit for the year attributable to equity holders of the parent  | 3,176                                     | 4,446     | 6,233     | 8,906     | 7,592     |
| Weighted average number of shares (thousands)   | 4,987,751                                 | 4,870,852 | 4,778,999 | 4,758,707 | 4,645,852 |
| Basic and diluted earnings per share from continuing operations attributable to equity holders (euros)(2) | 0.60                                      | 0.90      | 0.97      | 1.87      | 1.63      |
| Basic and diluted earnings per share attributable to equity holders of the parent (euros)(2)              | 0.64                                      | 0.91      | 1.30      | 1.87      | 1.63      |
| Earnings per ADS (euros)(2)(3)  | 1.91                                      | 2.74      | 3.91      | 5.62      | 4.90      |
| Weighted average number of ADS (thousands)  | 1,662,584                                 | 1,623,617 | 1,592,999 | 1,586,236 | 1,548,617 |
| Cash dividends per ordinary share (euros)   | 0.40                                      | 0.50      | 0.55      | 0.65      | 0.90      |
| Consolidated Balance Sheet Data   |   |           |           |           |           |
| Cash and cash equivalents   | 914                                       | 2,213     | 3,792     | 5,065     | 4,277     |
| Property, plant and equipment   | 23,193                                    | 27,993    | 33,887    | 32,460    | 30,545    |
| Total assets  | 60,079                                    | 73,174    | 108,982   | 105,873   | 99,896    |
| Non-current liabilities   | 27,743                                    | 35,126    | 62,645    | 58,044    | 55,202    |
| Equity (net)  | 12,342                                    | 16,158    | 20,001    | 22,855    | 19,562    |
| Consolidated Cash Flow Data   |   |           |           |           |           |
| Net cash from operating activities  | 10,131                                    | 11,139    | 15,414    | 15,551    | 16,366    |
| Net cash used in investing activities   | (5,808)                                   | (9,592)   | (28,052)  | (4,592)   | (9,101)   |
| Net cash (used in) from financing activities  | (3,937)                                   | (435)     | 14,572    | (9,425)   | (7,765)   |

(1) Telefónica Publicidad e Información, S.A. (TPI) was sold in 2006 and its results of operations for 2006 and the gain we recorded on its sale are included under “Profit from discontinued operations after taxes” for 2006. Figures for 2005 and 2004 have been restated to present TPI’s results under the same caption.

- (2) The per share and per ADS computations for all periods presented have been presented using the weighted average number of shares and ADSs, respectively, outstanding for each period, and have been adjusted to reflect the stock dividends which occurred during the periods presented, as if these had occurred at the beginning of the earliest period presented.
- (3) Each ADS represents the right to receive three ordinary shares. Figures do not include any charges of the depositary.

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## Exchange Rate Information

As used in this Annual Report, the term “Noon Buying Rate” refers to the rate of exchange for euros, expressed in U.S. dollars per euro, in the City of New York for cable transfers payable in foreign currencies as certified by the Federal Reserve Bank of New York for customs purposes. The Noon Buying Rate certified by the New York Federal Reserve Bank for the euro on April 24, 2009 was \$1.2978 = €1.00. The following tables describe, for the periods and dates indicated, information concerning the Noon Buying Rate for the euro. Amounts are expressed in U.S. dollars per €1.00.

| Year ended December 31, | Noon Buying Rate |            |        |        |
|-------------------------|------------------|------------|--------|--------|
|                         | Period end       | Average(1) | High   | Low    |
| 2004                    | 1.3538           | 1.2478     | 1.3625 | 1.1801 |
| 2005                    | 1.1842           | 1.2400     | 1.3476 | 1.1667 |
| 2006                    | 1.3197           | 1.2661     | 1.3327 | 1.1860 |
| 2007                    | 1.4603           | 1.3797     | 1.4862 | 1.2904 |
| 2008                    | 1.3919           | 1.4698     | 1.6010 | 1.2446 |

Source: Federal Reserve Bank of New York.

(1) The average of the Noon Buying Rates for the euro on the last day reported of each month during the relevant period.

| Month ended       | Noon Buying Rate |        |
|-------------------|------------------|--------|
|                   | High             | Low    |
| October 31, 2008  | 1.4058           | 1.2446 |
| November 30, 2008 | 1.3039           | 1.2525 |
| December 31, 2008 | 1.4358           | 1.2634 |
| January 31, 2009  | 1.3946           | 1.2804 |
| February 29, 2009 | 1.3064           | 1.2547 |
| March 31, 2009    | 1.3730           | 1.2549 |
| April 24, 2009    | 1.3458           | 1.2978 |

Source: Federal Reserve Bank of New York.

Monetary policy within the member states of the euro zone is set by the European Central Bank. The European Central Bank has set the objective of containing inflation and will adjust interest rates in line with this policy without taking account of other economic variables such as the rate of unemployment. It has further declared that it will not set an exchange rate target for the euro.

Our ordinary shares are quoted on the Spanish stock exchanges in euro. Currency fluctuations may affect the dollar equivalent of the euro price of our shares listed on the Spanish stock exchanges and, as a result, the market price of our ADSs, which are listed on the New York Stock Exchange. Currency fluctuations may also affect the dollar amounts received by holders of ADSs on conversion by the depositary of any cash dividends paid in euro on the underlying shares.

Our consolidated results are affected by fluctuations between the euro and the currencies in which the revenues and expenses of some of our consolidated subsidiaries are denominated (principally the Brazilian real, pounds sterling, the Venezuelan bolivar, the Czech koruna (crown), the Argentine peso, the Chilean peso, the Peruvian nuevo sol, the

Colombian peso and the Mexican peso).

B. Capitalization and Indebtedness

Not applicable.

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C. Reasons for the Offer and Use of Proceeds

Not applicable.

D. Risk Factors

In addition to the other information contained in this Annual Report, prospective investors should carefully consider the risks described below before making any investment decision. The risks described below are not the only ones that we face. Additional risks not currently known to us or that we currently deem immaterial may also impair our business and results of operations. Our business, financial condition, results of operations and cash flow could be materially adversely affected by any of these risks, and investors could lose all or part of their investment.

Risks Relating to Our Business

A material portion of our operations and investments are located in Latin America, and we are therefore exposed to risks inherent in operating and investing in Latin America.

At December 31, 2008, approximately 36.3% of our assets were located in Latin America. In addition, approximately 38.7% of our revenues for 2008 were derived from our Latin American operations. Our operations and investments in Latin America (including the revenues generated by these operations, their market value and the dividends and management fees expected to be received therefrom) are subject to various risks linked to the economic, political and social conditions of these countries, including risks related to the following:

- government regulation or administrative policies may change unexpectedly and negatively affect our interests in such countries;
- currencies may be devalued or may depreciate or currency restrictions and other restraints on transfer of funds may be imposed;
- the effects of inflation or currency depreciation may result in certain of our subsidiaries having negative equity, which would require them to undertake a mandatory recapitalization or commence dissolution proceedings;
- governments may expropriate or nationalize assets or increase their participation in the economy and companies;
  - governments may impose burdensome taxes or tariffs;
- political changes may lead to changes in the economic conditions and business environment in which we operate; and
  - economic downturns, political instability and civil disturbances may negatively affect our operations.

Finally, our operations are dependent, in many cases, on concessions and other agreements with existing governments in the countries in which we operate. These concessions and agreements, including their renewal, could be directly affected by economic and political instability, altering the terms and conditions under which we operate.

Our financial condition and results of operations may be adversely affected if we do not effectively manage our exposure to foreign currency exchange rate, interest rate or financial investment risks.

We are exposed to various types of market risk in the normal course of our business, including the impact of changes in foreign currency exchange rates and the impact of changes in interest rates, as well as the impact of changes of credit risk in our treasury investments or in some of our financial transactions. We employ risk management strategies to manage this exposure, in part through the use of financial derivatives such as foreign currency forwards, currency swap agreements and interest rate swap agreements. If the financial derivatives market is not sufficiently liquid for our risk management purposes, or if we cannot enter into arrangements of the type and

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for the amounts necessary to limit our exposure to currency exchange rate fluctuations or if our counterparties fail to deliver on their commitments due to lack of solvency or otherwise, such failure could adversely affect our financial condition, results of operations and cash flow. Also, our other risk management strategies may not be successful, which could adversely affect our financial condition, results of operations and cash flow. Moreover, if the rating of our counterparties in treasury investments or in our financial transactions deteriorates significantly or if any of such counterparties were to fail in its obligations to us, we may suffer a loss of value in our investments, incur unexpected losses and assume additional financial obligations under these transactions, and such failure could adversely affect our business, financial condition, results of operations and cash flow.

For a more detailed description of our financial derivatives transactions, see “Item 11. Quantitative and Qualitative Disclosures about Market Risk” and Note 16 to our Consolidated Financial Statements.

Adverse economic conditions could reduce the purchase of our products and services.

Our business is impacted by general economic conditions and other similar factors in each of the countries in which we operate. The current adverse economic environment and uncertainty about present global economic conditions may negatively affect the level of demand of existing and prospective customers, as our services may not be deemed critical for these customers. Other factors that could influence customer demand include access to credit, consumer confidence and other general macroeconomic factors.

In addition, there could be other possible follow-on effects from the financial crisis on our business, including insolvency of key suppliers or customers. A loss of customers or a reduction in purchases by our current customers could have a material adverse effect on our business, financial condition, results of operations and cash flow and may negatively affect our ability to meet our growth targets.

Existing or worsening conditions in the international financial markets may limit our ability to carry out our business plan.

The development and distribution of our services as well as the operation, expansion and upgrading of our networks and the fulfillment of our dividend payout commitment to our shareholders, require substantial financing. Moreover, our liquidity and capital resource requirements may increase if we participate in other fixed line or mobile license award processes or make acquisitions. We also have major capital resource requirements relating to, among other things, the development of distribution channels in new countries of operations and the development and implementation of new technologies.

If our ability to generate cash flow were to decrease, whether due to the current financial and economic crisis or otherwise, we may need to incur additional debt or raise other forms of capital to support our liquidity and capital resource requirements for the ongoing development and expansion of our business.

The current financial crisis affecting the international banking system and financial markets generally has resulted in a significant tightening of credit markets, a low level of liquidity in many financial markets and high volatility in credit, equity and currency markets. Existing or worsening conditions in the international credit markets may make it more difficult and more expensive to refinance our financial debt (of which €7,014 million matures in 2009) or to incur additional debt. For example, in February 2009 we issued €2 billion in principal amount of five-year bonds with a spread of 250 basis points over swaps, approximately 150 basis points higher than what we paid on bonds issued with the same tenor in May 2008, although in a lower principal amount (€1.25 billion). In addition, our capacity to raise capital in the international capital markets would be impaired if our credit ratings were downgraded, whether due to decreases in our cash flow or otherwise. Further, current market conditions may make it more difficult to renew our unused bilateral credit facilities scheduled to expire prior to December 31, 2009 (for an aggregate amount of €2,720

million).

The current financial and economic crisis may also make it more difficult and costly for us to launch a rights issue to our current shareholders or to raise additional equity capital if further funds were needed for pursuing our business plans.

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The successful implementation of our strategy for our mobile operations in Brazil depends on the development of our joint venture company with Portugal Telecom, SGPS, S.A.

Our mobile business in Brazil is conducted through a 50/50 joint venture company, Brasilcel, N.V., or Brasilcel, which is jointly controlled by us and Portugal Telecom SGPS, S.A., or Portugal Telecom. As a result of our less than controlling interest in this joint venture, we do not have absolute control over the operations of the venture. As a result, there is an inherent risk for management or operational disruptions whenever a disagreement between us and our partner arises. Therefore, we must cooperate with Portugal Telecom in order to implement and expand upon our business strategies and to finance and manage the operations of the joint venture. If we do not manage to obtain the cooperation of Portugal Telecom or if a disagreement or deadlock arises we may not achieve the expected benefits from this joint venture, including economies of scale and opportunities to achieve potential synergies and cost savings.

## Risks Relating to Our Industry

We face intense competition in most of our markets, which could result in decreases in current and potential customers, revenues and profitability.

We face significant competition in all of the markets in which we operate, and we are therefore subject to the effects of actions by our competitors in these markets. Our competitors could:

- offer lower prices, more attractive discount plans or better services and features;
- develop and deploy more rapidly new or improved technologies, services and products;
  - launch bundle offerings of one type of service with others;
- in the case of the mobile industry, subsidize handset procurement; or
  - expand and enhance their networks more rapidly.

Furthermore, some of our competitors in certain markets have, and some potential competitors may enjoy, in certain markets, competitive advantages, including the following:

- greater brand name recognition;
- greater financial, technical, marketing and other resources;
- dominant position or significant market power;
  - better strategic alliances;
  - larger customer bases; and
- well-established relationships with current and potential customers.

To compete effectively with our competitors, we need to successfully market our 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 by our competitors, pricing strategies adopted by our competitors and changes in consumer preferences and in general economic, political and social conditions. If we are unable to effectively compete, it could

result in price reductions, lower revenues, under-utilization of our services, reduced operating margins and loss of market share, any of which could have a material adverse effect on our business, financial condition, results of operations and cash flow.

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We operate in a highly regulated industry, which could adversely affect our businesses.

As a multinational telecommunications company that operates in regulated markets, we are subject to different laws and regulations in each of the jurisdictions in which we provide services. Furthermore, the licensing, construction, operation and interconnection arrangements of our communications systems are regulated to varying degrees by the European Union, national, state, regional and local authorities. Furthermore, our activities are subject to strict regulation in many of the countries and market segments in which we operate, particularly in many areas of the fixed telephony business.

Regulatory authorities regularly intervene in the offering and pricing of our products and services. Furthermore, they could also adopt regulations or take other actions that could adversely affect us, including revocation of or failure to renew any of our licenses, authorizations or concessions, changes in the spectrum allocation, revocation of or failure to renew authorizations or concessions to offer services in a particular market, changes in the regulation of international roaming prices and mobile termination rates, introduction of virtual mobile operators, and regulation of the local loop. Such regulatory actions could place significant competitive and pricing pressure on our operations, and could have a material adverse effect on our business, financial condition, results of operations and cash flow.

Regulatory policies applicable in many of the countries in which we operate are designed to increase competition in most of our market segments, especially in the fixed telephony, broadband and mobile telephony segments, including by, among other methods, granting new licenses in existing licensed territories in order to permit the entry of new competitors or imposing special rules and obligations upon currently present operators, such as the requirement for number portability in those countries where it has not yet been implemented. Since these regulatory policies are designed to favor the entry and establishment of new operators, they are likely to have the effect, over time, of reducing our market share in the relevant markets in which we operate.

In addition, since we hold a leading market share in many of the countries where we operate, we could face regulatory actions by the European Union or national antitrust or competition authorities if it is determined that we have prevented restricted or distorted competition in such markets. These authorities could prohibit us from taking further actions such as making further acquisitions or continuing to engage in particular practices or impose fines or other penalties on us, which, if significant, could result in loss of market share and harm to our financial performance and future growth.

Furthermore, we can expect the regulatory landscape to change in Europe as a consequence of the revised regulations resulting from the review of the common regulatory framework currently in place in the European Union. These revised regulations are expected to be approved at the end of 2009 or the beginning of 2010 and could result in increases in the regulatory pressure on the competitive environment in every national market. This could lead national regulatory authorities to impose as a remedy in certain and exceptional circumstances the functional separation of the retail and wholesale operations of operators with significant market power, or the regulation and supervision of the wholesale and retail markets via the creation of a new European body composed of national regulatory authorities.

We may also face new regulatory initiatives in the area of mobile telecommunications in Europe, including increased regulatory pressure on international roaming tariffs for data and SMS services and on mobile termination rates. In addition, we may also face pressure from regulatory initiatives in some European countries regarding the reform of spectrum rights of use and spectrum allocation.

Finally, the recent adoption of new regulations regarding wholesale services (such as access to ducts or dark fiber) in Spain may result in an increase of competitive pressures in the provision of high speed telecommunication services. For further information regarding the matters discussed above and other aspects of the regulatory environments in which our businesses operate, see “Item 4. Information on the Company—Business

Overview—Regulation”.

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We operate under licenses, authorizations and concessions granted by government authorities.

Most of our operating companies require licenses, authorizations or concessions from the governmental authorities of the countries in which they operate. These licenses, authorizations and concessions specify the types of services permitted to be offered by the operating company holding such license, authorization or concession. The continued existence and terms of our licenses, authorizations and concessions are subject to review by regulatory authorities in each country and to interpretation, modification or termination by these authorities. Moreover, authorizations, licenses and concessions as well as their renewal terms and conditions may be affected by political and regulatory factors.

The terms of these licenses, authorizations and concessions granted to our operating companies and conditions of the renewals of such licenses, authorizations and concessions vary from country to country. Although license, authorization and concession renewal is not usually guaranteed, most licenses, authorizations and concessions do address the renewal process and terms. As licenses, authorizations and concessions approach the end of their terms, we intend to pursue their renewal to the extent provided by the relevant licenses, authorizations or concessions, although we cannot guarantee that we will always complete this process successfully.

Many of our licenses, authorizations and concessions are revocable for public interest reasons. The rules of some of the regulatory authorities with jurisdiction over our operating companies require us to meet specified network build-out requirements and schedules. In particular, our existing licenses, authorizations and concessions typically require us to satisfy certain obligations, including, amongst others, minimum specified quality standards, service and coverage conditions and capital investment. Failure to comply with these obligations could result in the imposition of fines or revocation or forfeiture of the license, authorization or concession for the relevant area. In addition, the need to meet scheduled deadlines may require our companies to expend more resources than otherwise budgeted for a particular network build-out.

For further information regarding the licenses and concessions of our operating companies, see “Item 4. Information on the Company—Business Overview—Regulation”.

The industry in which we operate is subject to rapid technological changes, which requires us to continuously adapt to such changes and to upgrade our existing networks. If we are unable to adapt to such changes, our ability to provide competitive services could be materially adversely affected.

Our future success depends, in part, on our ability to anticipate and adapt in a timely manner to technological changes. We expect that new products and technologies will emerge on a continuous basis and that existing products and technologies will further develop. These new products and technologies may reduce the prices for our existing services or may be superior to, and render obsolete, the products and services we offer and the technologies we use and may consequently reduce the revenues generated by our products and services and require investment in new technology. In addition, we may be subject to competition in the future from other companies that are not subject to regulation as a result of the convergence of telecommunications technologies. As a result, it may be very expensive for us to upgrade our products and technology in order to continue to compete effectively with new or existing competitors. Such increased costs could adversely affect our business, financial condition, results of operations and cash flow.

In particular, we must continue to upgrade our existing mobile and fixed line telephony networks in a timely and satisfactory manner in order to retain and expand our customer base in each of our markets, to enhance our financial performance and to satisfy regulatory requirements. Among other things, we could be required to upgrade the functionality of our networks to accommodate increased customization of services, to increase coverage in some of our markets, or to expand and maintain customer service, network management and administrative systems.

Many of these tasks are not entirely under our control and may be affected by applicable regulations. If we fail to execute these tasks successfully, our services and products may be less attractive to new customers and we may lose existing customers to our competitors, which would adversely affect our business, financial condition, results of operations and cash flow.

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Spectrum capacity may become a limiting factor.

Our mobile operations in a number of countries may rely on our ability to acquire additional spectrum. The failure to obtain sufficient capacity and spectrum coverage could have a material adverse impact on the quality of our services and on our ability to provide new services, adversely affecting our business, financial condition, results of operations and cash flow.

Our business could be adversely affected if our suppliers fail to provide necessary equipment and services on a timely basis.

We depend upon a small number of major suppliers for essential products and services, mainly network infrastructure and mobile handsets. These suppliers may, among other things, extend delivery times, raise prices and limit supply due to their own shortages and business requirements. Furthermore, these suppliers may be adversely affected by current economic conditions. If these suppliers fail to deliver products and services on a timely basis, our business and results of operations could be adversely affected. Similarly, interruptions in the supply of telecommunications equipment for our networks could impede network development and expansion, which in some cases could adversely affect our ability to satisfy our license terms and requirements.

We may be adversely affected by unanticipated network interruptions.

Unanticipated network interruptions as a result of system failures whether accidental or otherwise, including due to network, hardware or software failures, which affect the quality of or cause an interruption in our service, could result in customer dissatisfaction, reduced revenues and traffic and costly repairs and could harm our reputation. We attempt to mitigate these risks through a number of measures, including backup systems and protective systems such as firewalls, virus scanners and building security. However, these measures are not effective under all circumstances and cannot avert every action or event that could damage or disrupt our technical infrastructure. Although we carry business interruption insurance, our insurance policy may not provide coverage in amounts sufficient to compensate us for any losses we may incur.

The mobile industry may be harmed by reports suggesting that radio frequency emissions cause health problems.

Over the last few years, the debate about the alleged potential effects of radio frequency emissions on human health has increased significantly. In many cases, this has hindered the deployment of the infrastructures necessary to ensure quality of service.

Institutions and organizations, such as the World Health Organization (WHO), have stated that exposure to radio frequency emissions generated by mobile telephony, within the limits established, has no adverse effects on health. In fact, a number of European countries, including Spain among others, have drawn up complete regulations reflecting the Recommendation of the Council of the European Union dated July 12, 1999. These add planning criteria for new networks, thus ensuring compliance with the limits on exposure to radio frequency emissions.

Whether or not other research or studies conclude there is a link between radio frequency emissions and health, popular concerns about radio frequency emissions may discourage the use of mobile communication devices and may result in significant restrictions on both the location and operation of cell sites, either or both of which could have a detrimental impact on our mobile companies and consequently on our financial condition, results of operations and cash flow. While we are not aware of any evidence confirming a link between radio frequency emissions and health problems and we continue to comply with good practices codes and relevant regulations, there can be no assurance of what future medical research may suggest.

Developments in the telecommunications sector have resulted, and may in the future result, in substantial write-downs of the carrying value of certain of our assets.

We review on an annual basis, or more frequently where the circumstances require, the value of each of our assets and subsidiaries to assess whether the carrying values of such assets and subsidiaries can be supported by the future cash flows expected to be derived from such assets and subsidiaries, including in some cases synergies included in their acquisition costs. The current economic environment and changes in the short and medium term,



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as well as changes in the regulatory, business or political environment may result in the necessity of recognizing impairment charges on our goodwill, intangible assets or fixed assets.

Although the recognition of impairments of tangible, intangible and financial assets result in a non-cash charge on the income statement, such charge would adversely affect our results of operations and consequently, our ability to achieve our growth targets.

### Other Risks

We are involved in disputes and litigation with regulators, competitors and third parties.

We are party to lawsuits and other legal, regulatory and antitrust proceedings in the ordinary course of our business, the final outcome of which is generally uncertain. Litigation and regulatory proceedings are inherently unpredictable. An adverse outcome in, or any settlement of, these or other proceedings (including any that may be asserted in the future) could result in significant costs to us. Such disputes and litigation (or settlements thereof) may have a material adverse effect on our business, financial condition, results of operations and cash flow. Moreover, our involvement in these disputes or proceedings may adversely affect our reputation.

For a more detailed description of current legal proceedings, see “Item 8. Financial Information—Legal Proceedings”.

## Item 4. Information on the Company

### A. History and Development of the Company

#### Overview

Telefónica, S.A., is a corporation duly organized and existing under the laws of the Kingdom of Spain, incorporated on April 19, 1924. We are:

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

The following significant events occurred in 2008:

- In March 2008, Telco, S.p.A., or Telco, acquired 0.9% of Telecom Italia S.p.A.’s, or Telecom Italia’s, ordinary share capital for an aggregate purchase price of €149.8 million, and as a result Telco’s voting rights in Telecom Italia’s ordinary share capital increased from 23.6% to 24.5% and its dividend rights to 16.9%. Our indirect stake in Telecom Italia’s ordinary share capital as a result of this transaction has increased to 10.4%.
- On April 3, 2008, Vivo Participações, S.A., or Vivo, completed the acquisition of 53.90% of the voting stock and 4.27% of the preferred stock of Telemig Celular Participações, S.A., the controlling shareholder of Telemig Celular, S.A. The total purchase price was 1,163 million Brazilian reais (equivalent to approximately €429 million at the transaction date). Vivo also acquired the right held by the seller to subscribe in the future for paid up shares in Telemig Celular Participações, S.A. for a price of approximately 70 million Brazilian reais (equivalent to approximately €26 million at the agreement date).

- On April 8, 2008, Vivo, through its subsidiary Tele Centro Oeste IP, S.A., or TCO, launched a voluntary tender offer for shares representing up to one-third of the free float represented by the preferred stock of Telemig Celular Participações, S.A. and its subsidiary Telemig Celular, S.A. at a price of 63.9 and 654.7 Brazilian reais per share, respectively. This offer, which concluded on May 15, 2008, had an acceptance rate of close

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to 100%, which resulted in the acquisition by TCO of 31.9% and 6% of the preferred shares of Telemig Celular Participações, S.A. and Telemig Celular, S.A., respectively.

- On July 15, 2008, we executed a deed of capital reduction to reflect the reduction of our capital through the cancellation of 68,500,000 of our treasury shares. After such capital reduction our share capital stood at €4,704,996,485, made up of an equal number of ordinary shares.
- On September 17, 2008, we launched a tender offer through our Inversiones Telefónica Internacional Holding, Ltda. subsidiary to acquire all the outstanding shares of Compañía de Telecomunicaciones de Chile, S.A., or CTC, that we did not already control directly or indirectly, amounting to 55.1% of CTC's share capital. This included all CTC shares listed on the Santiago de Chile and New York Stock Exchanges (represented by American Depositary Shares).

Upon completion of the acceptance period of the tender offer, a total of 496,341,699 shares issued by CTC were tendered, representing 94.11% of the shares to which the offer related and a total investment by us of approximately €640 million.

Upon settlement of the transaction, we increased our indirect ownership in CTC's share capital from 44.9% to 96.75%.

On December 1, 2008 we, through our subsidiary Inversiones Telefónica Internacional Holding, Ltda., made a second tender offer to acquire all the outstanding shares of CTC that we did not own, directly or indirectly, after settlement of the first offer (representing the remaining 3.25% of CTC's share capital), on the same economic terms as the initial bid. In January 2009, upon completion of the acceptance period of the second offer, our indirect ownership in CTC had increased from 96.75% of the total outstanding shares to 97.89%.

Business areas

We have implemented a regional, integrated management model based on three business areas, with each area in charge of the fixed and mobile telephone and other businesses within its borders:

- Telefónica Spain: oversees the fixed and mobile telephone, broadband, Internet, pay TV and valued added services and data businesses in Spain.
- Telefónica Europe: oversees the fixed and mobile telephone, broadband, Internet, pay TV and value added services and data businesses in the United Kingdom, Germany, Ireland, the Czech Republic, Slovakia and the Isle of Man.
- Telefónica Latin America: oversees the fixed and mobile telephone, broadband, Internet, pay TV and value added services and data businesses in Latin America.

We are also involved in the media and contact center segments through Telefónica de Contenidos and Atento, respectively.

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The following chart shows the organizational structure of the principal subsidiaries of the Telefónica Group at December 31, 2008, including their jurisdictions of incorporation and our ownership interest. For further detail, see Exhibit 8.1 to this Annual Report.

- 
- (1) Ownership in Telefónica Móviles España, S.A.U. is held directly by Telefónica, S.A.
  - (2) 85.5% representing voting interest.
  - (3) Ownership in Telefónica International Wholesale Services. S.L. (Spain) is held 92.51% by Telefónica, S.A. (Spain) and 7.49% by Telefónica Datacorp, S.A.U (Spain).
  - (4) Ownership in O2 (Europe) Ltd. is held directly by Telefónica, S.A.
  - (5) Companies held indirectly by Telefónica, S.A.

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Telefónica, S.A., the parent company of the Telefónica Group, also operates as a holding company with the following objectives:

- coordinate the Group's activities;
- allocate resources efficiently among the Group;
- provide managerial guidelines for the Group;
- manage the Group's portfolio of businesses;
- foster cohesion within the Group; and
- foster synergies among the Group's subsidiaries.

Our principal executive offices are located at Distrito C, Ronda de la Comunicación, s/n, Las Tablas, 28050 Madrid, Spain, and our registered offices are located at Gran Vía, 28, 28013 Madrid, Spain. Our telephone number is +34 900 111 004.

Capital Expenditures and Divestitures

Our principal capital expenditures excluding acquisitions during the three years ended December 31, 2008 consisted of additions to property, plant and equipment and additions to intangible assets. In 2006, 2007 and 2008, our capital expenditures were €8,010 million, €8,027 million and €8,401 million, respectively.

Year ended December 31, 2008

Our capital expenditures increased 4.7% to €8,401 million in 2008 compared to €8,027 million in 2007, mainly as a result of investments made to support the growth in Telefónica Latin America's broadband and pay TV businesses and to further develop ADSL and adapt existing loops to FTTx (fiber optic) technology in order to enhance coverage for new services in Spain and expand the coverage and capacity of our mobile networks in all regions.

Year ended December 31, 2007

Capital expenditures increased by 0.2% to €8,027 million in 2007 from €8,010 million in 2006 principally related to our investments in Spain in our growing Internet and broadband businesses, with significant investments related to ADSL and IP services, such as Imagenio, our IPTV business. In Latin America capital expenditures were directed toward satisfying increased customer demand in our fixed line business (particularly in broadband and pay TV) and increasing coverage and capacity of our second generation, or GSM, networks and acquiring spectrum in Venezuela, Brazil and Panama to expand coverage and guarantee service quality in areas where traffic is heaviest. In 2007, capital expenditures in Europe decreased primarily as a result of Telefónica O2 Germany bringing forward capital investment from 2007 into 2006 as part of our build-out of our mobile third generation, or 3G, network.

Year ended December 31, 2006

In 2006, capital expenditures increased by 46.4% from 2005, impacted by the acquisition of the O2 Group in 2006 and principally due to expenditures relating to investment in broadband networks in Spain and Latin America in response to the need to bring higher capacity and new services to households, triggered by higher-than-forecast customer and market growth. We also made expenditures associated with a faster roll out of 3G networks, mainly in Germany. In

order to meet growing traffic and customer needs, investments were also made in GSM in Latin America (mainly Brazil).

#### Financial Investments and Divestitures

Our principal financial investments in 2008 were made by Inversiones Telefónica Internacional Holding, Ltda., which invested €640 million for the acquisition of the additional 51.85% of CTC, and Vivo, which invested Brazilian reais 1,163 million (equivalent to approximately €429 million at the transaction date) for the acquisition of

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53.90% of the voting stock and 4.27% of the preferred stock of Telemig Celular Participações, S.A.

Our principal financial investments in 2007 were made by Telefónica (€2,314 million for the acquisition of indirect shareholding in Telecom Italia). Our principal financial divestitures in 2007 were the sale of Airwave and Endemol N.V., or Endemol, for £1,932 million (equivalent to approximately €2,841 million at the transaction date) and €2,629 million, respectively.

Our principal financial investments in 2006 were made by Telefónica (€23,553 million for the acquisition of O2 plc, or O2). Our principal financial divestitures in 2006 were the sale of TPI and a 6.6% stake in Sogecable, S.A., or Sogecable, for €1,816 million and €330 million, respectively.

## Public Takeover Offers

The principal public takeover offers which occurred in 2008 and in 2009 through the date of this Annual Report were the following:

- On September 17, 2008, we launched a tender offer through our Inversiones Telefónica Internacional Holding, Ltda. subsidiary to acquire all the outstanding shares of CTC that we did not already control directly or indirectly. For more information on this transaction, see “—Overview”, above.
- On April 3, 2008, Vivo completed the acquisition of 53.90% of the voting stock and 4.27% of the preferred stock of Telemig Celular Participações, S.A. as well as the rights held by the seller to subscribe in the future for paid up shares in Telemig Celular Participações, S.A. For more information on this transaction, see “—Overview”, above.
- On April 8, 2008, Vivo, through its subsidiary TCO, launched a voluntary tender offer for shares representing up to one third of the free float represented by the preferred stock of Telemig Celular Participações, S.A. and in its subsidiary Telemig Celular, S.A. For more information on this transaction, see “—Overview”, above.

Furthermore, in accordance with Brazilian Corporations law, TCO submitted a mandatory tender offer on July 15, 2008, for all of the remaining voting stock of Telemig Celular Participações, S.A. and Telemig Celular, S.A. at a price per share equivalent to 80% of the purchase price of the voting stock of these companies.

On December 19, 2008, approval was given by shareholders of Telemig Celular Participações, S.A., Telemig Celular, S.A. and Vivo in their respective extraordinary meetings to reorganize the Vivo Group, whereby TCO IP was spun off. Its assets were subsequently integrated under Telemig Celular, S.A. and Telemig Celular Participações, S.A., making Vivo a shareholder in both of these Brazilian companies, with direct and indirect stakes at December 31, 2008 amounting to 90.65% of Telemig Celular, S.A. and 58.9% of Telemig Celular Participações, S.A. Both companies are included in the Telefónica Group’s consolidation perimeter using proportionate consolidation.

## Recent Developments

The principal events that have occurred since December 31, 2008 are set forth below:

- On January 7, 2009, upon completion of the acceptance period for the second tender offer we made for CTC’s shares, our indirect stake in CTC increased to 97.89%. For more information on this transaction, see “—Overview” above.
- On January 7, 2009, after the Italian courts rejected Ipse 2000 S.p.A.’s case regarding the UMTS license this company held, we paid an aggregate amount of €241.3 million corresponding to the annual license payments for

2006, 2007 and 2008. At the date of this Annual Report, we owe an additional €151.7 million in this respect. See Note 21.b to the Consolidated Financial Statements.



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- At its meeting of January 28, 2009, the Board of Directors approved a proposal to increase the amount of dividend corresponding to the 2009 fiscal year to €1.15 per share, to be payable in two tranches subject to the appropriate corporate resolutions.
- In accordance with the above, at its meeting of February 25, 2009, the Board of Directors agreed to propose to the 2009 annual shareholders' meeting the payment of a dividend with a charge to reserves of a gross amount of €0.50 per outstanding share carrying dividend rights.
- On March 23, 2009, we signed an agreement with Vodafone to share network infrastructure in Germany, Spain, Ireland and the United Kingdom with detailed discussions ongoing in the Czech Republic. This agreement is expected to reduce the environmental impact of both companies' roll out activities due to the consolidation of existing sites and joint building of new sites.
  - On April 1, 2009, we announced that the second tranche of the 50 million share buyback program announced on October 13, 2008 (as an extension of the share buyback program then in place) was completed on March 31, 2009. Therefore, the share buyback program initiated on February 2008 for a total amount of 150 million shares has been concluded.
- On April 29, 2009, the Board of Directors resolved to pay an interim dividend of €0.50 per share from 2009 net income, such dividend to be paid on May 12, 2009. With this dividend and the last one paid in November 2008, we have achieved our commitment to distribute a dividend of €1.00 per share prior to the end of the first half of 2009.

For information related to our significant financing transactions completed in 2008 and through the date of this Annual Report, see "Item 5. Operating and Financial Review and Prospects – Liquidity and Capital Resources – Anticipated Sources of Liquidity".

B. Business Overview

We increased our customer base, measured in terms of total accesses, by 13.2% to 258.9 million accesses at December 31, 2008 from 228.7 million accesses at December 31, 2007. This growth was primarily driven by a 16.6% increase in mobile accesses, a 20.9% increase in broadband accesses and a 29.7% increase in pay TV accesses. By geographic area, Telefónica Latin America increased its accesses by 18.0% to 158.3 million at December 31, 2008 from 134.1 million at December 31, 2007, primarily as a result of strong growth in broadband, net adds in its mobile business and an expanding pay TV customer base.

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The following table shows our total accesses at the dates indicated. The classifications and explanatory notes below also apply, to the extent applicable, to the tables detailing our accesses by business area and country elsewhere in this section.

|                               | At December 31,  |                  |                  |
|-------------------------------|------------------|------------------|------------------|
|                               | 2006             | 2007 (1)         | 2008<br>(1)(2)   |
|                               | (in thousands)   |                  |                  |
| Fixed telephony accesses (3)  | 42,340.7         | 43,433.6         | 42,930.8         |
| Internet and data accesses    | 12,170.9         | 13,156.6         | 14,654.3         |
| Narrowband accesses           | 3,997.7          | 2,678.7          | 1,997.2          |
| Broadband accesses (4)        | 7,974.8          | 10,320.2         | 12,472.1         |
| Other accesses (5)            | 198.4            | 157.7            | 185.0            |
| Mobile accesses (6)           | 145,125.1        | 167,781.1        | 195,598.9        |
| Pay TV accesses               | 1,064.0          | 1,748.1          | 2,267.5          |
| Final clients accesses        | 200,700.7        | 226,119.4        | 255,451.4        |
| Unbundled local loop accesses | 962.2            | 1,396.5          | 1,748.1          |
| Shared UL accesses            | 527.7            | 776.4            | 602.3            |
| Full UL accesses              | 434.5            | 620.1            | 1,145.8          |
| Wholesale ADSL accesses (7)   | 1,288.6          | 571.7            | 534.7            |
| Other accesses (8)            | 228.6            | 656.0            | 1,150.1          |
| Wholesale accesses            | 2,479.4          | 2,624.2          | 3,433.0          |
| <b>Total accesses</b>         | <b>203,180.2</b> | <b>228,743.6</b> | <b>258,884.4</b> |

(1) At January 1, 2007, Iberbanda accesses are included. At January 1, 2007, Group accesses have been reclassified, to include “fixed wireless” accesses under the caption of fixed telephony. These accesses were previously classified, depending on the country, under mobile or fixed accesses.

(2) At January 1, 2008, fixed wireless public use telephony accesses are included under the caption “fixed telephony accesses”.

(3) PSTN (including public use telephony) x1; ISDN basic access x1; ISDN primary access; 2/6 access x30. Includes the Group’s accesses for internal use.

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

(5) Includes remaining non-broadband final client circuits.

(6) Includes accesses of Telemig from April 2008.

(7) Includes unbundled lines by Telefónica O2 Germany.

(8) Includes circuits for other operators.

## Our Services and Products

### Fixed business

The principal services we offer in our fixed businesses in Spain, Europe and Latin America are:

- Traditional fixed telecommunication services. Our 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 terminal equipment; and telephony information services.
- Internet and broadband multimedia services. Our principal Internet and broadband multimedia services include narrowband switched access to Internet; Internet service provider service; portal and network services; retail and wholesale broadband access through ADSL, LMDS and satellite technologies; residential-oriented value-added services (including instant messaging, concerts and video clips by

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streaming video, e-learning, parental control, firewall protection, anti-virus protection, content delivery and personal computer sales); television services such as Imagenio, our IPTV business, cable television and satellite television; companies-oriented value-added services, like puesto integral o puesto informático, which includes ADSL, computer and maintenance for a fixed price and VoIP services.

- Data and business-solutions services. Our 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. Our 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.

## Mobile business

We offer a wide variety of mobile and related services and products to personal and business customers. Although the services and products available vary from country to country, the following are our principal services and products:

- Mobile voice services. Our principal service in all of our markets is mobile voice telephony.
- Value added services. Customers in most of our markets have access to a range of enhanced mobile calling features, including voice mail, call hold, call waiting, call forwarding and three-way calling.
- Mobile data and Internet services. Current data services offered include Short Messaging Services, or SMS, and Multimedia Messaging Services, or MMS, which allow customers to send messages with images, photographs and sounds. Customers may also receive selected information, such as news, sports scores and stock quotes. We also provide mobile broadband connectivity and Internet access. Through mobile Internet access, our customers are able to send and receive e-mail, browse the Internet, download games, purchase goods and services in m-commerce transactions and use our other data services.
  - Wholesale services. We have signed network usage agreements with several MVNOs in different countries.
- Corporate services. We provide business solutions, including mobile infrastructure in offices, private networking and portals for corporate customers that provide flexible on-line billing. Telefónica Móviles España, S.A.U., or Telefónica Móviles España, offers corporate services through MoviStar Corporativo, and other advanced solutions for data developed for specific sectors.
- Roaming. We have roaming agreements that allow our customers to use their mobile handsets when they are outside of our service territories, including on an international basis.
- Fixed wireless. We provide fixed voice telephony services through mobile networks in Venezuela, Argentina, Peru, Mexico, Ecuador, El Salvador, Guatemala and Nicaragua.
- Trunking and paging. In Spain and Guatemala, we provide digital mobile services for closed user groups of clients and paging services.

- M-payment. Through our subsidiary, Telefónica Móviles España, and together with Vodafone España, Orange and financial institutions and payment processing companies, we have a 13.36% interest in Mobipay España, a company incorporated to develop micro-payments via mobile technology. We also have a 50% interest in Mobipay International, a company incorporated to expedite payments through mobile phones in an international setting. Banco Bilbao Vizcaya Argentaria, S.A. is the other 50% shareholder in Mobipay International.

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The following sections provide a description of the main markets in which we operate. Customer information on the markets in which we operate, including our market share based on accesses, are estimates that we have made based on annual reports and press releases made public by our competitors or information from local regulators in the respective markets.

## Telefónica Spain Operations

Telefónica Spain provides fixed and mobile telephony services, Internet and data and pay TV services in Spain.

Telefónica Spain's total accesses increased 2.0% to 47.3 million accesses at December 31, 2008 from 46.4 million accesses at December 31, 2007. Total accesses at December 31, 2008 included 23.6 million mobile accesses, 15.3 million fixed telephony accesses, 5.7 million Internet and data accesses and 0.6 million pay TV accesses. Additionally, it included 1.7 million unbundled local loop accesses and 0.4 million of wholesale ADSL accesses.

The following table presents, at the dates indicated, selected statistical data relating to our operations in Spain.

|                            | At December 31, |          |          |
|----------------------------|-----------------|----------|----------|
|                            | 2006            | 2007 (1) | 2008 (1) |
|                            | (in thousands)  |          |          |
| Fixed telephony accesses   | 15,949.9        | 15,918.8 | 15,326.3 |
| Internet and data accesses | 4,842.0         | 5,321.8  | 5,670.0  |
| Narrowband accesses        | 1,040.5         | 660.8    | 388.0    |
| Broadband accesses         | 3,742.7         | 4,614.0  | 5,246.4  |
| Other accesses             | 58.8            | 47.0     | 35.6     |
| Mobile accesses            | 21,446.0        | 22,826.6 | 23,604.8 |
| Pre-pay accesses           | 9,303.0         | 9,181.8  | 9,037.0  |
| Pay TV accesses            | 383.0           | 511.1    | 612.5    |
| Final clients accesses     | 42,620.8        | 44,578.2 | 45,213.6 |
| Wholesale accesses         | 1,531.8         | 1,855.5  | 2,136.1  |
| Total accesses             | 44,152.6        | 46,433.6 | 47,349.7 |

(1) At January 1, 2007, Iberbanda accesses are included.

## Telefónica Spain - Fixed business

Telefónica Spain provides fixed telephony services in Spain through the operator Telefónica de España, S.A., or Telefónica de España.

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## Operations

The following table presents, at the dates indicated, selected statistical data relating to the operations of Telefónica de España:

|                                | At December 31, |          |          |
|--------------------------------|-----------------|----------|----------|
|                                | 2006            | 2007     | 2008     |
|                                | (in thousands)  |          |          |
| Fixed telephony accesses       | 15,949.9        | 15,918.8 | 15,326.3 |
| Internet and data accesses     | 4,842.0         | 5,321.8  | 5,670.0  |
| Narrowband accesses            | 1,040.5         | 660.8    | 388.0    |
| Broadband accesses             | 3,742.7         | 4,614.0  | 5,246.4  |
| Other accesses                 | 58.8            | 47.0     | 35.6     |
| Pay TV accesses                | 383.0           | 511.1    | 612.5    |
| Final clients accesses         | 21,174.9        | 21,751.6 | 21,608.8 |
| Wholesale line rental accesses | –               | –        | 9.5      |
| Unbundled local loop accesses  | 939.0           | 1,353.9  | 1,698.0  |
| Shared UL accesses             | 527.7           | 776.4    | 602.3    |
| Full UL accesses               | 411.3           | 577.6    | 1,095.7  |
| Wholesale ADSL accesses        | 586.4           | 495.5    | 423.8    |
| Other accesses                 | 6.4             | 6.0      | 4.7      |
| Wholesale accesses             | 1,531.8         | 1,855.5  | 2,136.1  |
| Total accesses                 | 22,706.7        | 23,607.1 | 23,744.8 |

The total Spanish fixed telephony market grew by an estimated 0.7% in 2008 in terms of number of accesses. During the same period, Telefónica Spain's fixed telephony accesses decreased by 3.7% to 15.3 million accesses at December 31, 2008 from 15.9 million accesses at December 31, 2007. Telefónica Spain had net fixed telephony accesses losses of 0.6 million in 2008, higher than the 31.1 thousand net fixed telephony accesses losses recorded in 2007.

Estimated net adds in the total Spanish broadband market decreased 23.0% to 1.1 million in 2008 from 1.4 million in 2007. The total Spanish broadband access market stood at an estimated 9.3 million accesses at December 31, 2008. Telefónica Spain's broadband accesses increased 13.7% to 5.2 million at December 31, 2008 from 4.6 million accesses at December 31, 2007.

Beginning January 1, 2008, Telefónica Spain changed the business model for its Public Use Telephony, or PUT, service and related contracts in order to maximize its operations within the scope of the applicable regulatory framework (PUT revenues were 0.7% of Telefónica Spain's 2007 revenues). As a result, this business is now managed on a pure wholesale basis, with only net margin booked as revenues. Prior to January 1, 2008, this business was managed on a retail basis and we recorded both gross revenues and the associated sales and marketing expenses required to promote PUT traffic through resellers as separate line items.

The estimated market share of unbundled local loops in the broadband access market in Spain increased to 18.3% at December 31, 2008 from almost 17% at December 31, 2007. Unbundled local loops at December 31, 2008 amounted to 1.7 million accesses, of which 35.5% were shared access loops.

Telefónica Spain's total wholesale ADSL accesses decreased 14.5% to 0.4 million accesses at December 31, 2008 from 0.5 million accesses at December 31, 2007, mainly because of the migration to unbundled local loops. In 2008, Telefónica Spain continued to increase its presence in the pay TV market, achieving a customer base of 0.6 million accesses at December 31, 2008 from 0.5 million accesses at December 31, 2007.

Since 2005 Telefónica Spain has bundled ADSL products with other products in Duo bundles, which include voice services, and Trio bundles, which include voice and IPTV services. The total number of Duo and Trio bundles increased by 19.7% to 4.5 million units at December 31, 2008 from 3.8 million



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units at December 31, 2007. At December 31, 2008, 85% of Telefónica Spain's broadband accesses were included in Duo or Trio bundles compared to 80% at December 31, 2007.

### Sales and marketing

One of our main priorities has been to satisfy customer needs and increase customer loyalty by improving the quality of our customer service and offering a wide range of integrated telecommunications services. We have reinforced our strategy of customer segmentation in order to tailor our services to best meet the specific needs of each customer segment. In addition, with the purpose of increasing our ability to distribute our products and services, we have signed agreements with large Spanish department stores to complement our traditional channels of distribution.

In 2008 we marketed new products and promotions to strengthen our position in the market for fixed-mobile convergence, both for residential and business customers.

In 2008 we were also very active in capturing new fixed telephony customers (which, in many cases, includes broadband customers as well) through "free-connection fee" campaigns. These campaigns stimulated new adds, decreasing the net loss of fixed telephony lines.

During 2008 Telefónica Spain continued marketing bundled ADSL products, which included voice and IPTV services, and communicated to the Comisión del Mercado de las Telecomunicaciones, or the CMT, its intention to start marketing Quadruple bundles, which include fixed telephony, mobile telephony, broadband access and IPTV services.

In July 2008 Telefónica Spain launched a new ADSL offer at 6Mb intended for the residential market and upgraded the existing base of 3Mb customers (for loops compatible with such speed) to 6Mb.

ADSL commercial campaigns carried out to capture new broadband customers were very intense during 2008, in particular the Semana Loca campaigns, which had very positive results for Telefónica Spain. These campaigns introduced new promotions with attractive and competitive prices.

In 2008 Telefónica Spain also launched Fiber to the Home (FTTH) based services, including a new range of products and services named "FUTURA". This line of products includes high speed Internet (currently up to 30Mb), which allows Telefónica Spain to provide its customers with advanced IPTV services such as High Definition (HDTV) channels, Multiroom (allowing clients to watch different TV channels in different rooms) and Digital Video Recording (DVR). This offer was launched in November 2008, once Telefónica Spain received permission from the CMT allowing it to commercialize such products.

In the business segment, we continued to promote our Puesto de Trabajo services, which is a package of services designed to meet the voice, data and IT needs for small- and medium-sized businesses.

The corporate customer service model employed by Telefónica Spain, which is focused on achieving the highest degree of efficiency in customer service, has the following features:

- a 24-hour personal customer service line for purchasing any type of product and service and handling customer queries;
- Telefónica stores (Tiendas Telefónica) where customers can test and buy the products we market, including the opening in 2008 of our flagship store at the historic Telefónica headquarters building on the Gran Vía (Madrid), which is the largest telecommunications store in Spain;

- the Telefónica “virtual” store (Telefónica On Line), accessible by Internet, which offers customers the ability to order and purchase online the majority of services and products we offer; and
- a customer service system for corporate customers, ranging from a telephone help line for businesses to the assignment of sales managers to address the needs of larger corporate clients.

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### Competition

Telefónica Spain's main competitors in the fixed telephony market fall within three main categories:

- cable operators, such as Spanish nationwide cable operator ONO, which offers trio bundles, and regional cable operators;
- ULL operators, such as Orange and Ya.com (both directly or indirectly owned by France Telecom), Jazztel and Tele2 (owned by Vodafone); and
  - large-business oriented operators, such as British Telecom and Colt, which offer voice and data VPNs.

With the acquisition of Tele2, Vodafone now offers bundles of “naked” ADSL plus home zone mobile voice and fixed numbering.

Telefónica Spain's estimated market share at December 31, 2008 was as follows:

- fixed telephony accesses market share amounted to approximately 77% of retail accesses (down from approximately 81% at December 31, 2007);
- broadband market share amounted to approximately 57% of retail accesses (up from approximately 56% at December 31, 2007); and
- pay TV market share amounted to approximately 14% of the market in terms of accesses (up from approximately 13% at December 31, 2007).

In November 2008, the CMT approved “Wholesale Access for Telephone Lines”, or AMLT, a new product that allows operators to resell telephone lines to their final customers.

### Network and technology

Telefónica Spain has made significant investments to develop its broadband access business through ADSL technology, strongly increasing the coverage and the development of Imagenio, our IPTV service. Additionally Telefónica Spain has begun deploying a new fiber access network, or FTTX, which currently offers only limited coverage.

### Telefónica Spain - Mobile business (Spain)

Telefónica Spain provides mobile services in Spain through the operator Telefónica Móviles España.

### Operations

The Spanish mobile market exceeded 53.1 million accesses at December 31, 2008, which represented a penetration rate of 116%, an increase of more than 5 percentage points from December 31, 2007. The Spanish mobile market showed growth as a result of a decline of mobile handset prices and per minute call rates, and the success of pre-pay calling plans, with strong competition in number portability and pressure on pricing, including termination rate reductions along with the entry of new competitors such as MVNOs.

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The following table presents, at the dates or for the periods indicated, selected statistical data relating to Telefónica Spain's mobile business.

|                                      | At or for the year ended December |          |          |
|--------------------------------------|-----------------------------------|----------|----------|
|                                      | 31,<br>2006                       | 2007     | 2008     |
| Total mobile accesses (in thousands) | 21,446.0                          | 22,826.6 | 23,604.8 |
| Pre-pay accesses (in thousands)      | 9,303.0                           | 9,181.8  | 9,037.0  |
| MOU (minutes)                        | 156                               | 161      | 156      |
| ARPU (in euros)                      | 32.9                              | 32.3     | 30.4     |

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Our mobile customer base in Spain, measured in terms of accesses, increased 3.4% to 23.6 million accesses at December 31, 2008 compared to 22.8 million accesses at December 31, 2007. This growth was primarily driven by a 6.8% increase in accesses in the contract segment. At December 31, 2008, approximately 61.7% of our mobile accesses in Spain were through a contract, which represents an increase of 1.9 percentage points from December 31, 2007.

In the context of an increasingly competitive market, with strong competition in number portability and pressure on pricing, along with the entry of new competitors, Telefónica Móviles España estimated that it had the highest share of net adds in the Spanish mobile market in 2008 (approximately 31.3% based on accesses), thanks to its competitive tariff scheme, strong focus on high value customers and effective marketing and advertising strategies. Telefónica Spain's mobile business achieved net adds of 0.8 million accesses in 2008, down from net adds of 1.4 million accesses in 2007, with a noteworthy number of net accesses gains in the contract segment, 0.9 million accesses in 2008, down sharply from 1.5 million in 2007.

Commercial activity fell by 2.4% to 11.7 million commercial actions in 2008.

In terms of portability, which is customers transferring their number to Telefónica Móviles España from a competitor, Telefónica Móviles España's total net adds was a negative figure of 61.3 thousand lines in 2008. However, by continuing to focus on the higher value customer segments, net portability adds of contract lines was a positive figure of 38.8 thousand lines in 2008.

In terms of usage, the volume of traffic carried by Telefónica Móviles España grew 3.3% to more than 65,000 million minutes in 2008 from over 63,300 million minutes in 2007. "On net traffic", which means traffic originated and terminated on our network, rose 2.8% in 2008 compared to 2007. MOU decreased 2.8% to 156 minutes in 2008 from 161 minutes in 2007.

ARPU for Telefónica Spain's mobile business decreased 5.9% to €30.4 in 2008 from €32.3 in 2007. The decrease was partially driven by a decrease in voice ARPU of 8.5% to €25.2 in 2008 from €27.6 in 2007 as a result of increased competition, interconnection price cuts and roaming-out regulation. Outgoing voice ARPU also decreased 7.4% to €21.2 in 2008 from €22.9 in 2007. These decreases were partially offset by an increase in data ARPU of 9.3% to €5.2 in 2008 from €4.8 in 2007, with outgoing data ARPU growing 10.5% to €4.7 in 2008 from €4.2 in 2007.

At December 31, 2008, Telefónica Spain's customers held more than 6.2 million UMTS/HSDPA handsets, representing a penetration of 27% of our accesses base, excluding machine to machine, or M2M, an increase of 11.5 percentage points from December 31, 2007.

### Sales and marketing

Telefónica Spain is focused on key initiatives to preserve its position as a leading mobile operator in the market, leading it to increase commercial efforts with measures including:

- in-depth market segmentation, with a focus on customer value;
- programs to promote customer loyalty;
- pricing policy to stimulate usage, including launching segmented packages and innovative tariff options; and
- leveraging of UMTS to develop new services, deploying the network ahead of competitors.

Since Telefónica Spain began providing mobile services in Spain, its sales and marketing strategy has been to generate increased brand awareness and customer satisfaction to achieve customer growth and increased revenues. Telefónica Spain utilizes several types of marketing channels, including television, radio, exterior billboards, telemarketing, direct mail and Internet advertising. Telefónica Spain also sponsors several cultural and sporting events in order to increase its brand recognition.

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During 2008 Telefónica Spain's main marketing campaigns focused on boosting demand for mobile broadband, with the launch of data flat rates, and by serving as the exclusive distributor in Spain of high-capacity data transmission devices such as the iPhone. Also, we exclusively launched, during the launch campaign, the high-capacity data transmission devices "Nokia N96" and "Nokia N5800". In addition, Telefónica Spain offers ASSUS laptops, which allow customers to access mobile broadband services. These favorable data rates and mobile broadband capable devices have been bundled by Telefónica Spain in order to promote an increase in the number of accesses and level of use of mobile broadband services in Spain.

With respect to mobile voice service, Telefónica Spain promoted access to medium-range mobile phones for pre-pay customers with the launch of "Movistar Mix", and responded to the needs of cost control of different customer segments with different ranges of flat rate plans including: Planazos launched in October 2008 for residential customers that are high users of voice services, Autónomos Tú Eliges launched in September 2008 for independent professional customers, Megabonos in May 2008 for residential customers who are high users of messaging and Tarifa Plana Familiar in October 2008, designed for residential customers calling between family members.

## Competition

Telefónica Spain's main competitors in the Spanish market for mobile communications service are: Vodafone España, a subsidiary of Vodafone plc, Orange, which is the trade name of France Telecom España S.A., Yoigo, whose principal shareholder is TeliaSonera, and other MVNO operators.

Telefónica Spain's estimated market share in Spain in terms of mobile accesses was approximately 44% at December 31, 2008 (down from approximately 45.1% at December 31, 2007.)

## Network and technology

Telefónica Spain's digital network in Spain is based upon the GSM/UMTS standard. The prevalence of the GSM standard, together with Telefónica Spain's international roaming agreements, enable its mobile customers to make and receive calls in more than 200 countries worldwide. Telefónica Spain's GSM/UMTS based network provides its customers with access to many of the most advanced mobile handsets and a full range of services and products.

In 2007 and 2008, Telefónica Spain invested an aggregate amount of approximately €1,333 million in building out and enhancing its networks in Spain and developing its technological platforms and information systems. At December 31, 2008, Telefónica Spain's GSM/GPRS digital network in Spain, which consisted of 113 switching centers and approximately 22,000 base stations, provided coverage to approximately 99% of the Spanish population. In 2008, Telefónica Spain accelerated the expansion of its UMTS network with 1,324 new base stations with a total of more than 9,200 UMTS base stations installed at the end of the year.

## Telefónica Europe

Telefónica Europe's principal activities are the provision of fixed and mobile telephony services, Internet and data and pay TV services in the United Kingdom, Germany, the Czech Republic and the Isle of Man and of mobile telecommunications services in Ireland and Slovakia.

The Telefónica Europe business area was created in 2006 following our acquisition of the O2 Group.

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The following table presents, at the dates indicated, selected statistical data relating to our operations in Europe.

|                            | At December 31, |          |          |
|----------------------------|-----------------|----------|----------|
|                            | 2006            | 2007     | 2008     |
|                            | (in thousands)  |          |          |
| Fixed telephony accesses   | 2,462.9         | 2,130.0  | 1,952.7  |
| Internet and data accesses | 607.1           | 880.0    | 1,354.5  |
| Narrowband accesses        | 143.7           | 202.4    | 163.4    |
| Broadband accesses         | 451.9           | 670.3    | 1,158.7  |
| Other accesses             | 11.6            | 7.3      | 32.4     |
| Mobile accesses            | 35,225.2        | 38,263.8 | 41,182.1 |
| Pay TV accesses            | 15.6            | 73.2     | 114.5    |
| Final clients accesses     | 38,310.9        | 41,347.0 | 44,603.8 |
| Wholesale accesses         | 243.8           | 706.2    | 1,237.9  |
| Total accesses             | 38,554.7        | 42,053.2 | 45,841.7 |

Telefónica Europe's total accesses increased 9.0% to 45.8 million accesses at December 31, 2008 from 42.1 million accesses at December 31, 2007. Total accesses at December 31, 2008 included 41.2 million mobile accesses, 2.0 million fixed telephony accesses, 1.4 million Internet and data accesses and 0.1 million pay TV accesses. Additionally, it included 1.2 million ADSL wholesale accesses.

## United Kingdom – Telefónica O2 UK

## Operations

The following tables present, at the dates or for the periods indicated, selected statistical data relating to our operations in the United Kingdom.

|                            | At December 31, |          |          |
|----------------------------|-----------------|----------|----------|
|                            | 2006            | 2007     | 2008     |
|                            | (in thousands)  |          |          |
| Internet and data accesses | 16.8            | 70.7     | 340.9    |
| Broadband accesses         | 16.8            | 70.7     | 340.9    |
| Mobile accesses            | 17,633.2        | 18,382.1 | 19,470.0 |
| Pre-pay accesses           | 11,415.1        | 11,573.4 | 11,862.5 |
| Final clients accesses     | 17,650.0        | 18,452.8 | 19,810.8 |
| Total accesses             | 17,650.0        | 18,452.8 | 19,810.8 |

  

|                | Year ended December 31, |      |      |
|----------------|-------------------------|------|------|
|                | 2006                    | 2007 | 2008 |
| MOU (minutes)  | 171                     | 190  | 207  |
| ARPU (in eros) | 33.4                    | 34.4 | 30.0 |

The mobile penetration rate in the United Kingdom increased four percentage points to 123% at December 31, 2008 from December 31, 2007.

Telefónica O2 UK, Telefónica Europe's operating company in the United Kingdom, had total net adds of 1.4 million accesses in 2008, 69.1% more than its net adds in 2007. Total accesses increased 7.4% to 19.8 million accesses at



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December 31, 2008 compared to 18.5 million accesses at December 31, 2007 (excluding the Tesco mobile customer base, which is the result of a joint venture in which Telefónica O2 UK holds a 50% stake and whose customers use the Telefónica O2 UK network).

Telefónica O2 UK added 0.8 million contract accesses in 2008, bringing the total at December 31, 2008 to 7.6 million contract accesses, an increase of 11.7% from December 31, 2007. Pre-pay accesses increased by 0.3 million accesses from December 31, 2007 to 11.9 million accesses at December 31, 2008. At December 31, 2008 contract

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accesses made up 39.1% of Telefónica O2 UK's mobile customer base, compared to 37.0% at December 31, 2007. At December 31, 2008 Telefónica O2 UK had 0.3 million broadband accesses compared to 0.1 million broadband accesses at December 31, 2007.

Contract ARPU decreased to €53.3 in 2008 from €63.2 in 2007 (a decrease of 2.1% in local currency). Pre-pay ARPU decreased to €15.5 in 2008 from €18.1 in 2007 (a decrease of 0.6% in local currency). ARPU was €30.0 in 2008 down from €34.4 in 2007 (an increase of 1.4% in local currency). This increase in local currency ARPU was caused by the higher proportion of contract accesses in the customer base, customer adoption of new products and services and the continued growth in data ARPU. MOU increased 9.1% to 207 minutes in 2008 from 190 minutes in 2007.

### Sales and marketing

In the United Kingdom, we use a broad range of marketing channels, including television, radio, billboards, telemarketing, direct mail and Internet advertising to market Telefónica O2 UK's products and services.

In 2008, Telefónica O2 UK continued its focus on high-value customers across various segments with offerings such as "Simplicity", the 3G iPhone and mobile broadband. In 2008, Telefónica O2 UK topped the list of fixed and mobile broadband Internet service providers (ISPs) in the United Kingdom for customer satisfaction, according to a recent report by JD Power and Associates published in February 2009. The marketing firm conducted two customer satisfaction studies based on five factors that drive overall satisfaction with the provision of mobile and fixed broadband: performance and reliability, billing, cost, customer service/technical support, and offerings/promotions.

### Competition

Telefónica O2 UK, estimated market share was approximately 25.9% at December 31, 2008 compared with approximately 24.6% at December 31, 2007, based on the number of mobile accesses.

In addition to Telefónica O2 UK, there are currently four other network operators in the UK mobile telecommunications market: Vodafone UK, a subsidiary of Vodafone plc, T-Mobile, a subsidiary of Deutsche Telecom, Orange, owned by France Telecom, and 3, owned by Hutchison Whampoa. MVNOs operating in the UK market include Virgin Mobile and Fresh, owned by Virgin Media and The Carphone Warehouse Group, respectively, which both use T-Mobile's network, and Tesco Mobile, a joint venture in which Telefónica O2 UK holds a 50% stake and which uses the Telefónica O2 UK network.

### Network and technology

Telefónica O2 UK's digital network in the United Kingdom is based upon the GSM/UMTS standard. The prevalence of the GSM standard, together with Telefónica O2 UK's international roaming agreements, enables Telefónica O2 UK customers to make and receive calls in more than 200 countries worldwide. At December 31, 2008, Telefónica O2 UK's GSM/GPRS digital network consisted of approximately 11,482 base stations.

Telefónica O2 UK had rolled out ULL capabilities to 1,218 exchanges by the end of 2008, giving its broadband network population coverage of 65.9% in terms of the UK population.

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## Germany – Telefónica O2 Germany

## Operations

The following tables present, at the dates or for the periods indicated, selected statistical data relating to our operations in Germany.

|                            | At December 31,         |          |          |
|----------------------------|-------------------------|----------|----------|
|                            | 2006                    | 2007     | 2008     |
|                            | (in thousands)          |          |          |
| Internet and data accesses | 19.0                    | 74.7     | 214.8    |
| Broadband accesses         | 19.0                    | 74.7     | 214.8    |
| Mobile accesses            | 11,024.8                | 12,471.5 | 14,198.5 |
| Pre-pay accesses           | 5,544.1                 | 6,235.0  | 7,231.5  |
| Final clients accesses     | 11,043.8                | 12,546.2 | 14,413.3 |
| Wholesale accesses         | 149.3                   | 596.0    | 1,128.4  |
| Total accesses             | 11,193.1                | 13,142.3 | 15,541.7 |
|                            | Year ended December 31, |          |          |
|                            | 2006                    | 2007     | 2008     |
| MOU (minutes)              | 127                     | 131      | 138      |
| ARPU (in euros)            | 24.2                    | 20.4     | 17.4     |

The mobile penetration rate in Germany increased to 132.4% at December 31, 2008, an increase of 16.2 percentage points compared to the penetration rate at December 31, 2007.

Telefónica O2 Germany's total customer base, in terms of accesses, increased by 2.4 million accesses from December 31, 2007 to 15.5 million accesses at December 31, 2008. Telefónica O2 Germany's joint venture with Tchibo Mobile was responsible for 0.1 million of this increase in accesses from December 31, 2007 to 1.3 million accesses at December 31, 2008, while Telefónica O2 Germany's "Fonic" low-cost brand, added 0.5 million accesses from December 31, 2007, giving it a customer base of 0.7 million accesses at December 31, 2008. In addition at December 31, 2008, 3.1 million of Telefónica O2 Germany's accesses were on the "Genion S/M/L/XL" tariff structure, which is a flat rate tariff for calls made within and outside of the "Homezone".

Throughout 2008 Telefonica O2 Germany continued its program of migrating customers from legacy to new tariffs such as "Genion S/M/L/XL" and "Inklusivpakete", which offer significantly better value to the customer.

Telefónica O2 Germany had net adds of 0.7 million contract accesses and 1.0 million pre-pay accesses in 2008, bringing the pre-pay customer base at December 31, 2008 to 7.2 million accesses.

ARPU continued to decline in 2008, decreasing 14.9% to €17.4 in 2008 from €20.4 in 2007, partly as a result of an approximately 10% cut in the interconnection rate in November 2007, the level of competition in the German market and the previously described migration program. Contract ARPU decreased 15.0% to €29.0 in 2008 from €34.1 in 2007. Pre-pay ARPU decreased 11.0% to €5.9 in 2008 from €6.7 in 2007. MOU in 2008 was 138 minutes, an increase of 5.3% compared to 131 minutes in 2007.

At December 31, 2008 Telefónica O2 Germany had a customer base of 0.2 million broadband accesses. Telefónica O2 Germany reported 1.1 million ULL lines at December 31, 2008, up from 0.6 million lines at December 31, 2007.

Sales and marketing

In 2008, Telefonica O2 Germany continued to build on its core strategy of increasing its distribution network, which was ahead of target with 725 shops at year end. During 2008 Telefónica O2 Germany also launched the “O2 Handy flatrate” with a minimum contract duration of only six months. This contract offers a flat rate for calls to

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other Telefónica O2 Germany customers and to fixed lines with a monthly flat fee of €15. Calls to other networks and SMSs are charged at 19 euro cents per minute or message.

## Competition

Telefónica O2 Germany's estimated market share in Germany was approximately 13.5% at December 31, 2008 compared to approximately 13.0% at December 31, 2007, based on number of mobile accesses.

Telefónica O2 Germany competes primarily with three other companies in the German market for mobile telecommunications. These are T-Mobile, which is owned by Deutsche Telecom, Vodafone Germany, a subsidiary of Vodafone plc, and E-Plus, which is owned by KPN. Telefónica O2 Germany also competes with several MVNOs.

## Network and technology

Telefónica O2 Germany's digital network in Germany is based upon the GSM/UMTS standard. The prevalence of the GSM standard, together with Telefónica O2 Germany's international roaming agreements, enables Telefónica O2 Germany customers to make and receive calls in more than 200 countries worldwide.

At December 31, 2008, Telefónica O2 Germany's GSM/GPRS digital network consisted of approximately 8,951 base stations, the UMTS network consisted of approximately 3,161 base stations and there were approximately 5,887 shared GSM and UMTS base stations.

## Czech Republic and Slovakia – Telefónica O2 Czech Republic and Telefónica O2 Slovakia

Telefónica Europe provides fixed and mobile telephony services in the Czech Republic and mobile telephony services in Slovakia, where it launched operations during the first quarter of 2007.

## Operations

The following tables present, at the dates or for the periods indicated, selected statistical data relating to our operations in the Czech Republic.

|                            | At December 31, |         |         |
|----------------------------|-----------------|---------|---------|
|                            | 2006            | 2007    | 2008    |
|                            | (in thousands)  |         |         |
| Fixed telephony accesses   | 2,402.5         | 2,069.2 | 1,893.4 |
| Internet and data accesses | 560.3           | 719.1   | 779.5   |
| Narrowband accesses        | 143.7           | 202.4   | 163.4   |
| Broadband accesses         | 405.1           | 509.4   | 583.7   |
| Other accesses             | 11.6            | 7.3     | 32.4    |
| Mobile accesses            | 4,864.5         | 5,125.4 | 5,257.2 |
| Pre-Pay accesses           | 2,989.7         | 2,881.5 | 2,737.9 |
| Pay TV accesses            | 15.6            | 73.2    | 114.5   |
| Final clients accesses     | 7,842.9         | 7,986.8 | 8,044.6 |
| Wholesale accesses         | 94.5            | 110.2   | 109.5   |
| Total accesses             | 7,937.4         | 8,097.0 | 8,154.1 |

  

|  | Year ended December 31, |      |      |
|--|-------------------------|------|------|
|  | 2006                    | 2007 | 2008 |

|                |      |      |      |
|----------------|------|------|------|
| MOU (minutes)  | 102  | 117  | 121  |
| ARPU (in eros) | 18.0 | 18.9 | 20.7 |

The mobile penetration rate in the Czech Republic increased to 131% at December 31, 2008, five percentage points higher than the penetration rate at December 31, 2007.

Telefónica O2 Czech Republic's fixed telephony accesses decreased by 8.5% to 1.9 million accesses at December 31, 2008 from 2.1 million accesses at December 31, 2007, mainly as the result of fixed-to-mobile

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substitution. On a net basis, Telefónica O2 Czech Republic lost 47.3% less fixed telephony accesses in 2008 compared to 2007. This improvement compared to 2007 is the result of our strategy of enhancing the quality of fixed lines by improving broadband (basic speed was upgraded up to 8 Mbps, four times higher than the previous speed offered at the same price) and aggressively priced bundled offers.

Telefónica O2 Czech Republic's broadband accesses increased 14.6% compared to December 31, 2007 to 0.6 million accesses at December, 31 2008. The IPTV customer base increased to 0.1 million accesses at December 31, 2008. These increases are primarily as a result of increased demand for these services in the Czech Republic.

Telefónica O2 Czech Republic's mobile accesses increased 2.6% to 5.3 million accesses at December 31, 2008, from 5.1 million accesses at December 31, 2007. Contract accesses accounted for 47.9% of these accesses at December 31, 2008, up from 43.8% at December 31, 2007. The number of pre-pay accesses decreased 5.0% to 2.7 million accesses at December 31, 2008 from 2.9 million accesses at December 31, 2007.

ARPU increased to €20.7 in 2008 from €18.9 in 2007 (a reduction of 0.9% in local currency). Pre-pay ARPU increased to €9.8 in 2008 from €8.9 in 2007 (a reduction of 2.0% in local currency). Contract ARPU increased to €33.5 in 2008 from €32.7 in 2007 (a decrease of 6.7% in local currency primarily due to the introduction of flat-rate tariffs).

MOU for the year stood at 121 minutes, an increase of 3.6% compared to the 117 minutes in 2007. The increase in traffic is due to the growing number of contract customers generating higher average MOU and the launch of "O2 Neon" tariffs.

### Sales and marketing

The launch of "O2 Neon" tariffs designed to stimulate traffic through a simplified, flat tariff structure resulted in increased usage in 2008. By the end of December 2008, 0.3 million customers subscribed for one of the O2 Neon tariffs and O2 Neon accesses accounted for 11% of mobile voice contract accesses.

### Competition

There are currently two other primary competitors in the Czech Republic mobile telecommunications market. These are Vodafone Czech Republic, which is owned by Vodafone plc, and T-Mobile, which is part of Deutsche Telecom AG.

Telefónica O2 Czech Republic had an estimated mobile market share of approximately 38.6% at December 31, 2008 compared to approximately 39.2% at December 31, 2007, based on number of mobile accesses.

The fixed telephony market consists of six large operators and a number of other smaller providers. In voice the major competitors are Ceske Radiokomunikacie, U:fon, UPC and other cable operators which also provide integrated voice, Internet and pay TV offers. Internet service is offered by all major mobile operators as well as a large volume of WiFi providers. Pay TV is dominated by a number of cable and satellite companies, the biggest being UPC.

### Network and technology

Telefónica O2 Czech Republic's digital network in the Czech Republic is based upon the GSM/UMTS standard. The prevalence of the GSM standard, together with Telefónica O2 Czech Republic's international roaming agreements, enables its customers to make and receive calls in more than 200 countries worldwide.

At December 31, 2008, Telefónica O2 Czech Republic's GSM/GPRS digital network consisted of 12,676 base stations.

Slovakia

At December 31, 2008, Telefónica O2 Slovakia's total number of mobile accesses amounted to 0.5 million accesses, a decrease of 19.5% compared to December 31, 2007. In the second half of 2008 Telefónica O2 Slovakia



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launched the “O2 Fér” plan, a simple tariff which unifies pre-pay and contract rates and offers SIM-only products without a handset subsidy.

In 2008, Telefónica O2 Slovakia continued to roll out its own network infrastructure and by December 31, 2008 the company had more than 850 base stations, which fulfilled its license conditions. Its network currently covers close to 90 percent of the population, which is nearly double that required by its license.

## Ireland – Telefónica O2 Ireland

## Operations

The following tables present, at the dates or for the periods indicated, selected statistical data relating to our operations in Ireland:

|                       | At December 31,         |         |         |
|-----------------------|-------------------------|---------|---------|
|                       | 2006                    | 2007    | 2008    |
|                       | (in thousands)          |         |         |
| Total mobile accesses | 1,631.7                 | 1,646.1 | 1,727.7 |
| Pre-pay accesses      | 1,146.7                 | 1,090.9 | 1,084.6 |
|                       | Year ended December 31, |         |         |
|                       | 2006                    | 2007    | 2008    |
| MOU (minutes)         | 236                     | 248     | 245     |
| ARPU (in euros)       | 45.2                    | 45.9    | 43.2    |

The mobile penetration rate in Ireland reached 121% at December 31, 2008, a five percentage point increase over the penetration rate at December 31, 2007.

Telefónica O2 Ireland had net adds of 0.1 million mobile accesses in 2008. Telefónica O2 Ireland’s customer base, in terms of mobile accesses, increased 5.0% from December 31, 2007 to 1.7 million mobile accesses at December 31, 2008. Of Telefónica O2 Ireland’s total customer base, there were 0.1 million mobile broadband accesses at December 31, 2008, after a successful launch in July 2007.

Telefónica O2 Ireland had net adds of 0.1 million contract accesses in its mobile business in 2008, including the mobile broadband accesses mentioned above, an increase of 25.3% on December 31, 2007.

ARPU decreased by 5.9% in 2008 to €43.2 from €45.9 in 2007. Contract ARPU decreased 11.9% to €72.5 in 2008 from €82.3 in 2007 due to the introduction of new customer offers and promotions. Pre-pay ARPU decreased by 7.0% in 2008 to €27.0 in 2008 from €29.0 in 2007. MOU for the year was 245 minutes, a decrease of 1.1% from the 248 minutes in 2007.

## Sales and marketing

During the second quarter of 2008, Telefónica O2 Ireland launched “O2 Clear” an innovative new monthly pay option that gives customers the opportunity to sign up to post pay tariffs on a SIM-only basis without having to commit to a long-term contract. It was the first tariff of its kind in the Irish market. Later in the year Telefónica O2 Ireland introduced the 3G version of the iPhone and in December launched the “O2 Treats” program, a card which allows customers to spend up to €100 on different treats/activities for themselves or a friend.

## Competition

There are currently three other primary competitors in the Irish mobile telecommunications market: Vodafone Ireland, which is part of Vodafone plc, Meteor, which is part of Babcock and Brown, and 3 Ireland, which is part of Hutchison Wampoa Ltd.

Telefónica O2 Ireland had an estimated market share of the Irish mobile market of approximately 32.5% at December 31, 2008 compared to approximately 32.3% at December 31, 2007 based on number of mobile accesses.

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## Network and technology

Telefónica O2 Ireland's digital network in Ireland is based upon the GSM/UMTS standard. The prevalence of the GSM standard, together with Telefónica O2 Ireland's international roaming agreements, enables Telefónica O2 Ireland customers to make and receive calls in more than 200 countries worldwide.

At December 31, 2008, Telefónica O2 Ireland's GSM/GPRS digital network consisted of approximately 1,662 base stations.

## Telefónica Latin America

Telefónica Latin America provides fixed and mobile telephony, Internet and data services and pay TV services through the operators described in the following sections in the main Latin American markets. In addition, Telefónica Latin America's other members include: Telefónica Empresas, Telefónica International Wholesale Services, or TIWS, the business unit responsible for other telecommunications operators and for managing our international services and the network which supports these services, and Terra Networks Latin América.

The following table presents, at the dates indicated, selected statistical data relating to our operations in Latin America.

|                            | At December 31, |           |                |
|----------------------------|-----------------|-----------|----------------|
|                            | 2006            | 2007 (1)  | 2008<br>(1)(2) |
|                            | (in thousands)  |           |                |
| Fixed telephony accesses   | 23,916.9        | 25,381.0  | 25,644.5       |
| Internet and data accesses | 6,723.7         | 6,954.8   | 7,629.8        |
| Narrowband accesses        | 2,813.5         | 1,815.6   | 1,445.8        |
| Broadband accesses         | 3,780.3         | 5,035.9   | 6,067.0        |
| Other accesses             | 130.0           | 103.4     | 117.0          |
| Mobile accesses (3)        | 83,298.4        | 100,542.2 | 123,385.2      |
| Pay TV accesses            | 665.3           | 1,163.8   | 1,540.5        |
| Final clients accesses     | 114,604.4       | 134,041.8 | 158,200.1      |
| Wholesale accesses         | 65.9            | 62.6      | 59.0           |
| Total accesses             | 114,670.3       | 134,104.4 | 158,259.0      |

(1) At January 1, 2007, Group accesses have been reclassified, including "fixed wireless" accesses under the caption of fixed telephony. These accesses were previously classified, depending on the country, under mobile or fixed telephony accesses.

(2) At January 1, 2008, fixed wireless public use telephony accesses are included under the caption "fixed telephony accesses".

(3) Includes accesses of Telemig from April 2008.

Telefónica Latin America's total accesses increased 18.0% to 158.3 million accesses at December 31, 2008 from 134.1 million accesses at December 31, 2007. Total accesses at December 31, 2008 include 123.4 million mobile accesses, 25.6 million fixed telephony accesses, 7.6 million Internet and data accesses and 1.5 million pay TV accesses. Additionally, it includes 0.1 million wholesale accesses.



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The following table sets forth certain information at December 31, 2008 regarding the principal Latin American operating companies of Telefónica Latin America.

| Country     | Company                                      | Population<br>(in millions) | Interest<br>(%) |
|-------------|--|-----------------------------|-----------------|
| Brazil      | Telecomunicações de São Paulo, S.A.—Telesp   | 40.6 (*)                    | 87.95           |
|             | Brasilcel, N.V.(1)                           | 190.4                       | 50.00           |
| Mexico      | Telefónica Móviles México, S.A. de C.V.      | 109.6                       | 100.00          |
| Panama      | Telefónica Móviles Panamá, S.A.              | 3.4                         | 100.00          |
| Nicaragua   | Telefónica Móviles Nicaragua, S.A.           | 5.4                         | 100.00          |
| Guatemala   | Telefónica Móviles Guatemala, S.A.           | 13.5                        | 100.00          |
| El Salvador | Telefónica Móviles El Salvador, S.A. de C.V. | 5.9                         | 100.00          |
| Venezuela   | Telcel, S.A.                                 | 27.7                        | 100.00          |
| Colombia    | Colombia Telecomunicaciones, S.A. ESP.       | 44.7                        | 52.03           |
|             | Telefónica Móviles Colombia, S.A.            |                             | 100.00          |
| Peru        | Telefónica del Perú, S.A.A.                  | 27.9                        | 98.18           |
|             | Telefónica Móviles Perú, S.A.C.              |                             | 97.79           |
| Ecuador     | Otecel, S.A.                                 | 14.5                        | 100.00          |
| Argentina   | Telefónica de Argentina, S.A.                | 39.7                        | 98.05           |
|             | Telefónica Móviles Argentina S.A.            |                             | 100.00          |
| Chile       | Telefónica Chile, S.A.                       | 16.4                        | 96.75           |
|             | Telefónica Móviles Chile, S.A.               |                             | 100.00          |
| Uruguay     | Telefónica Móviles Uruguay, S.A.             | 3.3                         | 100.00          |

(\*) Concession area only.

(1) Jointly controlled and managed by Telefónica and Portugal Telecom. Brasilcel is the holding company which controls the mobile operating company Vivo.

## Brazil

The following table presents, at the dates indicated, selected statistical data relating to our operations in Brazil.

|                            | At December 31, |          |          |
|----------------------------|-----------------|----------|----------|
|                            | 2006            | 2007     | 2008     |
|                            | (in thousands)  |          |          |
| Fixed telephony accesses   | 12,107.1        | 11,960.0 | 11,661.9 |
| Internet and data accesses | 3,556.8         | 3,288.6  | 3,625.8  |
| Narrowband accesses        | 1,856.6         | 1,155.9  | 996.4    |
| Broadband accesses         | 1,608.2         | 2,069.6  | 2,557.8  |
| Other accesses             | 92.0            | 63.1     | 71.6     |
| Mobile accesses(1)         | 29,053.1        | 33,483.5 | 44,945.0 |
| Pre-pay accesses           | 23,543.4        | 27,236.4 | 36,384.0 |
| Pay TV accesses            | —               | 230.9    | 472.2    |
| Final clients accesses     | 44,716.9        | 48,963.1 | 60,704.9 |
| Wholesale accesses         | 38.4            | 37.4     | 34.1     |
| Total accesses             | 44,755.3        | 49,000.5 | 60,739.1 |

(1) Includes accesses of Telemig from April 2008.

Telefónica Latin America's accesses in Brazil increased 24.0% to 60.7 million accesses at December 31, 2008 from 49.0 million accesses at December 31, 2007. This growth reflects a 34% year-on-year increase in Vivo's (Telefónica Latin America's jointly-controlled Brazilian mobile business) customer base and, to a lesser extent, the expansion of Telesp's (Telefónica Latin America's Brazilian fixed line business) broadband and pay TV businesses. These increases were offset by a reduction in the number of fixed telephony accesses at Telesp and a decrease in narrowband Internet accesses primarily as a result of a strong migration to broadband accesses.

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Brazil Fixed Business – Telecomunicações de São Paulo, S.A. – Telesp

### Operations

Telesp provides fixed telephony and other telecommunications services in the Brazilian state of São Paulo under concessions and licenses from Brazil's federal government.

Telesp's fixed telephony, Internet and data and pay TV accesses increased 1.8% to 15.8 million accesses at December 31, 2008 from 15.5 million accesses at December 31, 2007 primarily due to the growth of broadband and pay TV accesses, that offset the reduction in the number of fixed telephony accesses, within the context of increased fixed-to-mobile substitution as a result of strong growth in Brazil's mobile sector, and a decrease in narrowband Internet accesses, as a result of migration to broadband solutions. Telesp's fixed telephony accesses decreased 2.5% to 11.7 million accesses at December 31, 2008 from 12.0 million accesses at December 31, 2007. Of these fixed telephony accesses, 23.8% were pre-pay accesses or accesses with consumption limits.

The Brazilian broadband market continued to grow strongly in 2008. Telesp increased its broadband customer base by 23.6% to 2.6 million accesses at December 31, 2008 from 2.1 million accesses at December 31, 2007. Since 2007 Telesp has marketed "Trio Telefónica", a Trio bundle with different connection speed options and a range of pay TV content choices, including GloboSat content. Telesp offers pay TV mainly through a DTH solution and, since the fourth quarter of 2007 after the acquisition of Navy Tree, also offers MMDS technology, reaching 0.5 million accesses at December 31, 2008, 0.3 million accesses more than at December 31, 2007.

Telesp's voice traffic increased by 7.7% in 2008 (to 76,653 million minutes) compared to 2007, due mainly to growth in long distance traffic from mobile accesses as a result of a joint marketing strategy with Vivo, as well as a higher interconnection traffic coming primarily from mobile networks. Fixed local traffic grew 3.4% despite the reduction in the number of fixed telephony accesses, driven by the implementation of flat rates and minutes bundles. Fixed-to-mobile traffic, measured in minutes, fell 1.7% in 2008 compared to 2007 as a result of a strong migration of traffic to mobile networks.

### Sales and marketing

In Brazil, we employ a differentiated approach to marketing whereby we use a mix of human and technological resources (a specialized team and business intelligence tools, respectively), in addition to specific studies that allow us to target various market segments according to the relevant needs of the customers in each segment. We continuously monitor market trends in an effort to develop new products and services that may address the future needs of our customers.

Telefónica Latin America employs the following strategies to deliver fixed telephony and other telecommunications solutions to residential, small and medium enterprises, or SMEs, and corporate customers in Brazil:

- person-to-person sales: customized sales services to achieve and preserve customer loyalty, customized consulting telecommunication services and technical and commercial support;
- telesales: a telemarketing channel;
- indirect channels: outsourced sales by certified companies in the telecommunications and data processing segments to provide an adequately sized network for our products and services;
- Internet: the Telefónica website;

- virtual shop for corporate clients: a “gateway” for our corporate customers to acquaint themselves with our portfolio through the Internet; and
- door-to-door: door-to-door sales of services by consultants in the State of São Paulo in order to approach more SMEs to convert them into Telefónica Negocios clients.



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We offer bundled products, which include both local and long-distance traffic and minutes bundled with broadband, in response to a growing demand from our clients. We believe that the trend towards bundled offers in Brazil will continue to grow, and that further developing such offers will be important to maintaining our competitiveness in the market.

### Competition

Our fixed telephony business in Brazil currently faces strong competition in the corporate and premium residential segments in respect of several types of services. In the corporate segment, there is strong competition in both voice services (local and long distance) and data transmission, resulting in greater retention costs to maintain client relationships.

Our main competitors in the corporate fixed telephony line segment are Oi, Intelig and Embratel, a subsidiary of Telmex International. In the high-income residential service segment, we compete for long-distance customers with Embratel and for broadband customers with cable TV providers, mainly NET Serviços de Comunicação S.A., or Net. For the local voice and high-income segments, we also face increasing competition from mobile telecommunications services, which have lower rates for certain types of calls, such as mobile-to-mobile calls. Such competition increases our advertising and marketing costs. In 2008, we also saw the entry into the market of small VoIP operators, focused on low- and middle-income corporate clients and SMEs whose impact has not been significant at this point. We are taking several steps to defend ourselves from increasing competition. We are focused on improving our broadband products, by offering bundled services that include voice, broadband and television, and by increasing the access speed offered to our clients. In addition, we are improving our market segmentation and developing more competitive products intended to defend our client base from our competitors' product offerings and to defend our market share.

In the low-income, local fixed telecommunications segment, we face less direct competition due to the low profitability of this market. The most significant competition is from pre-pay mobile telecommunications providers.

Telesp had an estimated market share in the fixed telephony market in the State of São Paulo of approximately 83.5% at December 31, 2008 based on the number of fixed telephony accesses, down from approximately 95.3% at December 31, 2007. This decrease is mainly due to intense competition from Net, which offers its "Net Phone" service as part of its offer of pay TV and broadband.

### Brazil mobile business – Brasilcel (Vivo)

#### Operations

With 150.6 million mobile accesses, Brazil ranked first in Latin America in terms of number of mobile accesses at December 31, 2008. At December 31, 2008, Brazil had an estimated mobile market penetration rate of 79%.

Telefónica and Portugal Telecom are 50:50 shareholders in Brasilcel, a joint venture which combines Telefónica's and Portugal Telecom's mobile businesses in Brazil. This joint venture is the leading mobile operator in Brazil in terms of number of mobile accesses at December 31, 2008. All of the operating companies participating in the joint venture have been operating under the brand name "Vivo" since April 2003. The licensed areas of Brasilcel include 20 states in Brazil with an aggregate population of approximately 190.4 million people.

Vivo's customer base, in terms of number of accesses, increased 34.2% to 44.9 million accesses at December 31, 2008 from 33.5 million accesses at December 31, 2007. Of these, 8.6 million were contract accesses. The primary factors contributing to this growth include the acquisition of Telemig, the wider range of handsets available, Vivo's leadership

in terms of brand and distribution chain, ongoing marketing campaigns for pre-pay traffic and an improved capacity to attract contract accesses with Vivo Escolha plans. At December 31, 2008, 53.9% of residential contract accesses had subscribed to a Vivo Escolha plan, which is a customized plan that allows customers to choose the mix of services with an extra bunch of free voice minutes, messaging, or mobile Internet access, demonstrating the popularity of this offer. These plans also helped to increase customer loyalty by encouraging increased minute consumption and maintaining the perception in the market of Vivo's low prices relative to its competitors. These

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plans are divided into different categories depending on the number of minutes included as well as additional upgrade features, such as extra SMS, extra minutes of long distance calls and extra MMS.

ARPU was €11.2 in 2008 compared to €11.9 in 2007 (a decrease of 5.8% in local currency), reflecting the increased proportion of “SIM only” accesses in the pre-pay customer base and control accesses in the contract customer base, despite continuous growth in data consumption.

### Sales and marketing

Brasilcel actively manages its distribution channels, which consisted of approximately 11,300 points of sale at December 31, 2008. Also, pre-pay customers have access to a wide range of “recharge” points. Credit recharges can also be made by electronic transfers through the commercial banking network. At December 31, 2008, approximately 19% of Brasilcel’s customer base were contract accesses and the remaining 81% were pre-pay accesses. Contract accesses growth was driven by customer acquisition and retention campaigns focused on high-value customers, with an emphasis on the Vivo Escolha plans.

### Competition

Vivo was the leading mobile operator in Brazil in terms of number of accesses at December 31, 2008. The growth of the Brazilian market was considerable during the past years while being accompanied by an increase in competition due to the introduction of new competitors in the regions in which Vivo operates. Vivo’s major competitors are subsidiaries of Telecom Italia, America Móvil and Oi.

Vivo’s estimated market share in terms of mobile accesses in the Brazilian mobile markets in which it operates was approximately 30% at December 31, 2008, down from approximately 36.7% at December 31, 2007. Our market share at December 31, 2007 did not include the state of Minas Gerais, which we incorporated after acquiring Telemig in 2008, and the North East region, where we began operations at the end of 2008. The incorporation of these additional concessions resulted in a reduction of our overall market share in 2008 as we build our customer base in these regions.

### Network and technology

The licenses granted to the companies integrated under the Vivo brand allow operations over the WCDMA, GSM, CDMA, CDMA 1XRTT, CDMA EVDO and TDMA systems. Vivo offers both analog and digital services in the bands of 800 MHz, 1900 MHz and 2100 MHz. In 2008 migration from the CDMA to the GSM network continued. In 2008 Vivo reached national coverage with the acquisition of 13 of a total of 15 1900 MHz licenses which were auctioned in September 2008 and, with the acquisition of the J sub-strip of the 3G licenses auction carried out by ANATEL in December 2008, Vivo should be able to improve service quality in the areas with the highest traffic on its network. At the end of 2007 Vivo reached an agreement for the purchase of Telemig in order to complete national coverage, which was closed in April 2008.

Vivo’s GSM customer base at December 31, 2008 amounted to 31.1 million accesses, 69% of its total customer base.

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## Mexico

Mexico mobile business – Telefónica Móviles México, S.A. de C.V.

## Operations

The following table presents, at the dates indicated, selected statistical data relating to our operations in Mexico.

|                         | At December 31, |          |          |
|-------------------------|-----------------|----------|----------|
|                         | 2006            | 2007     | 2008     |
|                         | (in thousands)  |          |          |
| Total mobile accesses   | 8,553.2         | 12,534.1 | 15,330.6 |
| Pre-pay accesses        | 8,017.8         | 11,833.7 | 14,432.4 |
| Fixed wireless accesses | 2.0             | 3.6      | 133.6    |
| Total accesses          | 8,553.2         | 12,537.6 | 15,464.2 |

The mobile penetration rate in Mexico was approximately 71.7% at December 31, 2008 an increase of 8.3 percentage points from December 31, 2007.

Telefónica Móviles México, S.A. de C.V.'s, or Telefónica Móviles México's, customer base increased 23.3% to 15.5 million mobile accesses at December 31, 2008 from 12.5 million accesses at December 31, 2007. Of these, 0.9 million were contract accesses. The increase was mainly the result of a 22.0% increase of pre-pay accesses in 2008 compared to 2007.

ARPU declined to €8.2 in 2008 compared to €9.3 in 2007 (a decrease of 4.3% in local currency), due to lower termination rates and usage.

## Sales and marketing

During 2008, Telefónica Latin America, through Telefónica Móviles México launched innovative products to maintain current customers and attract additional ones. In addition, Telefónica Móviles México focused on commercial activity and profitability while improving the quality of its network, which enabled the company to maintain robust customer growth during that year.

In Mexico, we use a broad range of marketing channels, including television, radio, billboards, telemarketing, direct mail and Internet advertising to market our products and services. At December 31, 2008, approximately 94.1% of our customers in Mexico were pre-pay accesses while approximately 5.9% were contract accesses.

Among business initiatives that improved Telefónica Móviles México's competitive positioning, Telefónica Móviles México launched "1-2-3 Movistar" during the 2008 Christmas season, which is a new three level, per-minute rate plan which allows clients to choose according to their level of consumption.

## Competition

Telefónica Móviles México is the second largest mobile operator in Mexico based on the number of mobile accesses, and competes with various mobile operators at the national level. Telefónica Móviles México's principal competitor is Telcel, a subsidiary of América Móvil. Other significant competitors are Nextel and Iusacell.

Telefónica Móviles México's estimated market share in the Mexican mobile market in terms of mobile accesses was approximately 19.5% at December 31, 2008, up from approximately 18.3% at December 31, 2007.

Network and technology

Telefónica Móviles México has 100% of its accesses on its GSM network.

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## Venezuela

## Venezuela mobile business – Telcel, S.A. – Telcel

## Operations

The following table presents, at the dates indicated, selected statistical data relating to our operations in Venezuela.

|                         | At December 31, |          |          |
|-------------------------|-----------------|----------|----------|
|                         | 2006            | 2007     | 2008     |
|                         | (in thousands)  |          |          |
| Total mobile accesses   | 8,826.2         | 9,434.0  | 10,584.0 |
| Pre-pay accesses        | 7,520.2         | 8,900.3  | 9,970.7  |
| Fixed wireless accesses | 836.6           | 995.9    | 1,312.8  |
| Pay TV                  | —               | —        | 8.5      |
| Total accesses          | 8,826.2         | 10,429.9 | 11,905.3 |

The mobile penetration rate in Venezuela stood at an estimated 100.2% at December 31, 2008, an increase of 13.5 percentage points from December 31, 2007.

Telefónica Latin America operates in Venezuela through Telcel, S.A., or Telcel, whose accesses increased 14.1% to 12.0 million accesses at December 31, 2008 from 10.4 million accesses at December 31, 2007. This growth was the result of net adds of over 1.5 million accesses in 2008. 66.3% of gross adds in 2008 were GSM, and GSM accesses made up over 55% of the total mobile accesses at December 31, 2008.

ARPU for 2008 was €16.9 compared to €16.3 in 2007 (an increase of 11.0% in local currency), reflecting the increased proportion of contract accesses in the customer base, customer adoption of new products and services and the continued growth in data revenues.

## Sales and marketing

In Venezuela, we use a broad range of marketing channels, including television, radio, billboards, telemarketing, direct mail and Internet advertising to market our products. At December 31, 2008, 5.8% of our mobile accesses in Venezuela were contract accesses (excluding fixed wireless accesses from the total number of mobile accesses), while approximately 94.2% were pre-pay.

In 2008 Telcel continued implementing its strategy of offering a wider range of handsets than its competitors, offering exclusive handsets, including the launch of the iPhone during the 2008 Christmas season, as well as increasing sales in fixed wireless.

## Competition

The major competitors in the Venezuela mobile business are Movilnet and Digitel. Movilnet is a mobile services communication provider owned by the public operator CANTV. Movilnet currently uses CDMA and TDMA technologies although it has started the migration process to GSM. Digitel is a mobile communications provider that uses GSM technology.

According to the Comisión Nacional de Telecomunicaciones de la República Bolivariana de Venezuela, or CONATEL, CANTV is the incumbent operator in Venezuela with a 79.0% share of the fixed market, and a 41.4% share of the mobile market (through Movilnet) as of December 31, 2008. CANTV is controlled by the government of Venezuela.

Telefónica's estimated market share in the Venezuelan mobile market, in terms of mobile accesses, was 37.8% at December 31, 2008, down from approximately 39.6% at December 31, 2007.

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## Network and technology

In Venezuela, we operate both digital and analog networks. Our digital network is based on the CDMA and GSM standard and our analog network is based on N-AMPS. At December 31, 2008, approximately 55% of accesses in Venezuela were based on the GSM network.

## Chile

The following table presents, at the dates indicated, selected statistical data relating to our operations in Chile.

|                            | At December 31, |         |          |
|----------------------------|-----------------|---------|----------|
|                            | 2006            | 2007    | 2008     |
|                            | (in thousands)  |         |          |
| Fixed telephony accesses   | 2,206.2         | 2,172.4 | 2,121.0  |
| Internet and data accesses | 557.7           | 686.8   | 743.8    |
| Narrowband accesses        | 53.3            | 31.8    | 18.7     |
| Broadband accesses         | 494.5           | 646.0   | 716.6    |
| Other accesses             | 10.0            | 8.9     | 8.6      |
| Mobile accesses            | 5,680.2         | 6,282.7 | 6,875.0  |
| Pre-pay accesses           | 4,507.6         | 4,742.2 | 4,956.0  |
| Pay TV accesses            | 94.2            | 219.9   | 263.0    |
| Final clients accesses     | 8,538.4         | 9,361.7 | 10,002.7 |
| Wholesale accesses         | 19.9            | 15.4    | 11.5     |
| Total accesses             | 8,558.3         | 9,377.2 | 10,014.3 |

At December 31, 2008 Telefónica Latin America managed a total of 10.0 million accesses in Chile, 6.8% more than at December 31, 2007, underpinned by growth in mobile accesses, which increased by 9.4% to 6.9 million accesses at December 31, 2008 from 6.3 million accesses at December 31, 2007. Growth was also driven, to a lesser extent, by a 10.9% increase in broadband accesses to 0.7 million accesses at December 31, 2008 and a 19.6% increase in pay TV accesses to 0.3 million accesses at December 31, 2008. Fixed telephony accesses decreased 2.4% to 2.1 million at December 31, 2008.

## Chilean fixed business – Telefónica Chile, S.A.

## Operations

Telefónica Latin America conducts its Chilean fixed business through Telefónica Chile S.A., or Telefónica Chile (formerly Compañía de Telecomunicaciones de Chile, or CTC Chile), the leading fixed line telecommunications operator in Chile based on number of accesses, according to information provided by its competitors and regulatory authorities. Telefónica Chile's accesses increased 1.4% from December 31, 2007 to 3.1 million accesses at December 31, 2008. Telefónica Chile's fixed telephony accesses decreased by 2.4% from December 31, 2007 to 2.1 million accesses at December 31, 2008. Broadband and pay TV accesses continued to grow in 2008, and Telefónica Chile managed 0.7 million broadband accesses at December 31, 2008, maintaining its leadership of the Chilean broadband market, in terms of accesses.

Telefónica Chile's pay TV business grew to 0.3 million accesses at December 31, 2008. Telefónica Chile established itself as the second pay TV operator in Chile, by number of accesses.



Sales and marketing

One of our main priorities in the Chilean fixed telephony business is to satisfy customer needs by improving the quality of our customer service. We continued our strategy of segmenting our customers in order to tailor our services to best meet the specific needs of each customer segment.

During 2008, Telefónica Chile and VTR, our main competitor in the broadband service market, twice increased the speed of their respective broadband networks during the year. In addition, Telefónica Chile also launched

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“Prepaid Broadband Service” while VTR launched “Naked Broadband” in Chile, aiming to target more customer segments.

The customer service model developed by Telefónica Chile, which is aimed at achieving the highest degree of efficiency in customer service, features the following:

- personal customer service lines for purchasing any type of product and service and handling customer queries;
- Telefónica stores (Tiendas Telefónica) where customers can test and buy products marketed by Telefónica;
- Telefónica’s “virtual” store, accessible by Internet, which offers customers the ability to order and purchase online the majority of services and products offered by Telefónica; and
- a sophisticated customer service system for corporate clients, ranging from a telephone help line for small and medium-sized businesses to the assignment of sales managers to address the needs of larger corporate clients.

## Competition

The competitive landscape in fixed telephony in Chile is marked by a significant fixed-to-mobile substitution effect. The increased sales of Duo and Trio bundles is the cornerstone of Telefónica Chile’s strategic focus, which aims to increase the number of revenue generating units per customer and, accordingly, revenue per customer. VTR is our principal competitor in the Chilean fixed telephony market, though Telmex has made a strong entrance into Chile as a “3-play player” like Telefónica.

Telefónica Chile’s estimated market share at December 31, 2008 was as follows:

- broadband market share amounted to approximately 49.4% of retail broadband accesses (down from approximately 50.0% at December 31, 2007);
- fixed telephony accesses market share amounted to approximately 62.1% of retail fixed telephony accesses (down from approximately 64.8% at December 31, 2007); and
- pay TV market share amounted to approximately 17% of the market by number of pay TV accesses (the same percentage as at December 31, 2007).

Chilean mobile business – Telefónica Móviles Chile, S.A.

## Operations

The mobile penetration rate in Chile stood at an estimated 96.6% at December 31, 2008, an increase of 6.6 percentage points from December 31, 2007.

Telefónica Latin America conducts its Chilean mobile business through Telefónica Móviles Chile, S.A., or Telefónica Móviles Chile, whose customer base increased 9.4% to 6.9 million accesses at December 31, 2008, making it the market leader in Chile in terms of mobile accesses. Growth in the customer base was driven by net adds to the GSM service, which accounted for 97.2% of the total customer base, 7.7 percentage points more than at December 31, 2007. The number of contract accesses rose by 24.6% to 1.9 million accesses at December 31, 2008 from 1.5 million accesses at December 31, 2007, accounting for more than 64% of net adds in 2008.

ARPU was €12.3 in 2008 compared to €12.0 in 2007 (an increase of 8.3% in local currency). The increase in local currency was driven by higher traffic and greater consumption by pre-pay customers.

#### Sales and marketing

In Chile, we use a broad range of marketing channels, including television, radio, billboards, telemarketing, direct mail and Internet advertising to market our products.

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## Competition

We currently have three primary competitors in the Chilean market for mobile telephony, each of which provides services on a nationwide basis: Entel, Claro and Nextel.

Telefónica Móviles Chile's estimated market share in the Chilean mobile sector in terms of mobile accesses was approximately 43.3% at December 31, 2008, down from approximately 44.0% at December 31, 2007.

## Network and technology

In Chile, Telefónica Móviles Chile operates with TDMA, CDMA and GSM networks. GSM customers represented 97.2% of Telefónica Móviles Chile's total customer base at December 31, 2008. In December 2007, the 3G network was launched, and Telefónica Móviles Chile had 0.1 million accesses on this network at December 31, 2008.

## Argentina

The following table presents, at the dates indicated, selected statistical data relating to our operations in Argentina.

|                            | 2006     | 2007     | At December 31,<br>2008 |
|----------------------------|----------|----------|-------------------------|
|                            |          |          | (in thousands)          |
| Fixed telephony accesses   | 4,636.3  | 4,682.5  | 4,603.1                 |
| Fixed wireless accesses    | –        | 104.3    | 22.4                    |
| Internet and data accesses | 973.7    | 1,149.9  | 1,284.3                 |
| Narrowband accesses        | 439.2    | 312.2    | 182.8                   |
| Broadband accesses         | 517.7    | 819.3    | 1,082.0                 |
| Other accesses             | 16.8     | 18.4     | 19.5                    |
| Mobile accesses            | 11,199.4 | 13,629.7 | 14,829.6                |
| Pre-pay accesses           | 7,315.8  | 8,836.0  | 9,687.6                 |
| Fixed wireless accesses    | 140.7    | –        | –                       |
| Final clients accesses     | 16,809.4 | 19,462.1 | 20,717.0                |
| Wholesale accesses         | 7.3      | 9.3      | 10.0                    |
| Total accesses             | 16,816.6 | 19,471.4 | 20,726.9                |

Telefónica Latin America managed a total of 20.7 million accesses in Argentina at December 31, 2008, an increase of 6.4% from December 31, 2007. This increase was underpinned by growth in mobile accesses, which increased by 8.8% to 14.8 million accesses at December 31, 2008 from 13.6 million accesses at December 31, 2007, and by growth in the number of broadband accesses, which increased by 32.1% to 1.1 million accesses at December 31, 2008 from 0.8 million accesses at December 31, 2007.

Argentina fixed business – Telefónica de Argentina, S.A.

## Operations

Telefónica Latin America conducts its Argentine fixed business through Telefónica de Argentina, S.A., or Telefónica de Argentina, the leading provider of fixed telephony services in Argentina in 2008 based on number of accesses, according to information provided by its competitors and regulatory authorities.

Telefónica de Argentina's accesses increased 1.0% to 5.9 million accesses at December 31, 2008 from 5.8 million accesses at December 31, 2007. This modest growth was primarily driven by a 32.1% increase in broadband accesses to 1.1 million accesses at December 31, 2008 from 0.8 million accesses at December 31, 2007. The growth in broadband accesses was accompanied by a slight decrease in fixed telephony accesses of 1.7% to 4.6 million accesses at December 31, 2008 from 4.7 million accesses at December 31, 2007.

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Total voice traffic (measured in minutes) remained almost stable during 2008 as compared to 2007 despite the sharp growth of mobile-to-fixed traffic. Local and interconnection fixed-to-fixed traffic (measured in minutes) decreased 8.0% and 3.9%, respectively, in the year ended December 31, 2008 compared to the year ended December 31, 2007. These decreases were offset by an increase in mobile-to-fixed interconnection traffic of 18.8% over the same period. Public use telephony traffic (measured in minutes) in 2008 decreased by 27.7% compared to the year ended December 31, 2007.

### Sales and marketing

In Argentina, Telefónica de Argentina uses a broad range of marketing channels, including television, radio, billboards, telemarketing, direct mail and Internet advertising to market its fixed telephony products and services. Telefónica de Argentina has continued answering customers' needs through the development of its broadband business and by providing them new value added services. Telefónica de Argentina also focused its product strategy on bundlings and packages, supported by commercial offerings like flat-rate plans (tarifa plana). In 2008, long distance flat-rate plans were launched. The flat-rate plan was primarily sold with the bundling of broadband access together with a local traffic plan. At December 31, 2008 approximately 58% of the broadband customer base subscribed to broadband through a bundled package.

### Competition

Telefónica de Argentina is the incumbent provider of fixed telephony services in the southern region of Argentina. However, other licensees currently providing fixed telephony services include Telecom Argentina, S.A., Telmex Argentina, S.A., Impsat S.A. (acquired by Global Crossing in May 2007) and Port-Hable (Hutchison Telecommunications Argentina S.A.). Claro, a mobile phone company owned by America Móvil, also competes in the fixed telephony market.

Telefónica de Argentina is using its expanded fiber-optic network in the northern region of Argentina to carry long-distance traffic and a multiservice network to provide local service in the three most important cities in the northern region of Argentina where Telecom Argentina, S.A. is the incumbent provider. Telefónica de Argentina expanded and improved its network capacity by the construction of fixed wireless networks and the activation of new lines.

Telefónica de Argentina also competes with Grupo Clarín, a company with a growing broadband and TV businesses as a result of the merger of its affiliate Cablevisión with Multicanal in 2007. In 2008, Telecentro, a small provider, without global coverage in the country, launched a triple-play offering reaching a customer base of around 40 thousand clients.

Telefónica had an estimated market share in the Argentine fixed telephony market of approximately 48.1% at December 31, 2008 based on number of fixed telephony accesses, down from approximately 48.5% at December 31, 2007.

Argentina mobile business – Telefónica Móviles Argentina, S.A.

### Operations

The Argentine mobile market continued to grow at a strong pace in 2008, with an increase in its penetration rate from 98% to 110% at December 31, 2008, based on number of mobile accesses.

Telefónica Latin America conducts its Argentine mobile business through Telefónica Móviles Argentina, S.A., or Telefónica Móviles Argentina, whose accesses increased 8.8% to 14.8 million accesses at December 31, 2008 from 13.6 million accesses at December 31, 2007. Telefónica Móviles Argentina also increased its number of contract accesses by 7.3% to 5.1 million accesses at December 31, 2008 from 4.8 million accesses at December 31, 2007. Of Telefónica Móviles Argentina's total customer base at December 31, 2008, 99.8% were on Telefónica Móviles Argentina's GSM network, which represents an increase of 13.4 percentage points from December 31, 2007.

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ARPU for 2008 was €8.7 in 2008 compared to €8.5 in 2007 (an increase of 10.5% in local currency), reflecting customer adoption of new products and services (upgrades and more consumption), tariff increases and the continued growth in data revenues.

## Sales and marketing

In Argentina, Telefónica Móviles Argentina uses a broad range of marketing channels, including television, radio, billboards, telemarketing, direct mail and Internet advertising to market its products. At December 31, 2008, approximately 34.7% of our accesses in Argentina were contract accesses.

## Competition

We currently have three competitors in the Argentine market for mobile communications services, each of which provides services on a nationwide basis: Telecom Personal, which is controlled by Telecom Italia through Telecom Argentina; Claro, controlled by América Móvil; and Nextel, owned by NII Holdings Inc.

Telefónica Móviles Argentina's estimated market share in the Argentine mobile market in terms of mobile accesses was approximately 34.0% at December 31, 2008, down from approximately 35.3% at December 31, 2007.

## Network and technology

In Argentina we operate on digital networks based upon GSM and UMTS technology. In 2008, Telefónica Móviles Argentina deactivated its analog network. At December 31, 2008, GSM accesses represented 99.8% of Telefónica Móviles Argentina's accesses.

## Colombia

The following table presents, at the dates indicated, selected statistical data related to our operations in Colombia.

|                            | 2006           | At December 31,<br>2007 | 2008     |
|----------------------------|----------------|-------------------------|----------|
|                            | (in thousands) |                         |          |
| Fixed telephony accesses   | 2,359.4        | 2,328.5                 | 2,299.2  |
| Internet and data accesses | 70.9           | 200.3                   | 395.9    |
| Narrowband accesses        | 2.9            | 0.0                     | 0.3      |
| Broadband accesses         | 68.0           | 200.3                   | 393.9    |
| Other accesses             |                |                         | 1.7      |
| Mobile accesses            | 7,759.7        | 8,372.1                 | 9,963.1  |
| Pre-pay accesses           | 5,960.5        | 6,612.9                 | 8,327.3  |
| Pay TV accesses            |                | 72.9                    | 142.3    |
| Final clients accesses     | 10,190.0       | 10,973.8                | 12,800.5 |
| Wholesale accesses         |                |                         | 2.9      |
| Total accesses             | 10,190.0       | 10,973.8                | 12,803.4 |

Telefónica Latin America managed a total of 12.8 million accesses in Colombia at December 31, 2008, an increase of 16.7% from December 31, 2007. This increase was underpinned by the sharp growth in mobile accesses, which increased 19.0% to 10.0 million accesses at December 31, 2008 from 8.4 million accesses at December 31, 2007, and by growth in the number of broadband accesses, which increased 96.7% to 0.4 million accesses at December 31, 2008



from 0.2 million accesses at December 31, 2007.

Colombian fixed business - Colombia Telecomunicaciones, S.A. ESP

Operations

Telefónica Latin America conducts its Colombian fixed telephony business through Colombia Telecomunicaciones, S.A. ESP, or Colombia Telecom, which is present in approximately 1,000 municipalities in

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Colombia. In April 2006, Telefónica Internacional, S.A., acquired 50% plus one share of Colombia Telecom for approximately €289 million pursuant to an auction process. In December, 2006 Colombia Telecom merged with Telefónica Data Colombia, S.A. As a result of the merger, Telefónica Internacional, S.A.'s stake increased to 52.03%.

Colombia Telecom reached 2.8 million accesses at December 31, 2008, which represents an increase of 9.2% from 2.6 million accesses at December 31, 2007. Of these accesses, 0.4 million accesses were broadband accesses, which represents an increase in broadband accesses of 96.7% compared to December 31, 2007. This increase in broadband accesses also helped to offset the decrease of 1.3% in fixed telephony accesses from December 31, 2007 to 2.3 million accesses at December 31, 2008.

Colombia Telecom also launched a pay TV product using satellite technology at the beginning of 2007, allowing it to begin offering Trio bundles (voice, broadband and pay TV). As of December 31, 2008, Colombia Telecom had 0.1 million pay TV accesses.

Colombia Telecom has a finance lease agreement with PARAPAT. PARAPAT is the consortium which owns the telecommunications assets and manages the pension funds for the entities which were predecessors to Colombia Telecom and regulates the operation of assets, goods and rights relating to the provision of telecommunications services by Colombia Telecom. This finance lease agreement includes the lease of the telecommunications assets and the transfer of these assets to Colombia Telecom once the last installment of the lease has been paid which, in accordance with the payment schedule, is expected to be in 2022.

### Sales and marketing

In Colombia, Colombia Telecom uses a broad range of marketing channels, including television, radio, billboards, telemarketing, direct mail and Internet advertising to market its products.

In Colombia, we are currently pursuing a strategy to increase market penetration, by offering bundled products such as "Trio Telefónica".

### Competition

Colombia Telecom's principal competitors in the Colombian market are Telmex and ETB.

Colombia Telecom had an estimated market share in the Colombian fixed telephony market of approximately 29.2% at December 31, 2008 based on number of fixed telephony accesses, down from approximately 30.6% at December 31, 2007.

Colombian mobile business – Telefónica Móviles Colombia, S.A.

### Operations

At December 31, 2008 the Colombian mobile market had 44.7 million accesses, representing an estimated mobile penetration rate of 91.1%. This penetration rate represents an increase of 15.9 percentage points from December 31, 2007.

Telefónica Latin America conducts its Colombian mobile business through Telefónica Móviles Colombia, S.A., or Telefónica Móviles Colombia, whose customer base increased by 19.0% from December 31, 2007 to 10.0 million accesses at December 31, 2008, 91.6% of which were GSM accesses. The number of GSM accesses at December 31,

2008 represents a 10.1 percentage point increase from December 31, 2007.

In 2008 Telefónica Móviles Colombia focused on its commercial restructuring and increased the breadth and depth of its distribution capabilities. Telefónica Móviles Colombia continued to expand its GSM coverage. Also, Telefónica Móviles Colombia continued to work on a commercial offering with the same rate structure regardless of call destination.

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ARPU for 2008 was €6.8 in 2008 compared to €8.8 in 2007 (a decrease of 21.6% in local currency), reflecting the decreased proportion of contract accesses in the customer base and the reduction of interconnection tariffs, which came into force as a result of change in regulation in December 2007.

## Sales and marketing

Telefónica Móviles Colombia uses a broad range of marketing channels, including television, radio, billboards, telemarketing, direct mail and Internet advertising to market its products. At December 31, 2008, approximately 16.4% of our mobile accesses in Colombia were contract accesses, while approximately 83.6% were pre-pay accesses.

Telefónica Móviles Colombia implemented, in the contract segment, commercial promotions geared toward achieving increased customer loyalty and new tariff plans focused on a single tariff to any destination with lower basic charges to attract customers.

## Competition

Telefónica Móviles Colombia currently has two primary competitors in the Colombian market for mobile communications services: Comcel, which is owned by América Móvil, and Colombia Móvil, who operates under the brand “Tigo” and is owned by Millicom.

Telefónica Móviles Colombia’s estimated market share in the Colombian mobile market in terms of mobile accesses was approximately 24.5% at December 31, 2008, down from approximately 26.0% at December 31, 2007.

## Network and technology

Telefónica Móviles Colombia operates digital networks based upon the GSM, CDMA 1XRTT and TDMA standards. At December 31, 2008, GSM accesses represented 91.6% of total accesses.

## Peru

The following table presents, at the dates indicated, selected statistical data relating to our operations in Peru.

|                            | 2006           | At December 31,<br>2007 | 2008     |
|----------------------------|----------------|-------------------------|----------|
|                            | (in thousands) |                         |          |
| Fixed telephony accesses   | 2,569.8        | 2,843.4                 | 2,986.5  |
| Fixed wireless accesses    |                | 290.0                   | 485.5    |
| Internet and data accesses | 525.5          | 623.1                   | 728.9    |
| Narrowband accesses        | 47.8           | 40.3                    | 17.7     |
| Broadband accesses         | 468.5          | 572.1                   | 698.4    |
| Other accesses             | 9.2            | 10.7                    | 12.8     |
| Mobile accesses            | 4,987.2        | 8,067.3                 | 10,612.7 |
| Pre-pay accesses           | 4,353.3        | 7,238.1                 | 9,575.2  |
| Fixed wireless accesses    | 71.3           |                         |          |
| Pay TV accesses            | 557.2          | 640.0                   | 654.5    |
| Final clients accesses     | 8,710.9        | 12,173.8                | 14,982.6 |
| Wholesale accesses         | 0.4            | 0.5                     | 0.4      |
| Total accesses             | 8,711.4        | 12,174.3                | 14,983.0 |

At December 31, 2008, Telefónica Latin America had 15.0 million accesses in Peru, which represents an increase of 23.1% from December 31, 2007. This growth in accesses was primarily driven by a 31.6% increase in mobile accesses from December 31, 2007 to 10.6 million mobile accesses at December 31, 2008, mostly in the pre-pay segment. The IRIS project, a collaboration between fixed telephony operators and mobile operators in Peru, which was launched in March 2007 with the aim of increasing fixed telephony and broadband penetration, also contributed to the overall growth in accesses.

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Peruvian fixed business – Telefónica del Perú, S.A.A.

### Operations

Telefónica Latin America conducts its Peruvian fixed telephony business through Telefónica del Perú, S.A.A., or Telefónica del Perú, which at December 31, 2008 was the leading fixed line telecommunications operator in Peru based on number of fixed telephony accesses.

Telefónica del Perú had total accesses of 4.4 million at December 31, 2008, an increase of 6.4% from December 31, 2007, due primarily to increases in fixed wireless telephony and broadband accesses. Fixed telephony accesses increased 5.0% from December 31, 2007 to 2.9 million accesses at December 31, 2008, primarily as a result of growth in fixed wireless accesses, which totaled 0.5 million accesses at December 31, 2008. Broadband accesses grew by 22.1% from December 31, 2007 to 0.7 million at December 31, 2008. In addition, pay TV accesses totaled 0.7 million accesses at December 31, 2008 recording growth of 2.3% from December 31, 2007 primarily due to increased cable pay TV subscriptions.

### Sales and marketing

Telefónica del Perú's commercial strategy is based on achieving and maintaining high levels of market penetration by offering customized services to different customer segments, with marketing campaigns focused on maintaining customer loyalty and increasing the options available to potential customers. The primary products offered by Telefónica del Perú include fixed telephony, broadband, pay TV, data and IT services.

During 2008 Telefónica del Perú launched Duo and Trio bundle promotions, which include, with a flat tariff structure, fixed telephony, broadband and pay TV.

In the long distance market, after elimination of pre-selection of Telefónica del Perú by default in 2007, Telefónica del Perú began to offer tariffs per second for its Hola Perú card and tariff reductions for long distance national public telephone-to-mobile calls. These promotions have helped offset the effect of fixed-to-mobile substitution.

The reductions achieved in average tariffs for local fixed telephony are the result of implementation of a productivity factor as mandated by the Peruvian government and the execution of agreements established with the Peruvian government. During 2007 Telefónica del Perú began implementation of an agreement reached with the Peruvian government in December 2006 to, among other things, reduce tariffs by up to 29% in basic fixed telephony plans, increase the period of validity for pre-pay fixed telephony cards to 180 days, reduce public telephony tariffs and implement per second tariff plans.

In the broadband market, Telefónica del Perú broadened its coverage in three regions: Ancash, Ica and Junín, as well as reduced "Giga ADSL" tariffs.

In pay TV, Telefónica del Perú announced the launch of Evolución Cable Mágico to increase customer value by adding more channels and improving service with certain digital offerings. Additionally, Direct TV, Telefónica del Perú's main competitor in the pay TV market, launched its pre-pay digital subscription TV which allows it to access low-income customers, while Telmex incorporated new channels to its offer.

Star Global Com was purchased by Telefónica del Perú in September 2008, adding 19 thousand accesses (13 thousand pay TV accesses and 6 thousand Internet accesses).

### Competition

In 2008, Telmex and Americatel, Telefónica del Perú's two primary competitors, focused on offering bundled products (local and long distance telephony together with broadband).

In October 2007 a pre-selection long distance service was implemented in Peru whereby customers must now dial a company code, pre-select an operator or use a pre-pay card to make a long-distance call. This has resulted in an increase of competition in this market reducing prices in general.

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Telmex implemented an aggressive strategy to enter the residential market by offering a “triple play” service. The response from Telefónica del Perú consisted of increasing Trio bundle options at lower prices.

Telefónica del Perú had an estimated market share in the Peruvian fixed telephony market of approximately 94.0% at December 31, 2008, based on number of fixed telephony accesses, down from approximately 95.9% at December 31, 2007.

Peruvian mobile business – Telefónica Móviles Perú, S.A.C.

### Operations

The pace of growth of the Peruvian mobile market accelerated in 2008, with an estimated mobile penetration rate of 60.6% at December 31, 2008, which represents an increase of 13.1 percentage points compared to December 31, 2007.

Telefónica Latin America conducts its Peruvian mobile business through Telefónica Móviles Perú, S.A.C., or Telefónica Móviles Perú, whose customer base increased 31.6% from December 31, 2007 to 10.6 million accesses at December 31, 2008. This increase was primarily driven by a 32.3% increase in the number of pre-pay accesses from December 31, 2007 to December 31, 2008. In 2008, Telefónica Móviles Perú continued the migration to GSM technology, and at December 31, 2008, GSM accesses accounted for 89.6% of its total customer base, which represents an increase of 52.3% from December 31, 2007.

ARPU for 2008 was €6.0 in 2008 compared to €7.3 in 2007 (a decrease of 16.6% in local currency), as a consequence of reductions in both contract and pre-pay tariffs.

### Sales and marketing

Telefónica Móviles Perú uses a broad range of marketing channels, including television, radio, billboards, telemarketing, direct mail and Internet advertising to market its products. At December 31, 2008, approximately 90.2% of Telefónica Móviles Perú’s mobile accesses were pre-pay accesses, while approximately 9.8% were contract accesses.

### Competition

Telefónica Móviles Perú currently has two primary competitors in the Peruvian market for mobile telephony services: Claro, owned by América Móvil, and Nextel Perú.

New mobile price tariffs were launched by both Telefónica Móviles Perú and Claro at the beginning of 2008, which consist of mobile tariffs that do not differentiate between on-net and off-net calls.

Telefónica’s estimated market share in the Peruvian mobile market in terms of mobile accesses was approximately 62.6% at December 31, 2008, up from approximately 61.2% at December 31, 2007.

### Network and technology

At December 31, 2008 Telefónica Móviles Perú operated both GSM and CDMA technology. Its digital network is based upon the CDMA/CDMA 1XRTT standard, and Telefónica Móviles Perú launched its GSM network in February 2006. At December 31, 2008, approximately 89.6% of Telefónica Móviles Perú’s customer base was GSM accesses.



Ecuador

Ecuadorian mobile business – Otecel, S.A.

Operations

The Ecuadorian mobile market experienced strong growth in 2008, with an estimated mobile penetration rate of 81% by the end of the year, which represents an increase of 11 percentage points from December 31, 2007.

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The following table presents, at the dates indicated, selected statistical data relating to our operations in Ecuador.

|                         | At December 31, |         |         |
|-------------------------|-----------------|---------|---------|
|                         | 2006            | 2007    | 2008    |
|                         | (in thousands)  |         |         |
| Total mobile accesses   | 2,490.0         | 2,581.1 | 3,122.5 |
| Pre-pay accesses        | 2,133.0         | 2,177.5 | 2,650.5 |
| Fixed wireless accesses | 1.7             | 1.3     | 89.4    |
| Total accesses          | 2,490.0         | 2,582.4 | 3,211.9 |

Telefónica Latin America conducts its Ecuadorian mobile business through Otecel, S.A., or Otecel, which had a customer base of 3.2 million accesses at December 31, 2008 an increase of 24.4% from 2.6 million accesses at December 31, 2007. Of these, 83.1% were GSM accesses, representing an increase of 13 percentage points from December 31, 2007.

ARPU for 2008 was €6.7 in 2008 compared to €6.6 in 2007 (an increase of 8.9% in local currency), as a result of higher consumption.

#### Sales and marketing

In Ecuador, Otecel uses a broad range of marketing channels, including television, radio, billboards, telemarketing, direct mail and Internet advertising to market their products. At December 31, 2008, approximately 84.9% of our mobile accesses in Ecuador were pre-pay accesses, while approximately 15.1% were contract accesses.

The number of accesses on the “movistar” and “multicolour” tariffs, which are preferential tariff plans for on-net and off-net calls, respectively, had an approximate three-fold aggregate increase to 2.7 million pre-pay accesses at December 31, 2008.

#### Competition

Otecel currently has two primary competitors in market for mobile communications services in Ecuador, Porta (América Móvil) and Alegro.

Telefónica’s estimated market share in the Ecuadorian mobile market in terms of mobile accesses was approximately 26.6% at December 31, 2008, up from approximately 26.0% at December 31, 2007.

#### Network and technology

Otecel operates both analog and digital networks. Its digital network is based upon the GSM standard and CDMA standard.

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## Central America

Telefónica Central America (which includes Panama, Guatemala, El Salvador and Nicaragua) reduced its commercial activity during 2008, compared to 2007, mainly due to the already high penetration levels reached, especially in El Salvador and Panama, implementation of a more selective commercial approach to capture higher value customers and intense competition.

At the end of 2008, the mobile penetration rate of the Central American market, where Telefónica operates, was 80.4%, which represents an increase of 11.2 percentage points from December 31, 2007.

The following table presents, at the dates indicated, selected statistical data related to our operations in Central America.

|                            | 2006           | At December 31,<br>2007 | 2008    |
|----------------------------|----------------|-------------------------|---------|
|                            | (in thousands) |                         |         |
| Fixed telephony accesses   | 320.3          | 393.4                   | 437.2   |
| Internet and data accesses | 26.0           | 22.0                    | 18.4    |
| Broadband accesses         | 24.1           | 19.8                    | 16.5    |
| Pay TV accesses            | 14.0           | —                       | —       |
| Mobile accesses            | 3,618.6        | 5,009.9                 | 5,702.0 |
| Total accesses             | 3,978.9        | 5,425.3                 | 6,157.6 |

Telefónica Central América's customer base increased by 13.5% from December 31, 2007 to 6.2 million accesses at December 31, 2008. Of this, Telefónica Central América had 0.4 million fixed telephony accesses and 0.4 million mobile contract accesses. Growth was fueled by the effectiveness of commercial campaigns carried out throughout 2008 based on new offers focused on competitive tariff plans.

ARPU for 2008 was €7.4 in 2008 compared to €9.7 in 2007 (a decrease of 17.7% on a constant euro basis), down sharply on a constant euro basis due to a decrease in usage and a lower proportion of contract accesses in the customer base.

## Atento - Call Center Business

Atento offers integrated telephone assistance services as well as sophisticated customer relationship management services, such as the development and implementation of customer loyalty programs, telemarketing services and market research. In addition, Atento rents call centers and provides staff for such centers to third parties. Atento has sought to diversify its client base and serves companies in the financial, consumer and energy sectors, as well as public institutions. At December 31, 2008, Atento operated more than 95 call centers and had 132,121 call center personnel in 16 countries on three continents, including Europe (Spain and Czech Republic), America (Latin America) and Africa (Morocco).

## Strategic Partnerships

## China Unicom

In June 2005, Telefónica Internacional, S.A.U., or Telefónica Internacional, acquired through open market purchases 2.99% of the outstanding shares of CNC, a Chinese telecommunications company, for an equivalent of approximately €240 million. In September 2005, Telefónica Internacional increased its stake in CNC to 5.0% of its outstanding shares

through open market purchases for a total equivalent of approximately €424 million.

Subsequently, both companies entered into a strategic alliance agreement on November 14, 2005 and a supplemental agreement on November 12, 2006.

In January 2008, we agreed to acquire an additional stake of approximately 2.22% in CNC through our subsidiary Telefónica Internacional, which closed on September 22, 2008, for an approximate purchase price of €313 million.

In addition, in September 2008, Telefónica Internacional agreed to acquire an additional stake of approximately 5.74% of CNC's share capital. This acquisition was structured in two stages. In the first stage of the acquisition, carried out in September 2008, Telefónica Internacional acquired shares representing 2.71% of CNC for approximately €374 million. Subsequently, on October 14, 2008 the merger between CNC and CU was carried out at an exchange ratio of 1,508 shares of the new company for each share of the former company. After this merger, the second stage of the acquisition was carried out, which consisted of our acquisition of additional shares issued by the new company for an approximate purchase price of €413 million.

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After these acquisitions and the merger between CNC and CU, our stake in CU at December 31, 2008 stood at approximately 5.38%.

## Portugal Telecom

At December 31, 2007, we held an 8.32% effective interest in Portugal Telecom (or 9.16% if shares held by Portugal Telecom in treasury are not counted as outstanding), our joint venture partner in Brazil.

In December 2008, Portugal Telecom bought back and cancelled 46,082,677 shares in line with its share buyback program. This raised our direct and indirect ownership interest to 10.48%. In accordance with Portuguese securities regulation, which require us to dispose of any shares which bring our ownership stake over 10%, we sold 4,264,394 shares of Portugal Telecom, thereby lowering our stake to 10%. We account for our interest in Portugal Telecom pursuant to the equity method.

Within the framework of our business cooperation with Portugal Telecom, we provide mobile services in Morocco (through Medi Telecom, S.A., in which we hold a 32.18% interest and share management responsibilities with Portugal Telecom) and Brazil (through Brasilcel, in which we hold a 50% interest and share management responsibilities with Portugal Telecom, under the brand name “Vivo”).

For more information on these joint ventures, please see “—Telefónica Latin America—Brazil—Brazil mobile business” above and “—Medi Telecom” below.

## Medi Telecom

Telefónica Spain provides mobile services in Morocco through Medi Telecom, S.A., or Medi Telecom, in which Telefónica Móviles España holds a 32.18% interest and shares management responsibilities with Portugal Telecom, as described above. Medi Telecom is one of three mobile operators in Morocco, with over 6.5 million accesses at December 31, 2008.

Medi Telecom commenced offering mobile services in Morocco in March 2000, eight months after it was awarded a GSM license covering the Moroccan national territory. In 2005, Medi Telecom obtained a fixed telephony license and the company is currently constructing a fixed network using WiMax technology.

Telefónica Móviles España has entered into a shareholders’ agreement with other shareholders of Medi Telecom under which it has the right to appoint the chief executive officer of Medi Telecom and sales of shares in Medi Telecom are subject to a right of first refusal by the other shareholders in Medi Telecom.

The following table presents selected financial data relating to Medi Telecom based on our percentage ownership.

| As of             | % Holding | Millions of euros |                      |                     |                        |    | Carrying amount | Fair value |
|-------------------|-----------|-------------------|----------------------|---------------------|------------------------|----|-----------------|------------|
|                   |           | Total assets(1)   | Total liabilities(1) | Current revenues(1) | Profit for the year(1) |    |                 |            |
| December 31, 2008 | 32.18%    | 1,217             | 951                  | 464                 | 30                     | 95 | N/A             |            |
| December 31, 2007 | 32.18%    | 1,275             | 1,023                | 447                 | 24                     | 91 | N/A             |            |

(1) Based on our proportionate interest.

Telecom Italia

Through a series of transactions throughout 2007 and 2008, we acquired an indirect holding of 10.4% in the voting shares of Telecom Italia (7.1% of the dividend rights). The Telecom Italia group is principally engaged in the

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communications sector and, particularly, in telephone and data services on fixed lines for final and wholesale customers, in the development of fiber optic networks for wholesale customers in the provision of broadband services and Internet services, in domestic and international mobile telecommunications (especially in Brazil), in the television sector using both analog and digital terrestrial technology and in the office products sector. Telecom Italia operates primarily in Europe, the Mediterranean basin and in South America. For more information, please see “Item 5. Operating and Financial Review and Prospects—Operating Results—Significant Transactions Affecting the Comparability of our Results of Operations in the Period Under Review” and “Item 10. Additional Information—Material Contracts”. Telco, through which we hold our stake in Telecom Italia, is included in our consolidated financial statements using the equity method.

## Regulation

As a telecommunications operator, we are subject to sector-specific telecommunications regulations, general competition law and a variety of other regulations. The extent to which telecommunications regulations apply to us depends largely on the nature of our activities in a particular country, with traditional fixed telephony services usually subject to more extensive regulations, which can have a direct and material effect on our business areas, particularly in countries that favor regulatory intervention.

To operate our networks, we must obtain general authorizations, concessions or licenses from national regulatory authorities, or NRAs, in those countries in which we operate. Licensing procedures also apply to our mobile operations with respect to radio frequencies. The duration of any particular license or spectrum right depends on the legal framework in the relevant country.

## Electronic Communication Regulation in the EU

The EU legal framework for electronic communications services has been developed with the aim of reinforcing the liberalization of the market and improving the functioning of the EU internal market for telecommunications networks and services, which culminated in the adoption of the 2002 EU regulatory framework for electronic communications sector (the “EU Framework”). Such regulatory framework primarily consists of Directive 2002/21/EC of the European Parliament and of the Council of 7 March 2002 on a common regulatory framework for electronic communications networks and service (“Framework Directive”) and of four specific Directives: Directive 2002/20/EC of the European Parliament and of the Council of 7 March 2002 on the authorization of electronic communications networks and services (“Authorization Directive”), Directive 2002/19/EC of the European Parliament and of the Council of 7 March 2002 on access to, and interconnection of, electronic communications networks and associated facilities (“Access Directive”), Directive 2002/22/EC of the European Parliament and of the Council of 7 March 2002 on universal service and users’ rights relating to electronic communications networks and services (“Universal Service Directive”) and Directive 97/66/EC of the European Parliament and of the Council of 15 December 1997 concerning the processing of personal data and the protection of privacy in the telecommunications sector (“Data Protection Directive”). These Directives set forth the main principles and procedures that NRAs should follow with respect to regulation for the provision of electronic communications services. The EU Framework establishes an authorization regime containing measures to ensure the universal provision of basic services to consumers and sets out the terms on which providers may access each other’s networks and services.

The e-Privacy Directive (2002/58/EC) (the “e-Privacy Directive”) complements and supplements the general Data Protection Directive in the area of electronic communications. It provides for basic obligations to ensure the security and confidentiality of communications over EU electronic communications networks and gives consumers a set of tools to protect their privacy and personal data.

In 2006, the European Union established a new regulation regarding data retention of electronic communications data in order to ensure that electronic communication data are available for the purpose of the investigation, detection and prosecution of serious crimes. These data retention rules set minimum standards for the type of data to be retained and the retention period. The initial impact of this new regulation is estimated to be significant, although it will depend on the requirements established at the national level and the extent to which operators will be compensated for the costs associated with its implementation. For further information regarding



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the matters discussed above and other aspects of the regulatory risks derived from the new regulation, see “Item 3. Key Information—Risk Factors—Risks related to our business”.

Notably, the EU Framework also harmonizes the rules for deciding when regulation may be imposed on electronic communications providers. In particular, it provides that electronic communications providers can generally only be subject to specific regulation in markets in which they have “significant market power”, or SMP. The concept of SMP, for these purposes, has been aligned to the competition law concept of dominance, which essentially means a market position which allows a company to act independently of customers, suppliers and competitors.

Accordingly, the European Commission has identified in a Recommendation a list of relevant markets whose conditions may justify the application of ex ante specific regulation. The Recommendation was published on February 2003 and it has been modified by another Recommendation published in December 2007, which reduces the relevant markets from 18 to 7. In order to determine whether a company has SMP in any of the markets identified in the Recommendations, NRAs must conduct a market analysis for the relevant market. When an NRA determines a company has SMP in a relevant market, that NRA must impose at least one obligation relating to price control, transparency, non-discrimination, accounting separation or access obligations.

Regulation with respect to roaming tariffs in the EU entered into force on June 30, 2007. The regulation introduces a maximum level for the charges that operators may levy at wholesale level as well as maximum retail ceilings (referred to “Eurotariff”) for making and receiving calls while roaming in the EU. The regulation is set to expire in 2010. This regulation could be extended beyond that date if this market is not deemed to be effectively competitive.

A wholesale tariff price cap has been set at €0.28 per minute (excluding VAT) from August 30, 2008. This will then decrease to €0.26 per minute (excluding VAT) from August 30, 2009. The price caps for retail tariffs (excluding VAT) were initially set at €0.49 per minute for making a call and €0.24 per minute for receiving a call while roaming in the EU. These caps were subsequently reduced to €0.46 per minute for making a call and €0.22 per minute for receiving a call from August 30, 2008 until August 30, 2009. These price caps will be further reduced in September 2009 to €0.43 per minute and €0.19 per minute, respectively.

Currently, the roaming regulation only applies to voice calls within the EU regardless of whether such calls are pre-paid or pursuant to a contract. It does not apply to other mobile phone services, such as SMS, MMS or data transfers. However, the European Commission has adopted a proposal to reduce prices for SMS services by proposing an €0.11 price cap on roaming text messages (excluding VAT) and has proposed to regulate wholesale data roaming tariffs with a price cap of €1 per megabyte. Pursuant to these proposals, on April 24, 2009, the European Parliament adopted changes to the existing roaming regulation for voice calls to extend its applicability for an additional two years and to expand its scope to include regulation of SMS and data roaming prices. Most of the new rules will apply beginning in the summer of 2009 with some of the transparency measures coming into effect in spring of 2010.

Last revised in 2002, the EU Framework is currently under review, to take account of developments in electronic communications. Hence, on November 13, 2007, the European Commission approved the Proposals for a Regulatory Framework for Electronic Communications, amending the Framework Directive, the Access Directive, the Authorization Directive, the Universal Service Directive, the e-Privacy Directive and Regulation (EC) No 2006/2004 on consumer protection cooperation. The European Commission also approved a proposal establishing the European Electronic Communications Market Authority. The approval of these proposals is foreseen at some point in 2009 or 2010.

In addition, the European Commission approved the Proposal for amending Council Directive 87/372/EEC on the frequency band 900 MHz in order to allow the use of such band by systems capable of providing electronic

communication services not limited to GSM.

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### EU Competition Law

The EU's competition rules have the force of law in EU Member States and are, therefore, applicable to our operations in EU Member States.

The EC Treaty prohibits "concerted practices" and all agreements for undertakings that may affect trade between Member States and which restrict, or are intended to restrict, competition within the EU. It also prohibits any abuse of a dominant competitive position within the common market of the EU, or any substantial part of it, that may affect trade between Member States.

The EU Merger Regulation requires that all mergers, acquisitions and joint ventures involving participants meeting certain turnover thresholds be submitted to the EU Commission for review, rather than to the national competition authorities. Under the amended EU Merger Regulation, market concentrations will be prohibited if they significantly impede effective competition in the EU common market. European Commission and the EU Competition Commissioner are granted the authority to apply the European Competition framework.

Similar competition rules are set forth in each EU Member State's legislation and are enforced by each of their national competition authorities, or NCAs. All European countries where we have activities and referred to below are Member States of the EU.

### Telefónica Spain

#### Spain

##### General regulatory framework

The legal framework for the regulation of the telecommunications sector in Spain is principally governed by the General Telecommunications Law (32/2003) and several Royal Decrees.

The General Telecommunications Law, among other things, sets forth rules regarding the new system of notification for electronic communications services, establishes the terms by which operators interconnect their networks, defines the universal service provision regime and subjects providers with SMP in particular telecommunications markets to specific obligations.

##### Regulatory supervision

The Telecommunications Market Commission, or the CMT, is the NRA responsible for regulating the telecommunications and audiovisual service markets in Spain. The CMT supervises the specific obligations imposed on operators in the telecommunications market, and it has the requisite power to enforce its decisions whenever necessary.

The Framework Directive requires that NRAs have the power to issue binding decisions to resolve disputes arising in connection with obligations imposed under the regulatory framework.

The Spanish regulatory framework explicitly acknowledges the right for third parties who are affected by a Spanish NRA decision to challenge this decision before the appeal body.

Licenses and concessions

Pursuant to the EU Framework, parties intending to operate a telecommunications network or engage in the provision of electronic communication services must notify the CMT prior to commencing such activity. The CMT will register the telecommunications operator in the Public Operator Registry. Every three years, operators must notify the CMT of their intention to continue offering electronic communications services or operating telecommunications networks.

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Concessions to use spectrum are awarded on a non-discriminatory basis by way of a competitive procedure. Telefónica Móviles España is entitled to provide mobile services on several spectrum bands. Our main concessions are:

| Technology | Duration | Ending Date      | Extension Period |
|------------|----------|------------------|------------------|
| GSM 900    | 15 years | February 3, 2010 | 5 years          |
| E-GSM 900  | 15 years | June 6, 2020     | 5 years          |
| DCS-1800   | 25 years | July 24, 2023    | 5 years          |
| UMTS       | 20 years | April 18, 2020   | 10 years         |

## Market analysis

In accordance with the EU Framework, the Spanish NRA should identify those markets which lack effective competition, in which case it would impose specific obligations upon operators with SMP. During 2008, the CMT conducted a second round of market analyses to determine which operators have SMP in which markets.

## Fixed markets

Retail access to the public telephone network at a fixed location market; Retail market for calls at a fixed location and Retail lease lines market

In March 2006, and following a market analysis, the CMT concluded that Telefónica de España is an operator with SMP in the provision of retail access to the public telephone network service at a fixed location. As an SMP operator, Telefónica de España has certain specific obligations and is subject to certain restrictions, the most relevant of which are maximum price caps for installation and monthly fees. Telefónica de España also has obligations regarding carrier selection, cost accounting and accounting separation.

With respect to the retail market for calls at a fixed location market, on December 12, 2008, the CMT has determined that this market is competitive and, thus, it has resolved to withdraw all obligations imposed on Telefónica de España with respect to such market.

In 2006, the CMT identified Telefónica de España as an operator with SMP in the retail lease lines market, and imposed, among other obligations, the duty to provide access to a minimum set of lease lines under price controls.

## Wholesale fixed call origination market

On March 22, 2007, the CMT adopted new regulations concerning call origination on the wholesale fixed call origination market, introducing additional obligations for Telefónica de España to provide wholesale access to its fixed network to other operators, allowing competitors to use its networks to provide access services and other associated services to their customers.

In December 2008, the CMT concluded that Telefónica de España is an operator with SMP in this market and it has requested that Telefónica de España offer wholesale service to assist other operators in offering IP telephony services and provide transparent information of migration to Next Generation Networks, or NGN, centrals, which implies the provision of broad information to competitors about network evolution.

## Fixed call termination market on individual networks

As an operator with SMP in fixed call termination market on individual networks, Telefónica de España is required to submit an “Interconnection Reference Offer (OIR)” outlining the terms and conditions under which it will interconnect with other operators.

In December 2008, the CMT concluded that Telefónica de España is an operator with SMP in this market. The CMT maintained its obligations for Telefónica de España to submit an Interconnection Reference Offer (OIR). The CMT also added the obligation that Telefónica de España provide transparent information with respect to migration to NGN centrals, which implies the provision of broad information to competitors about network evolution.

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### Mobile market

#### Mobile voice call termination

In September 2006, the CMT established a progressive reduction schedule for mobile termination rates (the “glide path”) from October 2006 to September 2009.

In December 2008, Telefónica Móviles España was again identified by the CMT as an operator with SMP in mobile voice call termination on individual mobile networks, and therefore continues to be subject to the obligations already imposed on it by the CMT and as well as the additional obligation to charge for seconds of usage according to a single termination price established by the CMT. Before July 30, 2009, it is expected that the CMT will establish a new glide path for mobile voice call termination rates with a single price that includes a glide path for the fourth largest operator in the Spanish market with the objective of price convergence with the other operators in the market.

#### Mobile voice call origination

MVNOs are mobile operators that are not entitled to use spectrum for the provision of mobile services. Consequently, they must reach an access agreement with a mobile network operator in order to provide mobile access to their customers.

On February 2, 2006, the CMT established that mobile network operators collectively hold a dominant position in the mobile access and voice call origination market. Mobile operators are, therefore, obliged to negotiate reasonable access to their network upon request from an MVNO, charging reasonable prices for access services provided. MVNOs and mobile operators negotiate an access agreement on a commercial basis. If parties are unable to reach an agreement independently, the CMT may intervene to resolve the dispute.

#### Wholesale (physical) network infrastructures access

In January 2009, the CMT concluded that Telefónica de España is an operator with SMP in the wholesale (physical) network infrastructures access market, and imposed the following obligations on Telefónica de España: access to full and shared unbundled access to copper loops, sub-loops and ducts, cost oriented tariffs and accounting separation, transparency and non-discrimination obligations including an “Unbundling Reference Offer” and a “Ducts Reference Offer”. In February 2008, the CMT imposed similar obligations with respect to vertical access to buildings.

#### Wholesale broadband access

In January 2009, the CMT identified Telefónica de España as an operator with SMP in the wholesale broadband access market, and consequently the CMT has imposed on Telefónica de España the obligation to provide wholesale broadband access service until 30 Mbps to other operators in copper and fiber infrastructure. The CMT also obliges Telefónica de España to publish a wholesale broadband access reference offer, provide cost-oriented tariffs and accounting separation, non-discrimination in network access and to communicate broadband retail changes in services prior to offering them in the market.

#### Universal service obligations

The General Telecommunications Law outlines provisions to ensure that certain basic telecommunications services are guaranteed to all Spanish citizens.

Universal service is defined, under the law, as a set of communication services guaranteed to all end users, irrespective of their geographic location, of a determined quality and at an affordable price. Universal service ensures that all citizens receive a connection to the fixed line public network and network services, a telephone directory service, a sufficient number of public telephones and functional Internet access. Additional provisions are included under the scope of universal service obligation, or USO, in order to ensure that users with disabilities and special social needs, including those with low incomes, have access to the services enjoyed by the majority of users.



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In December 2008, following applications by three operators, Telefonica de España was awarded a tender for the provision of directory enquiry services for a period of three years and it has also been designated for the provision of the remaining universal service elements for a period of two years by virtue of Order ITC/3808/2008.

To finance the USO, the General Telecommunications Law stipulates that the CMT must determine whether the net cost to provide universal service implies an unfair burden for the operators. On September 2008, the CMT published a resolution which established net cost of USO for the years 2003, 2004 and 2005, the obligation of operators to contribute to USO funding and the amount of contributions these operators must make.

### Protection of consumers

On December 29, 2006, Law 44/2006 regarding the protection of consumers and users was approved. Under this law, users may only be charged for services actually used. Consequently, operators can only charge for the exact seconds of usage. A draft law of User's Rights has been adopted and is basically the compendium of the current Spanish users rights framework derived from: General Telecommunications Law 32/2003 (LGT), Royal Decree 424/2005 of April 15, 2005 (RSU) and Order ITC/912/2006 (Quality Order).

### Service quality

On March 29, 2006, a regulation was approved which established certain quality of service, or QoS, obligations for electronic communications service providers such as including service level agreements, or SLAs, commitments in electronic communication retail contracts. This regulation also requires operators to provide adequate information to customers in relation to service quality levels and detailed billing disclosure to customers. Additionally, a standardized process for billing customers has been implemented under this regulation.

### Data retention for law enforcement purposes

The 2006 Directive 2006/24/EC of the European Parliament and of the Council on the retention of data generated or processed in connection with the provision of publicly available electronic communications services or of public communications networks ("Data Retention Directive") was incorporated into Spanish legislation on November 9, 2007. Electronic communications operators are obliged to ensure the retention of data on electronic communications for a period of twelve months.

Additionally, Spain has implemented a register of pre-pay mobile customers in conjunction with these requirements. Existing prepaid customers have a period of two years for the registration since the law entered into force and the new clients must be registered immediately.

### Telefónica Europe

#### United Kingdom

The EU Regulatory Framework was implemented in the United Kingdom by the Communications Act in 2003. Under this act, responsibility for the regulation of electronic communications networks and services rests with the Office of Communications, or Ofcom.

#### Licenses and concessions

Telefónica O2 UK has provided GSM services since July 1994. Its GSM license is of indefinite duration (GSM900: 2x17.4MHz and GSM1800: 2x5.8MHz). In April 2000 Telefónica O2 UK was awarded a UMTS license, which

expires on December 31, 2021 (2 x 10MHz + 5MHz).

The license can be surrendered by the operator at any time. However, Ofcom can only revoke the license if the licensee does not pay its fees, there has been a breach of the license or for reasons related to the management of the radio spectrum, provided that in such case the power to revoke may only be exercised after one year's notice is given in writing and after Ofcom has considered any pertinent factors. The UK Government may also revoke the license for national security reasons or in order to comply with the United Kingdom's EU or other international obligations.

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In January 2009, the UK Government published the “Digital Britain” interim report, in which it proposed that UMTS licenses which currently expire in 2021 could be converted to indefinite licenses, subject to a yearly fee to be charged beyond the end of the current term.

The Digital Britain interim report also set out the UK Government’s views on the liberalization of the 900MHz and 1800MHz bands for UMTS in light of the imbalance in spectrum holdings between the different UK mobile operators. The UK Government invited mobile operators to agree a set of radio spectrum trades in order to address this issue by the end of April 2009. If no agreement is reached, however, the Government has said that it will support an imposed solution.

In February 2009 Ofcom published a consultation document setting out Ofcom’s proposals for an imposed solution if the industry fails to reach an agreement by the end of April 2009. Ofcom’s proposals would require Vodafone and Telefónica Europe to release some of the 900MHz spectrum which they currently hold (2x2.5MHz each, 10MHz in total) to allow a third operator to have access.

### Future spectrum

On April 4, 2008 Ofcom announced a decision to award spectrum in the 2.6GHz and 2010MHz bands and indicated that it expected to auction this spectrum in July 2008. T-Mobile and Telefónica O2 UK brought legal challenges against Ofcom’s decision to proceed with the auction, which challenges are still ongoing. As a result of the legal proceedings, the auction is currently on hold.

### Market reviews

On March 27, 2007, Ofcom published the charge controls to which mobile operators are subject for the provision of mobile call termination services from April 1, 2007 until March 31, 2011. The charge control requires that Telefónica O2 UK’s average termination charges should be reduced to 5.1 pence per minute (at 2006-2007 prices) by the final year of the charge control period, and that the reduction should be implemented in four equal steps across the four years. Ofcom’s decision imposing the price controls was appealed by British Telecommunications plc and Hutchison 3G UK Limited and, pursuant to those appeals, the level of the price cap is currently being investigated by the UK Competition Commission, or the CC. In January 2009 the CC issued its final determination in which established that the reductions set by Ofcom were not sufficient. As a result, it concluded that Telefónica O2 UK’s average termination charges should be reduced to 4.0 pence per minute (at 2006-2007 prices) by the final year of the charge control period. Unless the CC’s conclusions are set aside by the court, a new price control will therefore be imposed in line with the determination of the CC.

### Germany

The EU Regulatory Framework was implemented in Germany at the end of June 2004 by the Telecommunications Act. Responsibility for regulation of electronic communications networks and services rests with the telecommunications regulator, Bundesnetzagentur, or BNetzA.

### Licenses and concessions

Telefónica O2 Germany was awarded a GSM license for 1800MHz spectrum in October 1998, and in February 2007 Telefónica O2 Germany was awarded 900MHz GSM spectrum for GSM use. Accordingly, Telefónica O2 Germany is now licensed to use GSM900 2x5MHz and GSM1800: 2x17.4MHz. The GSM license expires on December 31, 2016.

Under Section 58 VIII TKG (the German Telecommunications Act) frequency assignments are limited in time, although a renewal or extension of the term is possible. The federal network agency has not yet decided on the conditions for renewing the frequency assignments. However, before expiration, we expect there to be a public hearing, and for BNetzA to set out its approach to renewal, including the terms on which the licenses will be extended (pricing, technology neutrality, etc.).

In August 2000 Telefónica O2 Germany was awarded a UMTS license, which expires on December 31, 2020 (2x9.9MHz).

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### Market reviews

In August 2006, BNetzA completed its review of voice call termination on individual mobile networks and concluded that, as an operator with SMP, the charges Telefónica O2 Germany made to other operators for terminating calls on Telefónica O2 Germany network had to be reduced, requiring Telefónica O2 Germany to lower its call termination charges from €1.24 per minute to €0.994 per minute. In 2007, Telefónica O2 Germany was required to reduce further its termination charges from €0.994 per minute to €0.880 per minute. Telefónica O2 Germany has brought legal challenges of BNetzA's 2006 and 2007 decision that Telefónica O2 Germany has SMP and against the imposition of regulatory remedies. The Federal Administrative Court, as highest level of appeal, confirmed all regulatory remedies meaning that the price controls stay in force for all mobile operators. All four German mobile operators filed a Constitutional Complaint in order to challenge the decision regarding SMP. All other actions (regarding the amount of MTRs) are pending. The new market analysis of BNetzA in 2008 again concluded that all MNOs have SMP and the decision on remedies does not contain changes in comparison to 2006. This 2008 decision has also been challenged by Telefónica O2 Germany.

In March 31, 2009 and as of April 1, 2009, BNetzA approved MTR for Telefónica O2 Germany at (0.714 per minute for a period of 20 months (until November 30, 2010)).

### Spectrum

In February 2006, BNetzA decided to allocate 900MHz GSM spectrum to Telefónica O2 Germany. This decision was challenged in the courts by German Railways Deutsche Bahn AG, and in the first instance the court refused the claim. The applications for appeal of all parties involved have been granted by the relevant court.

At the end of 2007 BNetzA began a spectrum sale in the IMT2000/UMTS extension bands. BNetzA has indicated that it will auction mobile spectrum at 2.6 GHz (70 MHz FDD / 50 MHz TDD ) together with available spectrum at 2.1 GHz (19,8 MHz FDD/19,2 MHz TDD) and 1.8 GHz (10 MHz FDD). Due to technology neutrality, non-UMTS MNOs (e.g. WiMax) and due to three spectrum bands, additional new UMTS-entrants will be attracted. For existing UMTS-MNOs there shall be no preferred spectrum award (following existing UMTS-license). The licenses will last until December 31, 2025 and require 25% and 50% pop-coverage to be offered (by 2013 and 2015 respectively). BNetzA has published a decision that the allocation will take place by way of an auction procedure. However, it is not yet clear how and when this will take place, most likely in 2010.

### Czech Republic

The EU Regulatory Framework was implemented in the Czech Republic in 2005 by the Electronic Communications Act. Responsibility for regulation of electronic communications networks and services rests with the Czech Telecommunication Office, or CTO. Governmental responsibility for the area of electronic communications lies with the Ministry of Industry and Trade.

Several changes occurred in the legal environment of the electronic communications market in the Czech Republic in 2007. Act No. 127/2005 Coll. on electronic communications and on amendment of related laws was amended in respect of provisioning special price plans to the disabled as part of universal service and radio and television broadcasting. Furthermore, an amendment to the act on radio and television broadcasting was passed, primarily to unblock the transition to terrestrial digital broadcasting.

### Licenses and concessions

Telefónica O2 Czech Republic performs communication activities under the Electronic Communications Act based on a notification to and a certificate from the CTO number 516 as amended by later changes numbers 616/1, 516/2 and 516/3.

Mobile segment

Telefónica O2 Czech Republic provides mobile electronic communications services in the 900 and 1800 MHz frequency bands under the GSM standard on the basis of radio frequency assignment from CTO valid until February 7, 2016; in the 2100 MHz frequency band under the UMTS standard on the basis of radio frequency assignment

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from CTO valid until January 1, 2022; and in the 450 MHz frequency band using CDMA2000 (Code Division Multiple Access, or CDMA) technology.

### Market reviews

In accordance with the market analyses performed by the CTO, Telefónica O2 Czech Republic was designated an SMP entity in 12 Czech markets, both retail and wholesale. The CTO started a second round of market analysis in 2007, the results of which are still pending.

### Prices and tariffs

In April 2006, price regulations for access at a fixed point to the telephone network and for calls in the fixed network were abolished. Subsequent analyses of the relevant markets showed that no further price regulation was necessary. Additionally, provision of access at a fixed location was taken out of the scope of universal service in 2006.

### Slovakia

Telefónica O2 Slovakia performs electronic communication activities under Act No. 610/2003 Coll., the Electronic Communications Act, (as amended) and General Authorization (as amended) issued by the Slovak NRA (the Telecommunications Office of Slovakia) based on a notification, as well as a number of allocation certificates issued by the NRA.

Responsibility for regulation of electronic communications networks and services rests with the Telecommunication Office of Slovakia. Governmental responsibility for the area of electronic communications lies with the Ministry of Transport, Post and Telecommunications of Slovakia.

### Licenses and concessions

On September 7, 2006, Telefónica O2 Slovakia was granted a license to provide electronic communications services by the means of the public electronic communications network using the GSM and UMTS mobile telephone network standards within Slovakia. The license has been granted for 20 years and expires in September 2026. The commercial operations were launched on February 2, 2009.

### Market analysis

In accordance with the market analyses performed by the NRA, Telefónica O2 Slovakia is proposed to be an SMP entity in the wholesale mobile termination market. Price regulation is expected to be imposed upon Telefónica O2 Slovakia during the second half of 2009.

### Ireland

In Ireland responsibility for the regulation of electronic communications networks and services rests with the Commission for Communications Regulation, or ComReg. The main legislation under which Telefónica O2 Ireland operates includes: the Wireless Telegraphy Act 1926, as amended, (45 of 1926), Post and Telecommunications Services Act 1983 as amended, (24 of 1983), Communications Regulation Acts 2002 (20 of 2002) and 2007 (22 of 2007), 3G Mobile Telephony Licensing Regulations (340 of 2003) and GSM Mobile Telephony Licensing Regulations (339 of 2003).

Licenses and concessions

Telefónica O2 Ireland has provided GSM services since March 1997 after having been awarded a license in May 1996. Its GSM900 license has a duration of 15 years (GSM900: 2x7.2MHz) from 1996. In 2000 it was awarded an additional GSM1800 license (2x14.4MHz), which also has a term of 15 years. In October 2002 Telefónica O2 Ireland was granted a UMTS license, which has duration of 20 years (2 x 15MHz + 5MHz).



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The license can be surrendered by the operator at any time. However, ComReg can only revoke the license before its expiration date if the licensee does not pay its fees or if there has been a substantial breach of the terms of the license.

The Minister for Communications, Energy and Natural Resources may also revoke the license for national security reasons, or in order to comply with EU or other international obligations.

### Future mobile spectrum

In March 2008, ComReg published a draft strategy document for spectrum management during the period from 2008 through 2010. In July 2008, ComReg published a consultation proposing to auction spectrum in the 900MHz band. A second consultation is expected to be issued in the first quarter of 2009, and an auction is currently expected to take place in the first quarter of 2010.

### Market reviews

Telefónica O2 Ireland has been found to have SMP in the market for mobile termination. ComReg has previously decided to forebear from the imposition of regulated pricing so long as it could reach agreement with the main operators for a “glide path” for annual reductions in mobile termination rates. The current glide path has resulted in Irish mobile termination rates being, on average, above the EU average, and discussions are currently in progress that will accelerate the reduction. If agreement is not reached, ComReg will build a model and impose cost-based pricing.

### Telefónica Latin America

#### Brazil

#### Regulatory framework

The delivery of telecommunications services in Brazil is subject to regulation under the regulatory framework provided in the General Telecommunications Law enacted in July 1997.

The National Agency for Telecommunications, ANATEL, is the principal regulatory authority for the Brazilian telecommunications sector.

#### Licenses and concessions

Concessions are granted for services provided in the public regime and authorizations are granted for services provided in the private regime. The only service provided in both regimes is the switched fixed telephone service, or STFC. All other services are provided only in the private regime.

The main differences between the public regime and the private regime relate to the obligations imposed on the companies. The concessionaires in the public regime, such as Telesp, have network expansion obligations (universal services obligations) and continuity of service obligations. These obligations are not imposed on the companies which provide services in the private regime.

In the state of São Paulo, Telesp provides local and long distance STFC under the public regime. In the other Brazilian states, Telesp provides local and long distance STFC under the private regime and broadband services under the private regime.

Telesp's concession agreements (local and long distance) were extended in December 2005 for an additional period of 20 years. These agreements contemplate possible revisions in their terms by ANATEL in 2010, 2015 and 2020. Telesp's terms of authorization (local and long distance) were granted for an unlimited period of time.

Under the renewed concession agreements and during the 20-year renewal period, Telesp will be required to pay a biannual fee equal to 2% of its annual net revenue (excluding taxes and social contributions), for the provision of fixed-line public telecommunications services in its concession area (State of São Paulo) for the prior year.

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Brazilian telecommunications regulations require ANATEL to authorize private regime companies to provide local, national, and international long distance STFC.

On November 20, 2008, the Presidential Decree 6,654 altered the General Concessions' Plan, enabling one economic group to hold two of the four existing area concessions for providing STFC services. Thus, the Decree increased the flexibility of telecommunications provider groups as STFC concessionaries by allowing such providers to provide services in up to two General Plan regions. Prior to the Decree telecommunications provider groups could offer STFC services in only one region.

Telesp also has an authorization to provide data and broadband services in the private regime in the State of São Paulo.

On December 4, 2002, ANATEL authorized the migration from the cellular mobile service, or SMC, regime to a new licensing regime, personal mobile service. Brasilcel's operators replaced all their old licensing titles granted under the old SMC regime with new personal mobile service authorization titles. The new personal mobile service licenses include the right to provide mobile services for an unlimited period of time but restrict the right to use the spectrum according to certain schedules included in the licenses. All Telefónica's Brazilian mobile operating companies (the existing ones and some new acquisitions) were renamed "Vivo" with the exception of Telemig Celular. The following licenses are held by our Brazilian mobile operating company, Vivo:

- Vivo-Rio Grande do Sul ("A" Band) until 2022 (renewed in 2006);
- Vivo-Rio de Janeiro ("A" Band) until 2020 (renewed in 2005);
- Vivo-Espírito Santo ("A" Band) until 2023 (renewed in 2008);
- Vivo-Bahia ("A" Band) and Vivo-Sergipe ("A" Band) until 2023 (renewed in 2008);
- Vivo-São Paulo ("A" Band) until 2023 or 2024, for the cities of Ribeirão Preto and Guatapar (renewed in 2008);
  - Vivo-Paraná/Santa Catarina ("B" Band) until 2013;
  - Vivo-Distrito Federal ("A" Band) until 2021, (renewed in 2006);
- Vivo-Acre ("A" Band), Vivo-Rondnia ("A" Band), Vivo-Mato Grosso ("A" Band) and Vivo-Mato Grosso do Sul ("A" Band) until 2024 (renewed in 2008);
  - Vivo-Gois/Tocantins ("A" Band) until 2023 (renewed in 2008);
  - Vivo-Amazonas/Roraima/Amap/Par/Maranho ("B" Band) until 2013;
  - Telemig Celular (Minas Gerais) ("A" Band) until 2023 (renewed in 2007);
- Telemig Celular (for the cities where CTBC Telecom operates in the state of Minas Gerais) ("E" Band) until 2020.

For "A" and "B" Bands, the renewal of licenses must be solicited 30 months before expiration. Spectrum rights may be renewed only once for a 15-year period, after which title to the license must be renegotiated.

For “E” Band, the renewal of licenses must be solicited between 36 and 48 months before expiration. Spectrum rights may be renewed only once for a 15-year period, after which title to the license must be renegotiated. In December 2007, ANATEL auctioned fifteen new licenses in the 1900 MHz radio frequency band, denominated as “L” Band. Vivo acquired 13 spectrum licenses in “L” Band.

- Vivo-Rio Grande do Sul (“L” Band) until 2022 (renewed in 2006) or 2022 for the cities of the metropolitan area of Pelotas;

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- Vivo-Rio de Janeiro (“L” Band) until 2020 (renewed in 2005);
- Vivo-Espírito Santo (“L” Band) until 2023 (renewed in 2008);
- Vivo-Bahia (“L” Band) and Vivo-Sergipe (“L” Band) until 2023 (renewed in 2008);
- Vivo-São Paulo (“L” Band) until 2023 or 2024, for the cities of Ribeirão Preto and Guatapar (renewed in 2008) or 2022 for the cities where CTBC Telecom operates in the state of So Paulo;
  - Vivo-Paran (excluding the cities of Londrina and Tamarana)/Santa Catarina (“L” Band) until 2013;
  - Vivo-Distrito Federal (“L” Band) until 2021, (renewed in 2006);
- Vivo-Acre (“L” Band), Vivo-Rondnia (“L” Band), Vivo-Mato Grosso (“L” Band) and Vivo-Mato Grosso do Sul (“L” Band) until 2024 (renewed in 2008) or 2022 for the city of Paranaba of Mato Grosso do Sul; and
- Vivo-Gois/Tocantins (“L” Band) until 2023 (renewed in 2008) or 2022 for the cities where CTBC Telecom operates in the state of Gois; and Vivo-Alagoas/Cear/Paraba/Piaui/Pernambuco/Rio Grande do Norte (“L” Band), until 2022.

For “L” Band, the renewal of licenses must be solicited between 36 and 48 months before expiration. Spectrum rights may be renewed only once for a 15-year period, after which title to the license must be renegotiated.

In April 2008, ANATEL auctioned 36 new licenses in the 1900-2100 MHz radio frequency bands (3G licenses). Vivo was awarded seven spectrum licenses in Band J and Telemig Celular was awarded two licenses.

- Vivo-Rio Grande do Sul (including the cities of the metropolitan area of Pelotas) (“J” Band) until 2023;
  - Vivo-Rio de Janeiro (“J” Band) until 2023;
  - Vivo-Esprito Santo (“J” Band) until 2023;
  - Vivo-Bahia (“J” Band) and Vivo-Sergipe (“J” Band) until 2023;
- Vivo-So Paulo (including the cities of Ribeiro Preto and Guatapar and the cities where CTBC Telecom operates in the state of So Paulo) (“J” Band) until 2023;
  - Vivo-Paran (including the cities of Londrina and Tamarana)/Santa Catarina (“J” Band) until 2023;
  - Vivo-Distrito Federal (“J” Band) until 2023;
- Vivo-Acre (“J” Band), Vivo-Rondnia (“J” Band), Vivo-Mato Grosso (“J” Band) and Vivo-Mato Grosso do Sul (including the city of Paranaba) (“J” Band) until 2023;
- Vivo-Gois (including the cities where CTBC Telecom operates in the state of Gois)/Tocantins (“J” Band) until 2023;
  - Vivo-Alagoas/Cear/Paraba/Piaui/Pernambuco/Rio Grande do Norte (“J” Band), until 2023;

- Vivo-Amazonas/Roraima/Amapá/Pará/Maranhão (“J” Band) until 2023; and
- Telemig Celular (including the cities where CTBC Telecom operates in the state of Minas Gerais) (“J” Band) until 2023.

For “J” Band, the renewal of licenses must be solicited between 36 and 48 months before expiration. Spectrum rights may be renewed only once for a 15-year period, after which title to the license must be renegotiated.

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### Prices and tariffs

ANATEL regulates rates for the STFC provided in the public regime. Operators with licenses to operate under the personal mobile regime are authorized to increase basic plan tariffs only for inflation and only on an annual basis. Operators are also allowed to establish non-basic tariffs and modify them without ANATEL's prior approval.

### Interconnection

In July 2005, ANATEL published a new regulation for interconnection among providers of telecommunications services, which require operators to issue a public document disclosing all of the conditions for the establishment of interconnection for all classes and types of services.

The SMP regime allows operators to freely negotiate interconnection rates with other operators. If they fail to reach an agreement, each operator may call upon ANATEL to determine the terms and conditions of interconnection.

### Competition law

Brazilian competition regulation is based on Law No. 8,884 of June 11, 1994 which prohibits any practice aimed at restricting free competition, dominating the relevant market of goods or services, arbitrarily increasing profits, or abusively exercising dominant market position. The Economic Law Office, or SDE, the Secretariat for Economic Monitoring, or SEAE, and the Administrative Council for Economic Defence, or CADE, are the agencies authorized to enforce the competition rules.

### Mexico

#### Regulatory framework

The provision of all telecommunication services in Mexico is governed by the Federal Telecommunication Law and various service-specific regulations. The governmental agencies which oversee the telecommunications industry in Mexico are the Secretariat of Communications and Transportation, or SCT, and the Federal Telecommunications Commission, or COFETEL.

#### Licenses and concessions

In Mexico, authorizations to provide mobile telephony services (mobile and personal communication services, or PCS, for the 800MHz and 1.9GHz bands, respectively) are granted through concessions. Currently, regarding the mobile licenses (800MHz), only one Band A and one Band B service provider may provide mobile telephony services in each region. Regarding PCS licenses, there is no exclusivity in the provision of service, in each region by more than one operator. In fact, there are currently three operators in each region. These concessions were granted in 1998 and 2005 for a period of twenty years, and may be renewed for additional 20-year periods, subject to the fulfillment by the operator of certain terms and conditions.

In total, Telefónica Móviles México, and its subsidiaries and participated companies have 22 licenses granted by SCT, which enable it to provide telecommunications services:

- Telefónica Móviles México's mobile operating companies have been granted concessions to operate mobile telephony services on Band A until 2010. SCT granted licenses to Baja Celular Mexicana, S.A. de C.V., or Bajacel, dated July 17, 1990 Movitel del Noroeste, S.A. de C.V., or Movitel, also dated July 17, 1990 Telefonía Celular del Norte, S.A. de C.V., or Norcel, dated July 23, 1990 and Celular de Telefonía, S.A. de C.V., or Cedetel, dated

August 2, 1990. The renewal of those four concessions was requested in 2005. The renewal decision is still pending.

·Furthermore, SCT granted to Telefónica Móviles México, through Pegaso Comunicaciones y Sistemas, S.A. de C.V. a license to provide public telecommunications services, on June 23, 1998, and nine spectrum licenses, dated October 7, 1998, in the 1900Mhz band to provide personal communication services in each of the nine PCS service region, and valid until 2018. Those licenses may be extended for additional



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twenty-year periods. For all of these licenses renewal was requested in 2008, and the renewal decision is still pending. On April 21, 2005, SCT granted Telefónica México four more spectrum licenses in the same 1900MHz band, to provide the PCS service and have more bandwidth in regions 3, 5, 7 and 8, valid for 20 years, and with the possibility be renewed for up to 20 additional years.

•SCT also granted to Grupo de Telecomunicaciones Mexicanas, S.A. de C.V., or GTM, a company in which Telefónica Móviles México has an interest, several licenses:

- i) on June 24, 1998, to install microwave links in 23GHz frequencies, for a period of 20 years;
- ii) on December 13, 1999, to install microwave links in 7GHz frequencies, for a period of 20 years, and that can be renewed;
- iii) on June 5, 2003, to install a public telecommunication network to provide domestic and international long distance service granted, for a period of 15 years, and that can be renewed; and
- iv) on March 28, 2006, GTM was authorized a renewal of the concession to provide fixed telephony and public telephony, nationwide for a period of 15 years, that can be renewed.

### Prices and tariffs

Tariffs charged to customers are not regulated. They are set by mobile operating companies and must be registered with COFETEL. Rates do not enter into force until registered by COFETEL.

### Interconnection

Mexican telecommunications regulations obligate all telecommunications network concessionaires to execute interconnection agreements on specific terms when requested by other concessionaires. Interconnection rates and conditions may be negotiated by the parties. However, should the parties fail to agree, COFETEL must fix the unresolved issues, including tariffs.

### Foreign ownership/restrictions on transfer of ownership

Mexican foreign investment law restricts foreign investment in local fixed service and other telecommunications services to a maximum of 49% of the voting stock, unless the Mexican National Commission of Foreign Investment approves a higher percentage participation, which it can do only in the case of mobile telecommunications companies.

Bajacel, Movitel, Norcel, Cedetel and Pegaso, as mobile telecommunications companies, received the required approvals from the National Commission of Foreign Investment permitting our ownership of more than 49% of their outstanding voting capital.

GTM, a company in which Telefónica México has an interest, provides local fixed and long distance services. This operator complies with Mexican foreign investment law, and has a stock structure that includes the participation of its Mexican partner, Enlaces del Norte. S.A. de C.V., which has 51% of the voting stock.

### Competition law

The Federal Economic Competition Law enacted in 1992 and amended on June 28, 2006 prohibits monopolies and any practices that tend to diminish, harm or impede competition in the production, processing, distribution or marketing of goods and services. The Federal Competition Commission, or COFECO, is the administrative body empowered to enforce the Law.

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### Venezuela

On June 1, 2000, the national legislative commission approved the Telecommunication Law. On February 1, 2006, the national legislative commission approved the Ley Habilitante that grants the President of the Republic capacity to enact decrees in relation to the telecommunication sector, though no formal modification to current law has been made.

#### Licenses and concessions

Telcel has been granted a mobile telephony concession to operate and offer mobile services in the 800 MHz band with national coverage, granted in 1991 and expiring on May 31, 2011 that may be extended for a term no longer than 20-year, subject to CONATEL's discretion. Telcel also holds a private network services concession, granted in 1993 and renewed on November 28, 2007, until December 15, 2025, that allows Telcel to offer point-to-point or point-to-multipoint private telecommunication services to corporations. In 2000, Telcel was granted a general license (Habilitación General) to offer local telephony services, national long distance services and international long distance services and to otherwise operate telecommunications networks for a 25-year period expiring on December 15, 2025. In 2001, Telcel obtained a concession to offer fixed wireless access services nationwide using wireless local loop technology.

On November 28, 2007, the National Telecommunications Commission, or CONATEL, in accordance with the Telecommunications Law, incorporated into the general license the rest of the services provided by Telcel: mobile, private networks, Internet access and transport. On that same date, Telcel was granted a concession to operate in the 1990 MHz band for a period of 15 years, until November 22, 2022, renewable for a period of ten years.

#### Prices and tariffs

Under Venezuelan regulations, telecommunications operators are free to determine and set prices for the services that they offer, within the price cap established by the regulator. However, exemptions to the free pricing regime may be applicable to market dominant operators, universal services projects or as a result of market distortions caused by anti-competitive conduct as determined by the Competition Agency.

#### Competition law

Venezuelan law governing competition is the Promotion and Protection of Free Competition Act 1992. It prohibits monopolistic and oligarchic practices and other means that could impede, restrict, falsify, or limit the enjoyment of economic freedom. The Office of the Superintendent for the Promotion and Protection of Free Competition is the agency empowered to apply the Competition Act.

### Chile

#### Regulatory framework

The General Telecommunications Law No. 18,168 of 1982, as amended, establishes the legal framework for the provision of telecommunications services in Chile.

The main regulatory authority in Chile is the Under-Secretary of Telecommunications, or SUBTEL.

#### Licenses and concessions

Under the General Telecommunications Law, companies must obtain licenses in order to provide fixed telecommunications services. Licenses granted for public and intermediate services generally have 30-year terms and may be renewed indefinitely for 30-year periods at the request of the operator, though certain licenses held by Telefónica Chile have longer terms.

Telefónica Chile holds the following licenses for the provision of telecommunications services:

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- Local telephony public service licenses. Telefónica Chile holds a license for local telephone service in all regions of Chile for a 50-year renewable period which began on December 1982, except Regions X and XI, which were incorporated to such license in 1995. In addition, Telefónica Chile holds various other renewable license for nationwide local telephone services oriented, exclusively, for rural localities. Telefónica Chile also holds a nationwide public service renewable license for data transmission for a 30-year period beginning as of July 1995, and four other public service renewable licenses for data transmission for a 30-year period beginning as of June 2008.
- Multicarrier long-distance licenses. Under the Multicarrier System, Telefónica Chile's former long-distance subsidiary, Telefónica Mundo Larga Distancia S.A. (before Telefónica Mundo), held 30-year renewable licenses, for a period beginning as of November 1989, to install and operate a nationwide fiber-optic network, a network of base stations and other transmission equipment, and to provide domestic and international long-distance services, including voice, data and image transmission, throughout Chile. In addition, Telefónica Mundo Larga Distancia S.A. held 30-year renewable licenses, for a period beginning as of June 1993, to nationwide public service data transmission. Telefónica Chile's other long-distance subsidiary, Globus, also held licenses for an indefinite term to provide domestic and international long-distance services through central switches and cable and fiber-optic networks nationwide. After the merger of these subsidiaries in 2006, all the aforementioned licenses remain under the ownership of the same company, which is now known as Telefónica Larga Distancia.
  - Public service data transmission. In addition to the 30-year data transmission license previously mentioned, Telefónica Chile, through Telefónica Empresas, holds, as of March 1987, nationwide public service data transmission licenses for an indefinite term.
- Public service mobile telephony licenses. Telefónica Móviles Chile holds licenses with indefinite terms, beginning as of November 1989, to provide public service mobile telephony services throughout Chile in the 800 megahertz frequency range. Telefónica Móviles Chile also holds three concessions for the provision of mobile telecommunications services nationwide in the 1900 MHz band. These concessions may be renewed for successive thirty-year periods as of 2002 at the request of the holder.
- Limited television license. Telefónica Chile's subsidiary Telefónica Multimedia, has a license to establish, operate, and use a part of the spectrum of the 2.6 GHz bandwidth in Santiago, Chile, for an intermediate telecommunications service concession, authorizing the frequencies used to communicate voice, data and images, for a 30-year period beginning as of May 2008. Telefónica Multimedia also holds a license authorized by Resolution No. 47 enacted on November 28, 1990, amended by Resolution No. 1536 of 1994, and Resolution 1453 of 2002, to provide limited television service in 2.6 GHz. Since December 2005, Telefónica Chile, through Telefónica Multimedia, holds a nationwide 10-year renewable license to provide limited satellite television service. Additionally, in January of 2006, Telefónica Chile, through Telefónica Multimedia, was assigned a limited television service license to provide the service nationwide in the main municipalities, except Region III, through Telefónica Chile's xDSL broadband network for an indefinite period. Moreover, in March 2007, a limited television service license was granted in order to provide this service, through the DSL broadband network, in the Santiago Metropolitan area, for an indefinite period.

## Prices and tariffs

Under the General Telecommunications Law, maximum tariffs for telephony services are set every five years by the Ministry of Transport and Telecommunications and the Ministry of Economy. In addition, the Competition Tribunal may subject any telephony service to price regulation, except for mobile telephone services to the public that are expressly exempted under the General Telecommunications Law.

The Competition Tribunal ruled in January 2009 that only some local telephone services were to be subject to tariff regulation (line connections, monthly fixed charges, variable traffics charges, and public payphone services are excluded). Accordingly, it was determined that every local telephone company, within its service zones, would be regulated with respect to tariff levels and structure. In addition, Telefónica Chile, in its capacity as a “dominant

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operator” (except in regions where other companies are the dominant operators), is regulated on a non-price basis, with requirements that it not engage in discriminatory pricing and that it give previous notice of plans and packages.

### Interconnection

Interconnection is obligatory for all license holders with the same type of public telecommunications services and between telephony public services and intermediate services that provide long distance services. The same requirement applies to holders of those intermediate service licenses, who are required to interconnect their networks to the local telephone network.

A “calling party pays” tariff structure was implemented on February 23, 1999. Under this tariff structure, local telephone companies pay mobile telephone companies an access charge for calls placed from fixed networks to mobile networks. Local telephone companies may pass this interconnection charge on to their customers. Every five years, SUBTEL sets the applicable tariffs for services provided through the interconnected networks.

### Competition law

The principal regulation concerning competition in Chile is Decree No. 211 of 1973, whose current text was established in Decree N° 1 of 2005. Pursuant to the provisions of this law, acts or behavior involving economic activities that constitute abuse of a dominant market position, or limit, restrain, or distort free competition in a manner that injures the common economic interest in the national territory are prohibited. The Competition Tribunal deals with infringements of competition law.

## Argentina

### Regulatory framework

The basic legal framework for the provision of telecommunications services in Argentina is set forth in the National Telecommunications Law (No. 19,798) of 1972 and in the specific regulations governing each type of telecommunications service. Also, Decree 264/98 established a transitory period from a monopolistic market towards a free market, promoting the protection of small operators while imposing obligations on basic services licensees. Decree 764/00, established the new and actual regulatory framework rules for a free market, and includes interconnection, licenses, universal service and spectrum rules.

The following regulatory authorities oversee the Argentine telecommunications industry:

- the National Communications Commission, or CNC, supervises compliance with licenses and regulations, and approves changes to mandatory goal and service requirements; and
- the Secretariat of Communications, or SECOM, grants new licenses, regulates the bidding and selection processes for radio-spectrum authorizations, and approves the related bidding terms and conditions.

### Licenses and concessions

Telefónica de Argentina holds licenses for fixed line services, all granted for an unlimited period of time, which entitle it to provide fixed line telecommunications services; international telecommunications services; local services in the northern and southern regions; long distance, international and data transmission telecommunications services in the northern region; and Internet access and international data transmission services.

Telefónica Móviles de Argentina's licenses for the provision of mobile services include PCS licenses and corresponding authorizations for use of spectrum for different regions, licenses and corresponding authorizations for use of spectrum for mobile telephone services for different regions; and licenses for trunking, or closed user group, services for different cities.

These licenses do not expire, but may be cancelled by the SECOM as the result of failure to comply with the terms of its license.



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### Prices and tariffs

On October 21, 2003, Law No. 25,790 became effective, extending the term for the renegotiation of concession or licensing agreements with public utilities until December 31, 2004, which was subsequently extended until December 31, 2009. This law also established that the decisions made by the Argentine government during the renegotiation process shall not be limited by, nor subject to, the stipulations contained in the regulatory frameworks currently governing concession or licensing agreements for the respective public utilities. Renegotiated agreements may cover some aspects of concession or licensing agreements and may contain formulas to adjust such agreements or temporarily amend them. As an investor in Argentina through Telefónica de Argentina, we commenced arbitration proceedings against the Republic of Argentina based on the Reciprocal Protection of Investments Treaty between Spain and Argentina for damages suffered by us because of the measures adopted by the Argentine government. We have temporarily suspended our participation in these proceedings in light of an agreement we reached with the Argentine government on February 15, 2006. If this agreement is approved by the Argentine Congress we plan to withdraw our claims against the Republic of Argentina.

Additionally, Decree No. 764/00 established that providers of telephone services may freely set rates and/or prices for their service which shall be applied on a non-discriminatory basis. However, 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. Providers may freely set their rates by areas, routes, long distance legs and/or customer groups so long as they are below the amounts established by the general tariff structure.

Also, the guidelines set forth in article 26 of Decree No. 1185/90 continue in effect for operators with significant market power. These guidelines establish information obligations with which operators must comply with respect to tariffs, both toward clients and the national regulator. This Decree also establishes the powers the regulator has to revise or revoke such tariffs.

Tariffs charged to customers for mobile services are not regulated in Argentina.

### Interconnection

Decree No. 764/00 approved new rules for national interconnection and established interconnection standards and conditions with which telephone service providers must comply regardless of pre-existing agreements. The rules for national interconnection set forth that interconnection agreements are to be freely negotiated between the relevant service providers, on a non-discriminatory basis. The regulations also establish the obligation for dominant and significant market operators to unbundle their local loops and to allow competitors to use them on a reasonable basis.

### Competition law

Law 25,156, on Protection of Competition prohibits any acts or behaviors related to the production or trade of goods or services, whose purpose or effect is to prevent, restrict or distort competition or market access, or that constitute abuse of dominant position in a market. The National Commission for the Defense of Competition is the authority entrusted with application of the law.

### Colombia

### Regulatory framework

In Colombia, telecommunications are a public service, subject to state regulation and oversight. Law 72/89 and Decree 1900/90 establish the general regime for telecommunications and broadcasting services and networks. Operators seeking to provide telecommunications services in Colombia must obtain a concession from the Colombian government. Concessions may be granted by license or contract.

In relation to value added services, by Decree 2870/07 the Communications Minister modified the authorization system. To provide these services under the modified authorization system, operators must apply for a convergent title. This title grants the right to provide convergent services like long distance communications, value added

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services and carrier services for a period of ten years (which can be extended for an additional ten years). Convergent titles do not cover mobile telephony and television services.

Also, due to decree 2870, 2007, the regulatory framework shall be transformed towards a relevant market regulation. In 2008 the Telecommunications Commission started the regulatory process to identify relevant markets, operators with dominance (SMP) and remedies via ex ante regulations.

### Licenses and concessions

Concessions for mobile services in the Eastern Region, the Caribbean Coast Region and the Western Region were granted in March 1994 for a ten-year period and extended for ten years until March 28, 2014. At the expiration of this period, the concessions must be renegotiated. Telefónica Móviles Colombia also holds two concessions to provide value added services nationwide, one granted in August 1997 initially for a ten-year period, extendible once for an additional ten years, and the other granted in December 1994 initially for a ten-year period, extended until December 2014.

Additionally, Telefónica Móviles Colombia holds concessions for carrier services nationwide, granted in June and November 1998 (initially for ten years and may be extended once for an additional ten years). Due to decree 2870 of 2007, these concessions were transformed into a convergent title. Ministry of Communications granted Telefónica Móviles on November 6, 2008 a convergent title to render carrier services for an additional ten-year period (which can be extended for an additional ten years).

With respect to fixed line services, Law 142/1994 establishes a general indefinite permission for all operators to operate as local exchange carriers in the national area. Colombia Telecom holds a legal indefinite authorization since 1947 to operate as a long-distance carrier throughout Colombia and abroad. Colombia Telecom holds a 20-year concession for offering value added services within Colombia and in-connection abroad, granted on November 8, 1991.

With respect to value added services, a national and in-connection abroad license was granted on December 2, 1994, for a ten-year period and was extended in 2004 until December 30, 2014. The license that Celumovil had until 2007 has expired and cannot be renewed due to the decree 2870 of 2007. As far as Colombia Telecom is concerned, pursuant to resolution No 4120 - November 8, 1991, the Minister of Communications granted its predecessor, Empresa Nacional de Telecomunicaciones, an authorization to provide value added services, telematic services and to extend a value added network for a 20-year period, until November 8, 2011.

Article 13 of Decree 1616/2003 establishes that Colombia Telecom can exploit the licenses, permissions, concessions and other authorizations which were granted to Empresa Nacional de Telecomunicaciones to provide telecommunications services. Consequently, Colombia Telecom has its authorization until to November 8, 2011.

### Interconnection

Mobile and fixed operators in Colombia have the right to interconnect to other operators' networks. Before the intervention of regulatory authorities, operators must attempt direct negotiations. Interconnection must assure compliance with the objectives of non-discriminatory treatment, transparency, prices based on costs plus a reasonable profit and promotion of competition.

### Prices and tariffs

Mobile tariffs charged to customers are not regulated, although they may not be discriminatory. Nevertheless fixed-to-mobile tariffs are subject to a price cap. Rates are fixed by mobile operating companies and must be registered with the Comisión de Regulación de Telecomunicaciones. The regulator set a price cap of 392 Colombian pesos per minute for fixed to mobile tariffs since November 1, 2006. Local tariffs are regulated, but operators have the opportunity to offer several alternative plans that are not regulated although they must be registered.

Due to market regulation process, the Telecommunications Commission in December 2008, published a proposed amendment to modify the price cap of 392 to 200 Colombian pesos per minute for fixed to mobile communications. This proposed amendment is currently subject to discussion with operators.

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### Television services

In January 2007, Colombia Telecom signed a concession agreement with the Television Commission to provide DTH services for ten years. This is a concession granted with a national scope.

In December 2008, the Television Commission published Agreement No. 006. By this disposition the carry obligations of operators of closed television has been modified to require that regional channels be broadcast only in the cover area of the channel and only if it is possible technically.

### Competition law

The Colombian Competition Law is incorporated in the Law No. 155/59 and Decree No 2153/92 on Restrictive Trade Practices. The law prohibits entering in any agreement or engaging in any type of practice, procedure, or system that aims to limit free competition and abuse of a dominant position. The Superintendent of Industry and Commerce is the Colombian competition authority.

### Peru

#### Regulatory framework

The provision of telecommunications services in Peru is governed by the Telecommunications Law and related regulations.

#### Licenses and concessions

Telefónica del Perú provides fixed line telecommunications services based on concessions granted by the Ministry of Transportation and Communications, or TMC. The concession term is for 20 years, which may be renewed totally or partially at Telefónica del Perú's request. Total renewal is for an additional 20-year period. Partial renewal is for periods of up to five additional years. Two partial renewals have been approved, extending the concession term until 2023.

Providers of mobile services seeking to operate in Peru must obtain a non-exclusive license from the TMC. Licenses are granted by means of a license agreement entered into between the TMC and the licensee and set forth the licensee's rights and obligations, including the regions where the licensee is authorized to operate. Licenses are granted either by application or through a bidding process.

Telefónica Móviles Perú has a concession for the provision of mobile services on Sub Band A of the 850 MHz Band and Sub Band of 1900 MHz (in these bands, Telefónica Moviles Perú can also provide fixed wireless services) for a 20-year period, renewable upon request for identical periods. It also holds concessions for offering international and domestic long distance carrier services, granted in February 2002 for a 20-year period. Additionally, it has a concession for the provision of wireless fixed telephony services on the 450 MHz and 900 MHz band for a 20-year period. Both concessions were granted on March 3, 2008. It also holds the concessions for local carrier services, which expire between 2016 and 2022. Concessions for domestic and international carrier services expire on February 5, 2019. In addition, it has a concession for local fixed telephony services for national coverage, granted on August 10, 1999 for a 20 year period. These concessions may be renewed for successive 20-year periods.

Under the concessions to provide mobile services, mobile operators are obligated to meet certain quality service requirements with respect to call failure, radio-electric coverage and quality of communications. These requirements are established on a yearly basis and are gradually increased in order to improve the quality of the service provided.



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### Prices and tariffs

Tariffs for fixed telephony services must be approved by the National Regulatory Authority, the Organization for Supervision of Private Investment in Telecommunications, or OSIPTEL, in accordance with a price cap formula based on a productivity factor. Rates charged by mobile providers to their customers have been subject to a free tariff regime supervised by OSIPTEL. Tariffs must be reported to OSIPTEL prior to implementation.

### Interconnection

Mobile service providers are required, upon request, to interconnect with other concession holders. According to the principles of neutrality and non-discrimination contemplated in the Telecommunications Law, the conditions agreed upon in any interconnection agreement will apply to third parties in the event that those conditions are more beneficial than terms and conditions agreed upon separately.

### Competition law

The general competition framework in Peru is based on the Legislative Decree No. 701. This law prohibits any monopolistic practices, controls, and restraints on free competition and it is applied, in the telecommunication sector, by OSIPTEL.

### Ecuador

#### Regulatory framework

The Special Telecommunications Law and the General Regulation to the Special Telecommunications Law establish the regulatory regime applicable to the provision of telecommunications services in Ecuador.

#### Licenses and concessions

After a new agreement with the Ecuadorian government, Otecel renewed its mobile telephony services concession which now allows Otecel to provide advanced mobile services, including 3G services. The concession will expire on November 29, 2023 and may be extended for a subsequent 15-year period.

Beside the above mentioned concession, Otecel holds a concession to provide fixed and mobile services carrier services, which expires on April 22, 2017 and may be extended for a subsequent 15-year period and different licenses for the provision of mobile value added services and Internet mobile access, each of which expires on February 21, 2010 and may be extended for a subsequent ten-year period. It also holds a license to provide conventional Internet services, which expires on January 25, 2011 and may be extended for a subsequent ten-year period.

A monthly fee amounting to 1% of the invoiced revenues of mobile services must be paid by all operators holding concessions to the National Secretary of Telecommunications as a contribution to support universal service. Otecel via its contract may cancel such fee by giving services to agreed zones within the National Plan for Universal Service.

### Prices and tariffs

The mobile services concession of Otecel is subject to a maximum rate of \$0.50 per minute for mobile services and a maximum rate of \$0.10 per minute for rural public telephony. Otecel may fix rates freely so long as it does not exceed these rates, and provided that it notifies the correspondent regulatory body 24 hours ahead of any price increase.

Otecel may fix rates freely under its carrier services concession.



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## Other business lines in Latin America

| Country     | License/Concession and authorizations | Type of service                    | Spectrum                 | Band                | Expiration   |
|-------------|---------------------------------------|------------------------------------|--------------------------|---------------------|--------------|
| El Salvador | Concession                            | Telecommunications services(1)     | 25 MHz/800MHz            | B Band              | 2018(2)      |
|             | Concession                            | Telecommunications services(1)     | 30 MHz/1900MHz           | C Band              | 2021         |
| Guatemala   | Concession                            | Telecommunications services(1)     | 80 MHz/1900MHz           | B, C, E and F Bands | 2014(3)      |
|             | Concession                            | Telecommunications services(1)     |                          |                     | 2014(3)      |
|             | Concession                            | Telecommunications services(1)     |                          |                     | 2014(3)      |
| Nicaragua   | Concession                            | Mobile telecommunications services | 800 MHz                  | A Band              | 2013(4)      |
|             | Concession                            | Mobile telecommunications services | Additional spectrum 1900 | D Band              | 2013         |
| Panama      | Concession                            | GSM/UMTS                           | 800/1900 Mhz             | A Band              | 2016(5)      |
| Uruguay     | License                               | Mobile telephony                   | 25 MHz 800 MHz           |                     | 2022-2024(6) |

(1)According to the Telecommunications Law all of such concessions were granted to provide any telecommunications services.

(2)Concessions for use of spectrum are granted for a 20-year period and may be renewed for additional 20-year periods upon execution of the proceedings set forth in the Telecommunications Law.

(3)All of such concessions are granted for a 15-year term and may be renewed for subsequent fifteen-year terms at the request of the holder. In order to renew a title, the holder must demonstrate before the regulatory body, that the spectrum was effectively used during the previous 15-year term. All of these titles are set to expire in 2014.

(4)Telefónica Móviles Nicaragua was granted a concession in 1992 for a ten-year period for the use of 25 MHz of spectrum in the 800 MHz Band A to provide mobile telecommunications services, the regulatory entity granted to Telefónica Nicaragua 10 Mhz of additional spectrum in the 1900 Band D. This concession was renewed for another ten-year period in 1998, and will expire on July 31, 2013. The concession may be renewed for another ten-year period through negotiation with TELCOR two years prior to the expiration of the current concession, subject to the fulfillment of certain terms and conditions by the operator.

(5)The concession period is for 20 years and expires in 2016. This can be extended for another period in accordance with the concession contract. The Panamanian government granted us the right to use 10 MHz (5+5) in the 1900 MHz Band until 2016, which can be extended for another period.

(6) The expiration date depends on the spectrum concession: band 800 MHz (12.5MHz + 12.5MHz) – 20 years from July 2004; band 1900 MHz (5MHz + 5MHz) – 20 years from December 2002; and band 1900 MHz (5MHz + 5MHz) – 20 years from July 2004.

#### Seasonality

Our main business is not significantly affected by seasonal trends.

#### Patents

Our business is not materially dependent upon the ownership of patents, commercial or financial contracts or new manufacturing processes.

#### C. Organizational Structure

See “—History and Development of the Company” and “—Business Overview.”

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### D. Property, Plant and Equipment

In 2007, we moved to our new central headquarters for the Telefónica Group, “Distrito C”, in Las Tablas (Madrid), Spain.

#### Fixed Networks

We have fixed networks in Spain, Latin America and Europe with a presence as incumbent in Spain, Argentina (the greater Buenos Aires metropolitan area and the southern portion of the country), Brazil (São Paulo), Chile, Peru, Colombia and the Czech Republic.

Following market trends, competitive environments, evolution of technologies and new multimedia and broadband services demanded by our customers, we have in recent years generally upgraded our networks as follows:

- progressive introduction of broadband access technologies over copper: ADSL, ADSL2+, VDSL2, etc. increasing the bandwidth capacity of the accesses;
- introduction of fiber access technologies (xPON) across different access scenarios: fiber to the home (FTTH), fiber to the building (FTTB), fiber to the curb (FTTC), fiber to the node (FTTN), etc., increasing the access speed up to 100Mbps;
- making available powerful Internet Protocol/ Multiprotocol Label Switching (IP/MPLS) backbones and transmission technologies providing full connectivity to the rest of the network layers, such as access and control, to support services for all business and customer market segments (fixed and mobile);
- migrating current time division multiplexing (TDM) switching networks (PSTN and ISDN) to new generation network (NGN) all IP packet networks;
- introduction of IMS (Internet Multimedia Subsystem) in many countries to simplify the control of the network and ease both the development and launching of new services;
- providing more intelligence to the network to better manage its use, avoid saturations and frauds and to identify new business opportunities;
  - providing for fixed-to-mobile convergence of networks, services and operation support systems & business support systems (OSS&BSS) systems in the operations and countries where it is feasible to do so;
- migrating and concentrating transport technologies from legacy ones, such as asynchronous transfer mode (ATM), frame relay (FR), leased lines at low speed, plesiocronous digital hierarchy (PDH) and synchronous digital hierarchy (SDH), to the new generation of optical transport ones, such as dense wavelength division multiplexing (DWDM), coarse wavelength division multiplexing (CWDM) and new generation - synchronous digital hierarchy (NG-SDH); and
- deployment of new services such as pay TV, under the Imagenio brand, to customers connected through broadband accesses in Spain, Czech Republic, Peru, Chile, Colombia and Brazil.

#### Mobile Networks

We have mobile networks in Spain, the United Kingdom, Germany, Ireland, the Czech Republic, Slovakia, Morocco, Brazil, Argentina, Venezuela, Chile, Peru, Colombia, Mexico, Guatemala, Panama, El Salvador, Nicaragua, Ecuador and Uruguay. In the case of Brazil (Brasilcel –Vivo) and Morocco (Medi Telecom) the ownership of the networks is shared with Portugal Telecom (50.0% and 32.18% respectively).

We use a number of mobile technologies in the countries in which we operate, for example, GSM and UMTS in Spain, the United Kingdom, Germany, Czech Republic, Slovakia, Latin America and Morocco; CDMA in other

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countries in Latin America (such as, Brazil and Colombia) and the Czech Republic and TDMA technology in certain other countries in Latin America (such as Venezuela).

We are continuing to work to upgrade our mobile networks in line with market trends, demand of new services from customers and the evolution of technologies. The main steps we are currently taking include:

- progressive migration from TDMA and CDMA technologies to GSM or UMTS technologies in markets where it is convenient;
  - introduction of broadband into mobile access using technologies such as UMTS, HSDPA and HSUPA;
- deploying new services such as mobile television and exploring next generation music, video and game services based on Microsoft's Playready technology;
- exploring the feasibility of new technologies as WiMax, HSPA and LTE (Long Term Evolution) to provide mobile accesses with increased bandwidth;
- HSPA: we have been committed to the deployment of this technology in countries in which we have presence and as of December 31, 2008 have increased our coverage up to around 80% in Europe and around 90% in Latin America; and
- LTE: together with main vendors and sharing experience with other operators, we have extensively analyzed the opportunities LTE will bring as 4G mobile technology is used to complement current network technology by creating higher capacity at lower relative cost by user/traffic unit, and we intend to start testing this technology in 2009; and