Fiscal Control Policy

Telefónica Group Regulations

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Telefónica, S.A.
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1. PURPOSE OF THE FISCAL CONTROL REGULATIONS

1.1 Purpose of the Regulations

The fiscal control framework of the Telefónica Group (the Group) is based on the following cornerstones:

- The Fiscal Strategy approved by the Board of Directors that incorporates the Group's responsible business principles that apply to tax matters.

- The fiscal control regulations defined in this document that outline the policies for the control and management of tax risk on the basis of the principles laid down in the Fiscal Strategy.

- The complementary regulations and operational processes for the day to day management of tax affairs that these regulations outline.

The purpose of these regulations is to define the Group's fiscal control framework, as well as the roles, tasks and responsibilities for the management thereof.

1.2 Scope of Application

These regulations are applicable to the Group, which includes Telefónica, S.A. and all the subsidiaries or companies that are dependent on it, in accordance with the provisions of section 42 of the Spanish Business Code.

Consequently, the directors of those entities shall take the necessary measures to apply the said regulations.

Telefónica, S.A., as the parent company of the Group, is in charge of establishing the foundations, instruments and mechanisms required to adequately and efficiently coordinate this company and all the other companies that make up the Group; all of which is to be applied without prejudice to and without impairing the autonomous decision-making capacity of each of the said companies, in accordance with their own corporate interests and with the fiduciary duties of the members of their boards of directors towards their shareholders.

1.3 Definition of Fiscal Control

Fiscal control consists of the activities aimed at ensuring:

- Correct compliance with tax obligations.
- The effectiveness and efficiency of operations from the point of view of taxation.
- The reliability of tax information.
- Transparency in the eyes of third parties, in particular, the Tax Authorities.

- The management of fiscal risks.

2. FISCAL CONTROL ROLE

The Group Tax Department is in charge of fiscal control, and it performs this task through the Regional Tax Departments, and the local heads of fiscal control in the various subsidiaries, in accordance with the principles defined below.

The Group undertakes to adopt whatever control mechanisms are needed to ensure compliance with tax legislation and the principles outlined below by all companies of the Group, within an appropriate business management framework, for which they shall dedicate the appropriate materials and personnel who have the necessary qualifications.

The fundamental principles of the fiscal control role are as follows:

2.1 Principle of Accountability

The head of fiscal control of each of the subsidiaries shall report to the Group Tax Department through the Regional Tax Departments.

2.2 Principle of Technical Qualification

Personnel in the Tax Department must have the necessary academic training and experience in the accountancy, financial and fiscal fields that will enable them to perform their duties in an appropriate manner.

All Fiscal Management professionals in the Tax Department must:

- Have the necessary academic training and experience in the accountancy, financial and fiscal fields which will enable them to comply with the Group's fiscal strategy.
- Implement practices aimed at the prevention and reduction of fiscal risks in the design and carrying out of their activities.
- Provide the advice needed to ensure that due consideration has been given to the tax implications of the implementation, documentation and maintenance of business decisions.
- Ensure that all fiscal decisions are motivated by business and commercial interests. Therefore, the tax implication of any transaction may not be justified independently of the commercial and business reasons for carrying out the operation in question.
- Ensure that every fiscal decision has a legal basis, and complies with the following basic conditions:
    - The revelation of information in full.
    - Knowledge of the actual circumstances and facts of the case.

- o An assessment of the fiscal risks regarding both fiscal technicalities, and those relating to reputation and business with regard to how a particular position may be perceived from the outside.

- Operate in jurisdictions that have adopted the standards of transparency and exchange of information recommended by the OECD and in particular the procedures set forth in Spanish tax law, while avoiding the use of structures of an opaque nature for tax purposes.
- Promote relations with the Tax Authorities which shall be governed by principles of mutual transparency, trust, good faith and loyalty.

2.3 Principle of Prevention and Management of Fiscal Risk

In the design and carrying out of their activities, every company shall apply the principles of sound and prudent fiscal policy embodied in the commitment to:

(i) Promote the practices aimed at the prevention and reduction of fiscal risks.
(ii) Avoid the use of opaque practices with regard to tax affairs, which are practices whose aim is to prevent the tax authorities concerned from discovering who is ultimately responsible for certain activities or the actual owner of the assets or rights involved.

Fiscal risks are managed with the aim of preventing and reducing tax disputes to those which are strictly necessary for the defence of fiscal policy which is adopted by the Group in accordance with the law.

This objective is achieved by adherence to the following criteria:
- A solid technical foundation in Law.
- Appropriate documentation with a clear explanation of the fiscal posture adopted.
- A close relationship with the tax authorities.
- Efficient tax management procedures which ensure accurate tax returns.

When it comes to business decision-making, an exhaustive analysis of the tax implications will always be carried out. If there are several tax alternatives which achieve the same objective, the most efficient alternative, from a tax point of view, shall be opted for.

The main situations which require a fiscal risk assessment are the following:
- Procurement and sale of shares.
- Decisions relating to changes in corporate structures.
- Business financing agreements.
- Significant transactions.
- International trade operations.
- New internal processes which may affect compliance with tax obligations.

2.4 Diligent Business Principles

In 2010, Telefónica, S.A. adopted the Code of Good Practice in Tax Affairs as decided by the Board of Directors. As a result, the Company does not use corporate structures in the pursuance of its business activity for the purpose of covering up or reducing the transparency of its activities in the eyes of the tax authorities or any other interested party, in accordance with the recommendations of the Code of Good Practice in Tax Affairs.

Furthermore, in accordance with the Capital Companies Act, the creation or procurement of shares in entities with special purposes or those domiciled in countries or territories which are considered tax havens, as well as any other transactions or operations of a similar nature which, owing to their complexity, could undermine the transparency of Telefónica, is reviewed and, where appropriate, subject to approval by the Board of Directors.

Telefónica will not create or acquire entities domiciled in any of the jurisdictions included in the list of tax havens established in Spanish regulations. If, for business reasons, the presence of an operator in a territory classified as a tax haven were to be necessary, authorisation would be sought from the Board of Directors.

The Group's operations in territories regarded by other bodies as having little or no taxation exist solely and exclusively for economic and commercial reasons (Business Purpose), and have the material and human resources needed to conduct the activities, and under no circumstances shall the purpose of those operations be to transfer profits to those jurisdictions in order to obtain a reduction in the tax burden.

Telefónica is committed to compliance with the stipulations of the "OECD Guidelines for Multinational Enterprises" in matters of taxation.

2.5 Principle of Transparency in the Relationship with the Tax Authorities

The relations of each company with the relevant tax authorities shall be governed by the principles of transparency, mutual trust, good faith and loyalty, and each company in the Group shall adopt the following good tax practices:

(i) Collaboration with the relevant tax authorities in the search for and identification of solutions with regard to any fraudulent tax practices of which the company is aware which could be implemented in the markets in which it is present.
(ii) Provision of all tax-related information and documentation requested by the relevant tax authorities in the shortest possible time and with the required scope.
(iii) The provision and open discussion of all relevant facts of which it is aware with the relevant department of the tax authorities concerned, in order to provide information, where necessary, of the cases in question and to reinforce the agreements

and compliance in the course of inspection procedures, to the extent reasonably possible and making every effort to apply good business management practice.

3. OPERATIONAL REGULATIONS FOR THE PREVENTION AND MANAGEMENT OF FISCAL RISK

Telefónica has a Corporate Risk Management Model based on the COSO (Committee of Sponsoring Organizations of the Treadway Commission), which enables the various risks to be identified, assessed and managed.

In accordance with this model, the Group has defined four risk categories: business, operational, financial and global. In this regard, fiscal risks are included in the category of financial risk.

In order to achieve this objective, the main guidelines for the management of the aforementioned risks are defined below.

3.1 Types of Fiscal Risk and Associated Verification Procedures

In accordance with their origin, fiscal risks are classified as follows:

- Risk of non-compliance: regarding compliance with obligations in the field of taxation (submission of tax returns, response to requests for information, and so on).

- Interpretative risk: concerning the possibility of interpreting tax law differently to the way the tax authorities interpret it.

- Regulatory risk: associated with legislative activity and regulatory complexity and volatility.

As well as having an economic impact, fiscal risks could have a reputational impact. This is in the light of the current context of public scrutiny and expectations with regard to transparency, and the perception, on the part of the various stakeholders, of the Companies' correct compliance with their fiscal obligations.

Telefónica performs the necessary verification procedures in relation to fiscal risks.

3.2 Identification and Assessment of Fiscal Risks

The Corporate Risk Management Model covers the identification and assessment of risks, response procedures and monitoring.

In spite of the fact that risk identification is a continuous process and one that requires the involvement of the entire organisation, in the case of fiscal risks, the Corporate Tax

Department will promote and coordinate the identification and regular updating (at least quarterly) of fiscal risks.

The assessment of fiscal risks will be performed in terms of probability and impact.

3.3. Information Obligations

On a quarterly basis, the fiscal control managers at each of the Group Companies shall inform the Group Tax Department, through the Regional Tax Departments, of the main conclusions of the process of identification and assessment of fiscal risks, as well as of the results of external tax audits and tax authority inspection processes.

In addition, Telefónica has a procedure of regular identification and reporting of Group risks in its main operations. In this regard, managers of tax affairs at each of the subsidiaries shall report on fiscal risks, including information about the following:

i) Lawsuits currently in the courts/arbitration
ii) Lawsuits subject to administrative law prior to going to court
iii) Operations with implicit risks that could be investigated by the tax authorities

The Tax Department shall be responsible for reporting on the situation and development of fiscal risks to those in charge of the Group's Risk Management (Internal Auditing), and ultimately to the Audit and Control Committee, without prejudice to the specific reporting of risks of non-compliance (identified as such in section 3.1) to those in charge of ensuring compliance.

3.4 Homogenisation of Tax Structures

The Group Tax Department, together with the Regional Tax Departments, is responsible for making proposals for the organisational structures of units, including proposals for the selection, appointment and remuneration of and incentives for its officials in coordination with the Human Resources Department and the Appointments and Remuneration Committee, where applicable, as well as the setting of their objectives and work plans and the evaluation of their performance. These proposals will be implemented by consensus with the senior managers of the fiscal control units in the companies.

3.5 Integration and Coordination

The manager of tax affairs in every company shall participate in the analysis of all operations that could have tax implications, and therefore shall:

- Be provided with the necessary financial, human and material resources.
- Have to establish permanent IT connections with the information systems of the companies in the Group, where necessary.
- Be provided with full support and assistance by the companies of the Group.
- Perhaps require the participation and collaboration of employees of those companies.

4. FISCAL CONTROL MONITORING: ORGANISATION

4.1 Audit and Control Committee of Telefónica, S.A.

The Group Tax Department shall report annually to the Audit and Control Committee and, where necessary, to the Board of Directors, on the fiscal policies of the Group, in order to facilitate the work of monitoring the fiscal risk management system, responsibility for which the Capital Companies Act assigns to the Audit and Control Committee, and also in accordance with the Code of Good Practice in Tax Affairs.

4.2 Group Tax Department and Regional Directorates

The role of the Group Tax Department, directly or indirectly through the Regional Tax Departments, is as follows:

- To define the Group's fiscal policies, and to establish the said policy's principles and criteria that govern how the Companies should act with regard to fiscal matters, in order to promote and execute projects that will benefit the Company and its employees, and contribute fairly to the public revenue of the countries in which we operate, with due rigour and transparency in internal relations and with the tax authorities.
- To inform the Audit and Control Committee, and where applicable, the Board of Directors of Telefónica, of the fiscal policies and criteria adopted by the company, as well as the fiscal impact of all the relevant operations that are subject to its approval in accordance with section 529 Ter. of the Capital Companies Act:
    - The approval of investments or operations of all kinds which, owing to their high amount or special characteristics, are strategic in nature or are particularly prone to tax risk – unless said approvals correspond to the General Meeting of Shareholders.
    - The creation or procurement of shares in entities with special purposes or those domiciled in countries or territories which are considered tax havens, as well as any other transactions or operations of a similar nature which, owing to their complexity, could undermine the transparency of the Group.
- To decide which tax issues should be reported to the Board or the Audit Commission, because of their relevance, complexity or impact on revenue.
- To represent the group as such and its companies in particular, in dealings with national or supranational tax authorities (AEAT, CEOE, OECD, etc.).
- To guide the Group through the continuous compliance and inspection procedures initiated by the tax authorities in various jurisdictions in coordination with the tax manager of the Company concerned.
- To sign the Consolidated Group Tax Returns as well as the records, notifications and procedural documents forming part of the Group inspection procedures.

- To sign, as the tax representative of the Group, all necessary claims and appeals in administrative lawsuits, whatever their level may be, either before national or international courts or for submission to supranational institutions (e.g. those of the EU).
- To authorise and sign on behalf of and in representation of the Group, all agreements reached by the Forum of Large Companies (IBEX 35) with the Ministry of the Economy and Finance and the Tax Agency.
- To create and manage working groups with companies in the industry or those with a similar turnover in order to obtain policy improvements or tax incentives for the activity of the Group, either as a whole or for the individual activity of any one of its Companies.
- To authorise the transactions, as appropriate, which are submitted to the Committee of Financial Operations (Spanish initials: COF) for approval.
- To authorise the hiring of each and every one of the external tax advisers in the Group as well as the signing of contracts for external tax advice in Spain and those which, owing to their purpose, affect the Group globally.
- To direct, authorise and control the actions and functions of the Tax Departments in the various countries where the Group operates.
- To appoint tax managers and directors in the countries where the Group operates.
- To decide on the optimal tax structures for the M&A processes and Group transactions.
- To direct and oversee supranational projects between different areas.
- To decide on the final, optimal tax analysis and design for the Group's investment, disinvestment and reorganisation transactions.
- To establish and validate the fiscal framework in which the Group's financial transactions are made.
- To decide on the feasibility of any actions identified for the purpose of optimising the Group's tax burden.
- To manage the direct taxes in the Group's profit and loss account and consolidated and individual financial statements which have a direct impact on the Group's net financial results and cash flow.
- To report on the situation and development of fiscal risks to those in charge of the Group's Risk Management (Internal Auditing), and ultimately to the Audit and Control Committee, without prejudice to the specific reporting of risks of non-compliance (identified as such in section 3.1) to those in charge of ensuring compliance.
- To coordinate, along with the Group's Internal Auditing personnel, the review and analysis procedures needed to ensure the control objectives of these regulations are reached.

4.3 Local Tax Manager

The tax managers of each subsidiary will be responsible for establishing the management procedures needed to ensure that fiscal control is performed in accordance with the operational principles and rules defined in these regulations.

A list of the main processes that are documented by control activities, is attached as Annex I to these regulations. In this regard, as a preliminary guide, the following related procedures are listed:

4.3.1 Accounting Procedures and Internal Control

- Check that the system of fiscal control in place in the subsidiary is in line with the characteristics of the entity.
- Review and update the accounting and internal control procedures adopted by the entity, related to the safeguarding of assets and the reliability of accounting records, which have tax implications.
- Prepare any suggestions and recommendations for improving fiscal control that may be deemed appropriate and, after they have been reviewed by the head of fiscal control, share them with the Regional Department.

4.3.2 Control Procedures for Corporation Tax

- Compare the Corporation Tax (Spanish initials: IS) return for the previous year with the corresponding audited account, and prepare a worksheet that includes all the temporary and permanent differences, and the fiscal risks, if any, arising from them.
- Verify the correct implementation of deductions in accordance with the limits set out in the regulations that apply at any given time.
- Verify the correct way to apply tax losses.
- Check the payment of Corporation Tax from the previous year and make sure that the possible differences between the provisional and the real figures have been paid/received in accordance with the General Accounting Aid (plangeneralcontable.com).
- Check the opening balances, movements and end of trading balances against relevant tax documentation.
- Verify the correct tax rate of the main income and expenditure components.
- Check the deductions for double taxation on dividends.
- Ensure that the legal requirements for the full enjoyment of tax incentives are being met.
- Check that there is not more than one type of deduction or incentive applied to the same item.

4.3.3 Control Procedures for Indirect Taxes

- Check due diligence is taken in keeping records of Value Added Tax (VAT) or equivalent indirect tax (Spanish initials: IIE): invoices received, invoices issued, investment assets.
- Check that VAT and IIE returns and payments are submitted correctly and in a timely fashion. Proof of income or request for postponement of payment.

- With regard to VAT or IIE incurred: balance sales and other transactions subject to tax, as shown in the profit and loss account of the audited financial year, with:
  i) The periodic returns to the Tax Authority for VAT or IIE incurred.
  ii) Sales figures, according to the Corporation Tax return.
  iii) The amounts given in the VAT or IIE records.
- With regard to VAT or IIE incurred: reconcile purchases, expenses or acquisitions of other assets and other transactions subject to tax, with:
  i) The periodic returns to the Tax Authority for VAT or IIE incurred.
  ii) The figures for purchases, expenses, property additions and other operations, according to the Corporation Tax return.
  iii) The amounts given in the VAT or IIE records.
- Check the correct application of tax rates.
- Verify that the pro rata rule is applied.
- Analysis of own-product consumption calculation.
- Analysis of calculation of exports to third countries.
- Analysis of charges incurred for imports from third countries: refund request.

4.3.4 Control Procedures for Income Tax Deductions

Deductions on Work Returns

- Reconcile the bases declared during the year with the eventual bases resulting from the annual return/summary.
- Check that returns are submitted correctly and in a timely fashion, along with payments or requests for the corresponding postponement.
- Reconciliation of the bases declared in the annual return/summary with the personnel expenditure recorded in the profit and loss account.
- Deduction rates applied in accordance with the nature of the contract and the date the employee joined the company.
- Check the deductions applied to: travel and food expenses, remuneration in kind or similar, bonuses, incentives and voluntary bonuses, personnel compensation and compensation for transfers.

Deductions on Income from Movable Capital Assets

- Check that deductions are declared in the period in which the tax is due and not when the corresponding payments are made.
- Verify that in cases of interest payments for related transactions, these are not lower than the official interest rate in force.
- Check that returns are submitted, even if they do not give rise to any taxable income or tax liability whatsoever.
- Check that the deductions on capital gains are performed in all cases and without prejudice to International Treaties or Agreements on: Dividends, technical assistance, leasing of movable property and business that does not constitute company activity.

- Check calculations and application of deduction rates in cases where International Treaties or Agreements exist, to avoid double taxation.
- Balance the annual deduction summary with: periodic returns made during the year and the profit and loss account.

5. AUDITING

The Internal Audit Directorate may perform however many audits and checks it deems appropriate to verify the correct application of the aspects contained in these regulations.

Annex I

List of Processes and Flowcharts

1. Fiscal Processes of the Corporate Tax Department

1.1 Corporate Tax Management
1.2 Fiscal Consolidation
1.3 Tax Situation Analysis
1.4 Corporation Tax Review
1.5 Tax Inspections
1.6 Tax Consulting and Support
1.7 Fiscal Planning of Operations
1.8 Tax Planning and Consultancy
1.9 Audit Planning
1.10 Tax Auditing

2. Fiscal Processes of the Shared Services Centre

2.1 Taxes (Shared Services Centre; Spanish initials: CSC)
2.2 Tax Return/Payment: General Process (CSC)
2.3 Prepare Tax Return/Payment Models (CSC)
2.4 Complete and Sign Tax Return/Payment Models (CSC)
2.5 Calculate and Pay Taxes (CSC)
2.6 Return/Payment of Local Taxes and other Taxes (CSC)
2.7 Corporation Tax Return/Payment (CSC)
2.8 EU VAT Refund Application (CSC)
2.9 Fiscal Processing of Invoices (CSC)
2.10 Intrastat Statement (CSC)
2.11 Public Authority Proceedings (CSC)
2.12 Tax Consulting (CSC)

3. Fiscal Processes of the Tax Management Department

3.1 Record Corporation Tax Expenditure
3.2 Make Periodic Corporation Tax Payments
3.3 Corporation Tax Return/Payment