

Suppliers: equality of opportunity and mutual benefit

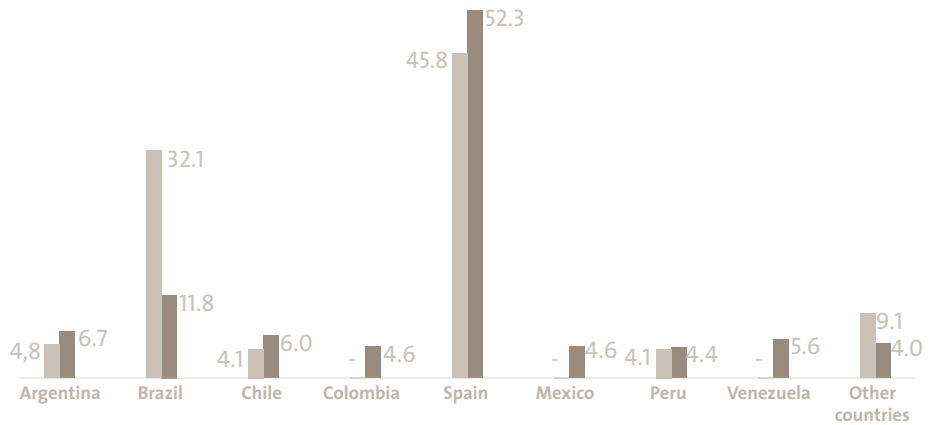
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Distribution of purchasing volume by countries

Data in percentage of total purchases



Purchasing volume¹

The purchasing volume awarded by the Telefónica Group in 2005 rose to over 13 billion euros (12 billion in 2004). Its distribution by country saw Spain remaining the country with the greatest volume of purchases with Brazil in second position.

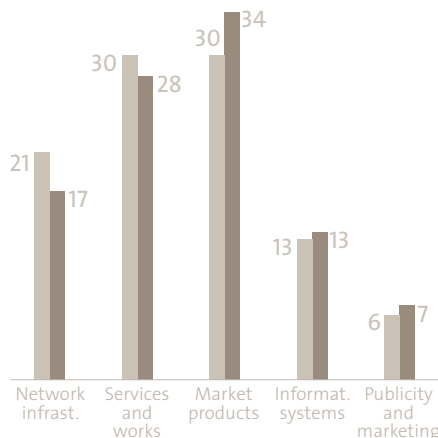
Said purchasing volume was awarded to over 18,834 suppliers throughout the world (15,539 in 2004). The ten main suppliers for the Telefónica Group worldwide were (in alphabetical order) Alcatel, Brightstar, Carat, Ericsson, IBM, Lucent, Motorola, Nokia, Siemens and Vitelcom.

Telefónica classifies its purchases into five major categories (network infrastructures, services and works, market products, information systems and advertising and marketing). Most of these are destined for the category of market products (including mobile terminals) which, together with the category of services and works, make up more than 60% of purchases. The remainder is distributed between network infrastructures, information systems and, to a lesser extent, advertising and marketing.

Telefónica is a company committed to the economic and social progress of the companies in which it is present. This commitment takes the form of a high percentage of awards to suppliers in the country itself, on average 90% in 2005 (92% in 2004).

Distribution of purchasing volume by product lines

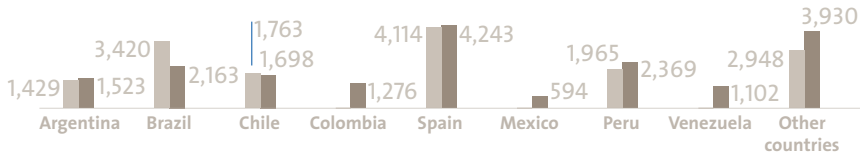
Data in percentages



¹ Data does not include Vivo or Telefónica companies in the Czech Republic.

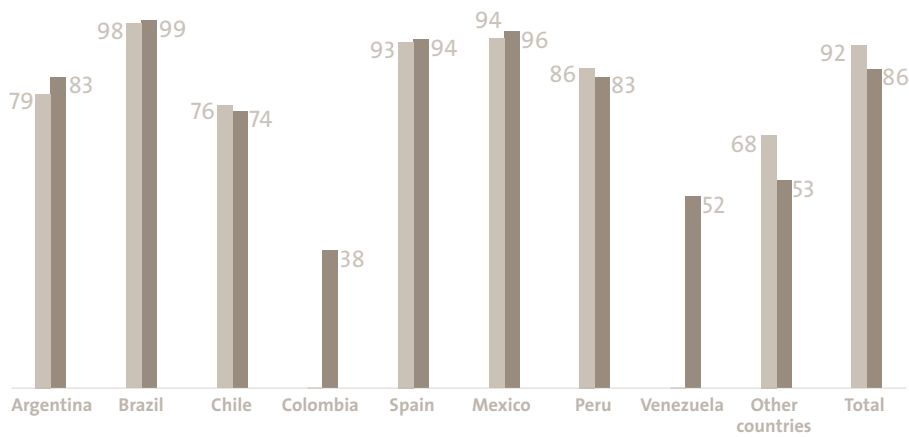
Distribution of awarded suppliers by country

Data in units



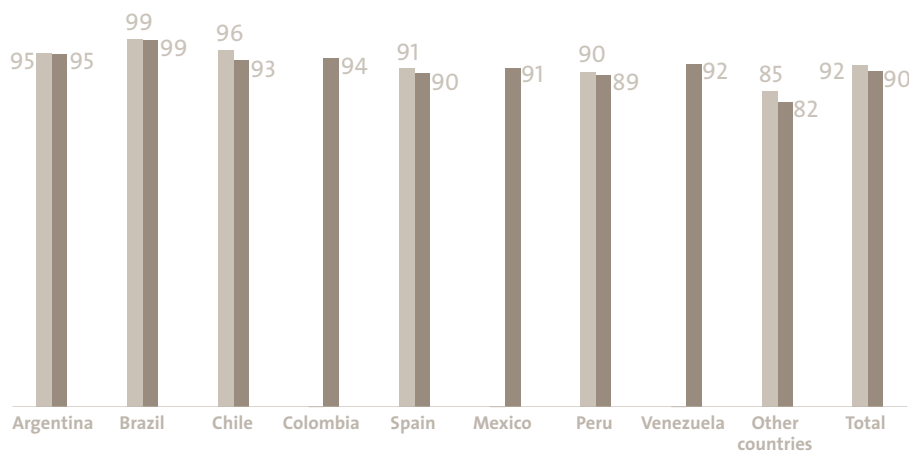
Distribution of local purchasing by country

Data in percentages



Local awards by country

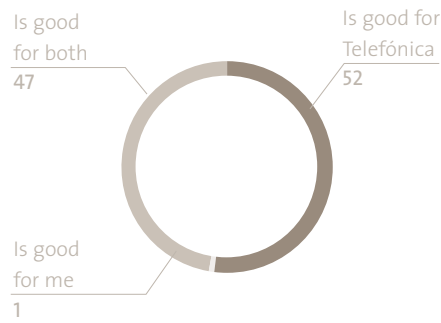
Data in percentages





Opinion of the supplier on the Telefónica purchasing model

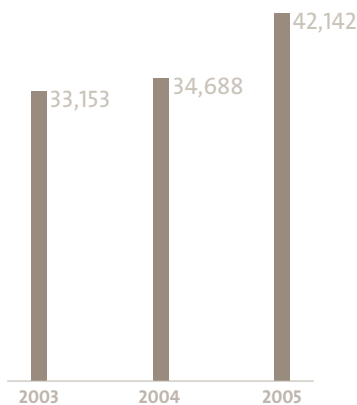
Data in percentages



Advanced purchasing Model

Suppliers registered in the Telefónica Catalogue suppliers

Data in units



Conscious of the importance of purchasing and relations with suppliers in business results, Telefónica handles purchasing in all its companies through a common management model: the Advanced Purchasing System (SAC). The goal of this model is to optimise purchases in its triple dimension of: price, quality and service, endeavouring to reduce costs, improve competitiveness and create value.

In December 2005, the purchases of 141 Group companies, distributed throughout the 19 main countries where Telefónica is present, were all managed through this model. The purchase process, according to the model, centres on Purchasing Boards, forums where the various areas involved analyse the purchase, establish their target prices for the same and finally decide unanimously on the award. There are currently nine Purchasing Boards located in Madrid, São Paulo, Rio de Janeiro, Lima, Buenos Aires, Santiago de Chile, México D.F., Bogotá and Caracas, enabling a global or local management of purchases depending on the most suitable model.

The Telefónica Purchasing Model has a series of features that facilitate objectivity and transparency:

- The opportunity for global registration in the Telefónica Catalogue of Suppliers is open to all those firms interested in working with Telefónica. This catalogue is valid for all the Group companies and registration is done through the Supplier website. At the end of 2005, there were 42,142 suppliers registered as possible bidders in the Telefónica Catalogue of Suppliers.

- All the areas affected by the purchase participate in the Purchasing Boards, and decisions are made unanimously.
- Telefónica has a Style Manual that describes the general principles and rules of conduct to be fulfilled by all those who participate in the purchase process. Among such principles, the most noteworthy is the equal opportunity afforded to all bidding suppliers.
- Furthermore, the e-business applications used and developed by the Telefónica Group also allow the automation and optimisation of the processes, as well as greater transparency in the management of suppliers' bids.

In Brazil, specifically, in compliance with resolution 155 of ANATEL, TeleSP is required to publicly advertise all its purchase processes for communication services and the acquisition of equipment valued over 1 million reales. For this reason, all public tenders are posted on the website to guarantee and encourage equal opportunity.

Distribution of Purchasing Volume by Product Lines

	e-Sourcing		Auctions	
	Purchasing volume (million euros)	N° Purchasing processes	Purchasing volume (million euros)	N° Purchasing processes
Argentina	755	2,303	49	126
Brazil	1,527	2,661	324	229
Chile	544	1,450	60	56
Spain	4,272	10,174	193	372
Mexico	506	870	8	27
Peru	492	3,154	52	138
Total	8.099	20.612	685	948

Electronic commerce

Telefónica uses the latest cutting-edge technology in its relationships with its suppliers to automate and optimise the entire purchase process and to establish new and better lines of communication with its suppliers.

In this respect, through Adquira España, Telefónica has already implemented a global ebusiness platform for the management of the purchase and supply process. Adquira España is a leading company in negotiation and supply of solutions and services, in which four large Spanish corporations hold stakes: BBVA, Iberia, Repsol-YPF and Telefónica. This e-business platform enables:

- The electronic management of bids and negotiation of same, as well as auctions (e-sourcing).
- The electronic preparation, approval and digital signature of commitments (contracts and award letters).
- The electronic management of goods and services orders by the relevant areas through catalogues previously negotiated by Purchasing Departments (e-procurement), dispatch of delivery notes by the supplier and acceptance of the goods or services at their destination.
- The supplier invoicing process from the orders placed and accepted electronically.

Electronic management of bids for certain products and services is currently a reality in Spain, Brazil, Argentina, Peru, Chile and Mexico. The purchasing volume negotiated in 2005 through the electronic market amounted to 8,264 millions of euro (399 in 2004), corresponding to 20,612 purchasing processes (12,675 in 2004).

The format of purchase negotiation through electronic auctions used since 2004 offers greater transparency and objectivity in the purchase process and full equal opportunity to all bidding suppliers, as well as making the process more agile and simplifying purchase management. In 2005, 685 million euros was awarded through this system, through 948 purchasing processes.

It is worth emphasising the significant improvement in results obtained for electronically negotiated purchases compared with conventional means.

Also, 2005 saw a continuance of the implementation of e-procurement in companies of the Telefónica in Spain, Brazil and Peru. An electronic invoicing solution was also implemented in Spanish companies. Finally, during 2005 an electronic contracts tool was setup in companies in Spain, Peru, Mexico, Colombia, Venezuela and Ecuador, involving 756 million euros

CASE STUDY

Supplier website

The Supplier Website, accessed at: www.telefonica.es/proveedores, is the main channel of information between Telefónica and its suppliers. It furnishes potential suppliers access to general information on how to become a Telefónica Group supplier, on Telefónica's purchase process and the main projects Telefónica is undertaking in relation to e-business.

Furthermore, registration in the Catalogue of Suppliers may also be handled through the Supplier Website, which also provides access to the Adquira e-business platform (primary operational channel for relations with suppliers). The website also includes access to other, specific websites for the Telefónica Group companies, such as e-Agora, from Telefónica de España.



Satisfaction surveys

Satisfaction surveys

Telefónica wishes to establish long term relationships with its suppliers, in which both Telefónica and its suppliers are satisfied. To assess the satisfaction levels of suppliers with Telefónica, in 2005 the first online survey was carried out, confidential and sent to all providers registered providers in the Telefónica catalogue.

Confidentiality of responses was guaranteed by using Atento intermediary suppliers and the absence of an individualised record of each response.

Over 2,700 response were received, forming a significant results base for Spain, Argentina, Brazil, Mexico, and Peru

Purchasing Model

The main strengths of the Telefónica purchasing model according to providers can be found in the establishment of an ethical and unambiguous purchasing process where the divisions involved have clearly defined roles and work in cooperation (7.4 points on a scale of 10 points).

The time spent on each purchasing model was seen by providers as an area which would be improved, although it was generally deemed adequate (6.6 points)

Electronic Commerce:

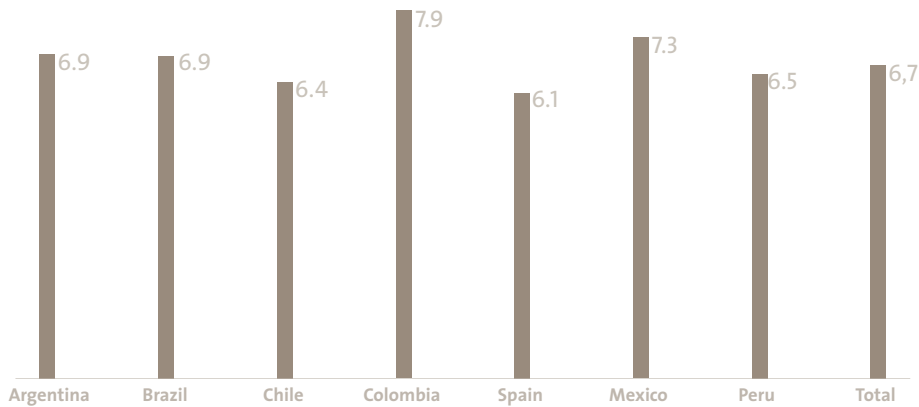
More than eight out of ten suppliers think that Telefónica e-commerce tools have added dynamism to the purchasing process (7.8) and greater transparency (6.8) and that they encourage competition and equality of opportunity between suppliers (7.4).

In relation to auctions, 51% of suppliers feel that products and services sold could be contracted through this negotiation model (5.6)

Most providers liked the idea of expanding e-commerce tools for electronic management of invoices (93% of suppliers like its implementation), for electronic management of orders (93%) and for electronic signing of contracts (88%).

Level of satisfaction of suppliers for the Telefónica Group

Data in units



The Purchaser

Purchasers had a high opinion of the suppliers' ethics and honesty (8.6) and its defence of the interests of Telefónica (8.8). Training as an interlocutor in the technical aspects of purchasing also received positive assessments (7.6)

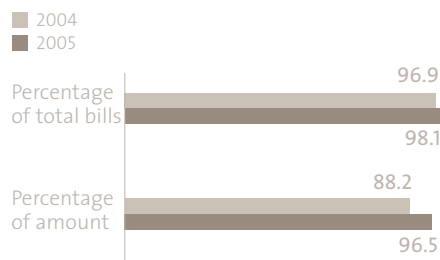
An area which could be improved (a mark of 6.6) is the purchaser's concern as to the quality of the product and not just the price, as well as a greater understanding of the situation of the suppliers in the negotiation (6.8 out of 10).

Administrative Processes

Fulfilment of Scheduled payment conditions to suppliers received positive assessments (7.8 out of 10)

Suppliers consider that there is a suitable communication process about purchasing outcome (7.8), although they request more information regarding the reasons in case of not being selected (5.6). Order placing in time and form received also positive assesment (6.6)

Compliance with payment terms for third party bills



Data corresponding to over 700,000 bills of Telefónica de España and Telefónica Móviles España for an amount over 9,389 million euros

Encouraging ethical standards

OPINION

What do suppliers think about Corporate Responsibility?
(from 0 to 5)

It is important for companies to exercise corporate responsibility 4,6

Generally, I would be very pleased to see Telefónica establish a purchasing code 4,5

I consider the activity the suppliers carry out should be considered 4,4

I consider that Telefónica requires compliance of minimum employment standards at an international level 4,2

The Telefónica Group endeavours to contribute to the encouragement of responsible business practises throughout its entire supply chain by its collaboration with other companies and in initiatives that go far beyond the legal requirements.

- In the case of suppliers from the telecom sector (typically “market product”, “network infrastructure” and “information systems” product lines”), of note is the company’s work with the GeSI supply chain working group.
- In the case of local and smaller suppliers (typically suppliers of “services and works”), Telefónica directly draws up specific conditions with its suppliers to ensure responsible behaviour by same.

As part of the supplier satisfaction study, they were asked about the appropriateness of introducing corporate responsibility codes and standards, a proposal which received a high level of acceptance among Telefónica suppliers.

GeSI Supply Chain Working Group

Many companies in the ICT sector (Information and Communications Technology) share the same suppliers throughout the world. Aware of the fact that joint actions carried out by several companies are more effective than the same carried out individually, in 2003 GeSI (www.gesi.org) established a working group on the supply chain. This was unique in that both Telefónica and O2 participated in same.

Said working group has been collaborating since 2004 with a range of American companies, signatories to the EICC, “Electronic Industry Code of Conduct”, with the aim of cooperating with a wider range of companies and thus ensuring more effective action.

The main achievements of this working group in 2005 were:

- Drawing up a methodology for the identification of risks associated with the RSC in the supply chain, based on products and services, size and location of supplier facilities.
- Development of a self assessment questionnaire for suppliers, so that they can indicate their level of compliance with employment, ethical, health and safety standards. Said questionnaire was published in English, Spanish and Mandarin in 2005.
- Design of an etool so that different industry suppliers and purchasers can fill in questionnaires, with clear savings of time and effort for the whole sector. Said tool should be implemented in 2006.
- Establishment of tools to audit the performance of companies, with respect to the declarations made in their self assessment questionnaires.

Requirements of suppliers in employment and human rights matters

In the General Conditions for the Supply of Goods to Telefónica SA, Telefónica requires compliance of legislation in force in relation to employment conditions, health and safety at the workplace and the environmental impact of its suppliers.

Criteria are of general application, notwithstanding the possibility of additional criteria in some countries or companies. Likewise, in the case of specific products and services, contracts may include additional aspects more directly related to the product or service being purchased.

Additionally, as a measurement of improvement deriving from the employment audit in the Telefónica Group and the risks detected in same, in 2005 Joint Corporate Action Criteria for the Control of Employment risks in the Contracting of Works and Services were drawn up and approved.

This is an internal regulation which includes:

- A list of pre-contract requirements (standardisation of suppliers and contracts)
- A list of the information to be provided at the beginning of the contract
- Obligations in matters of prevention of employment risk for the main company and the contracting company.
- Obligations in matters of information to be given to legal representatives of workers.
- Measures to be adopted during the contractual period
- Measures to be adopted after the termination of the contract
- Supervision and control mechanisms

Another of the corrective measures taken during 2005 was the obligation of training in Human Rights for employees of the security companies that work for Telefónica.

Requirements of suppliers in environmental matters

The most notable initiatives in environmental matters are described in chapter 08 of this report. They include training activities for employees of collaborating companies, the positive weighting given to environmental management certificates in the contract award phase or activities of evaluation and control of suppliers having an environmental impact.

Requirements of suppliers in matters of equality of opportunities

As a notable initiative in terms of integration, Telefónica requires compliance with the Law on Integration of Disabled persons of all suppliers who render services in District C. For those companies which do not comply with requirements, the ATAM Employment Integration Service is offered.

In 2006, Telefónica aims to establish a policy of purchasing from “social or minority” suppliers which may involve groups which have traditionally had difficulty accessing the employment market.

Credits

Departments that collaborated in the preparation of the report

Capítulo	Áreas implicadas
01 Corporate Governance	Secretariat General / Internal Auditing Department
02 Identity	Communication (Brand, Reputation and CSR) / Human Resources Office / Sponsorship / Internal Auditing Department
03 Driving Force for Progress	Finance (Consolidation, Management Control), Tax, Regulatory Affairs, Innovation, Telefónica I+D, Institutional Relations, Information Systems, Investor Relations
04 Customers	Corporate Marketing Development / Quality, marketing and customer service departments of the main business lines (Telefónica de España, Telefónica Móviles, Telefónica Latinoamérica) / Secretariat General / Communication / Security
05 Shareholders	Shareholders' Office / Investor Relations / Secretariat General
06 Employees	Corporate Human Resources / Human Resources Departments of the main lines of business (Telefónica de España, Telefónica Móviles, Telefónica Latinoamérica, TPI, Terra, Atento, T-Gestiona) / Communication / Health and Safety / Fundación Telefónica / ATAM / Fonditel
07 Society	Main lines of business (Telefónica de España, Telefónica Latinoamérica, Telefónica Móviles) / Institutional Relations / Management Control / Regulatory Affairs / Reputation and Corporate Social Responsibility / Fundación Telefónica / ATAM / Sponsorship
08 Environment	Internal Auditing / Reputation and Corporate Social Responsibility / Environmental Departments of the main lines of business (Telefónica de España, Telefónica Móviles, Telefónica Latinoamérica)
09 Suppliers	Purchasing / Internal Auditing / Reputation and Corporate Responsibility
10 Media	Communication
Annex 1: About the Report	Reputation and Corporate Responsibility
Annex 2: Verification Report	Ernst&Young. Report
Coordination	Reputation, Brand and Corporate Social Responsibility (G.D. of Communication)

