REPORT BY THE EXECUTIVE COMMITTEE OF THE BOARD OF DIRECTORS OF TELEFÓNICA, S.A. ISSUED ON 30 JULY 2014, IN RELATION TO THE RESOLUTION TO ISSUE MANDATORILY CONVERTIBLE AND/OR EXCHANGEABLE NOTES AND WARRANTS, EXCLUDING THE PREFERENTIAL SUBSCRIPTION RIGHT, PURSUANT TO THE AUTHORITY GRANTED BY THE ORDINARY GENERAL SHAREHOLDERS' MEETING HELD ON 30 MAY 2014 (POINT IV OF THE AGENDA)

1. PURPOSE OF THE REPORT

The present report is drafted by the Executive Committee of the Board of Directors of Telefónica, S.A. ("**Telefónica**", the "**Company**" or the "**Issuer**"), pursuant to the provisions of Articles 414, 417 and 511 of the Restated Spanish Companies Act (*texto refundido de la Ley de Sociedades de Capital*) (the "**Spanish Companies Act**" or "**LSC**") in relation to the resolution to issue notes which are mandatorily convertible into and/or exchangeable for shares in Telefónica for a maximum face value amount of one billion, five hundred million (1.5 bn) euros and an issue of warrants also over shares in Telefónica, excluding in both cases the preferential subscription right held by shareholders, and the corresponding share capital increase in the amount necessary to fulfil the respective conversion and/or acquisition rights (the "**Issue**"). The Issue has been approved by the Executive Committee pursuant to the powers conferred by virtue of the resolution adopted under point IV of the Agenda of the Ordinary General Shareholders' Meeting held on 30 May 2014, delegating to the Board of Directors, with powers of substitution, the authority to issue notes and other debt instruments, and pursuant to the powers conferred on the same date by the Board of Directors, thereby delegating such authority to the Executive Committee.

Article 414 LSC mentioned above permits Spanish joint stock companies (*sociedades anónimas*) to issue notes which can be converted into shares, provided that the General Meeting determines the basis and methods for the conversion and resolves to increase the share capital by the amount necessary. To do so, the administrators must draft a report explaining the conversion basis and methods, which must be submitted together with another report by an auditor, other than the auditor of the company's accounts, appointed for this purpose by the Mercantile Registry. And Article 417 LSC, in turn, permits the General Meeting to resolve to exclude the preferential subscription right held by the shareholders in issues of convertible notes, requiring for this purpose -among other requirements- that the administrators' report justify the proposal in detail and that the auditor's report pronounce on the admissibility of the data included in the administrators' report and on the suitability of both the conversion relationship and its adjustment formulas to offset a potential dilution of the financial stake held by the shareholders.

With regard to listed companies, as is the case of Telefónica, Article 511 LSC also permits the General Meeting to delegate to the administrators, together with the power to issue convertible notes, the additional power to exclude the preferential subscription right in relation to any issues whose adoption may be resolved, when the company's interests so require. For these purposes, both the administrators' report and the auditor's report mentioned above must refer to each specific issue carried out under the corresponding delegation of authority by the General Meeting. These reports will be made available to the shareholders and announced at the first General Meeting held following the adoption of the resolution to carry out the issue.

The same requirements likewise apply to other similar securities, such as in the particular case of warrants (rights to acquire shares).

The purpose of the present report is to fulfil the above-mentioned requirements.

2. THE ISSUE OF CONVERTIBLE AND/OR EXCHANGEABLE NOTES AND WARRANTS

2.1 Delegations of authority by the General Meeting and the Board of Directors pursuant to which the Issue is carried out

The Ordinary General Shareholders' Meeting of Telefónica, held on 30 May 2014, adopted the following resolution under point IV of the Agenda:

"To delegate to the Board of Directors, according to the general regime on bond issues, and pursuant to the provisions of Articles 285, 297 and 417 of the Spanish Companies Act (Ley de Sociedades de Capital) and 319 of the Mercantile Registry Regulations (Reglamento del Registro Mercantil), the authority to issue, on one or more occasions, debentures, bonds, promissory notes, and other fixed income securities or debt instruments similar in nature (including warrants), or hybrid instruments (including, among others, preferred stock), convertible into and/or exchangeable for shares, according to the following conditions:

1. *The issue of the indicated securities may be made on one or more occasions, at any time, within the maximum period of five years as from the date of adoption of the present resolution.*

2. *The securities issued may be debentures, bonds, promissory notes and other fixed income securities, or debt instruments similar in nature, or hybrid instruments in any of the forms admitted by law, both simple as well as, in the case of bonds, notes and hybrid instruments, convertible into shares in the Company and/or exchangeable for shares in the Company, in any of the companies of its Group or in any other company. This delegation also includes warrants or other similar securities which may directly or indirectly entitle the subscription or acquisition of new or existing shares in the Company, and which may be paid for by physical delivery or by offset.*

3. *The aggregate amount of the issue(s) of securities resolved pursuant to this delegation cannot exceed, at any time, 25 billion euros or its equivalent in another currency. In the case of promissory notes, the outstanding balance of those securities issued pursuant to the delegation will be calculated for the purposes of the above-mentioned limit. Also for the purposes of said limit, in the case of the warrants, the sum of the premiums and exercise prices for the warrants for each issue approved pursuant to the present delegation will be taken into account.*

4. *The delegation will include establishing the different aspects and terms and conditions of each issue (face value, issue price, redemption price, currency of the issue, interest rate, amortization, anti-dilution mechanisms, adjustments to the conversion price due to the payment of dividends, the circumstance of being mandatorily or voluntarily convertible and/or exchangeable securities, even on a contingent basis and, if voluntarily, at the option of the securities' holder or issuer, subordination clauses, issue guarantees, place of issue, listing on the securities market, applicable legislation, etc.).*

5. *For the case of the issue of convertible and/or exchangeable securities, and in order to determine the basis and methods of the conversion and/or exchange, it was resolved that the following criteria be established:*

   a) *The securities issued pursuant to this resolution may be converted into new shares in the Company and/or exchanged for existing shares in the Company, in any of the companies of its Group or in any other company, according to a fixed (determined or determinable) or variable conversion and/or exchange ratio, and the Board of Directors will have the authority to decide if they are convertible and/or exchangeable, and to determine if they are mandatorily or voluntarily convertible and/or exchangeable, even on a contingent basis, and, if voluntarily, at the option of the holder thereof or issuer, with the frequency and during the maximum period established in the resolution for the issue.*

   b) *Normally, the conversion and/or exchange ratio will be fixed, and for this purpose, the fixed income securities will be valued at their face value amount and the shares at the fixed exchange rate determined in the resolution of the Board of Directors, or at the exchange rate determinable on the date(s) indicated in the Board resolution itself, and according to the price of the Company's shares* *on the Securities Market on the date(s) or during the period(s) taken as a reference in the same resolution. In any event, the price of the shares for the purpose of the conversion and/or exchange cannot be less than the arithmetic mean of the closing prices, the weighted average price or another reference for the price of the Company's shares on Spain's Continuous Market during the period to be determined by the Board of Directors, which cannot be more than three months nor less than three days, prior to: (i) the date of the meeting of the Board of Directors which, pursuant to the present delegation, approves the issue of the securities, or (ii) a specific date falling between the date the issue is announced and the date the securities are disbursement by the subscribers (both inclusive). Furthermore, a premium or a discount, as the case may be, could be established on said price per share; although if a discount is applied to the price per share, this cannot exceed 25% of the value of the shares used as a benchmark, pursuant to the above. In the event of an exchange for shares in another company (of the Group or not), the same rules will apply, to the extent they are appropriate and with any necessary adaptations or adjustment, as the case may be, except that they will refer to the price of the shares in said company on the corresponding market.*

c) Notwithstanding the provisions of paragraph b) above, it may be resolved to issue the securities using a variable conversion and/or exchange ratio. In this case, the share price for the purpose of the conversion and/or exchange will be the arithmetic mean of the closing prices, the weighted average price or another benchmark for the price of the Company's shares on Spain's Continuous Market during a period to be determined by the Board of Directors, not more than three months nor less than three days prior to the conversion and/or exchange date, with a premium or a discount, as the case may be, on said price per share. The premium or discount *may be different for each conversion and/or exchange date of each issue (or each tranche of an issue, as appropriate), although if a discount is applied to the price per share, this cannot be more than 30%.*

This notwithstanding, in the terms to be decided by the Board, a minimum and/or maximum benchmark price for the shares could be established, as limits, for the purpose of their conversion and/or exchange. In the event of an exchange for shares in another company (of the Group or not), the same rules will apply, to the extent they are appropriate and with any necessary adaptations or adjustments, as the case may be, except that they will refer to the price of the shares in said company on the corresponding market.

d) Pursuant to the provisions of Article 415 of the Spanish Companies Act, bonds cannot be converted into shares when their face value is lower than the value of the shares. Furthermore, convertible notes cannot be issued for an amount lower than their face value.

e) When the conversion and/or exchange is to be carried out, any fractions of shares which are to be delivered, as the case may be, to the holder of the securities being converted and/or exchanged, these will be rounded down by default to the whole number immediately below, and each holder will receive in cash any difference which may be produced in this case.

f) When an issue of convertible and/or exchangeable securities is approved according to the authorisation contained in the present resolution, the Board of Directors will issue a report by the Administrators setting out and specifying, using the above-described criteria, the basis and methods of conversion specifically applicable to the issue in question. This report will be submitted together with *the corresponding Auditors' report indicated in Article 414 of the Spanish Companies Act.*

6. *In any event, the delegation for the issue of convertible and/or exchangeable securities will include:*

   a) *The power to increase the capital by the amount necessary to fulfil the conversion requests. Said power can only be exercised to the extent that the Board – adding together the capital increases effected to accommodate the issue of convertible securities and any other capital increase it may have resolved to effect, pursuant to authorisations granted by the shareholders at General Shareholders' Meetings - does not exceed the limit of half of the share capital figure established in Article 297.1 b) of the Spanish Companies Act, nor 20% of such total amount of share capital, if the issue of the convertible securities excluded the pre-emptive rights of the shareholders. This authorisation to increase the capital includes the authority to issue, on one or more occasion, the shares necessary to carry out the conversion, as well as the authority to amend the article of the corporate by-laws in relation to the amount of share capital.*

   b) *The power to partly or totally exclude the shareholders' preferential subscription right, when necessary in order to raise funds in national or international markets, in order to use bookbuilding technique, or as otherwise required by the corporate interest. In any event, if the Board were to decide to exclude the preferential subscription right in relation to a specific issue of convertible securities which it eventually decided to carry out pursuant to the present authorisation, it will issue a report, simultaneously to approving the issue, giving details on the specific reasons in the Company's interest which justify this measure, which will be the subject of the correlative report by an auditor, other than the*

Company's auditor, appointed for this purpose by the Mercantile Registry, as indicated in Article 417.2 a) and b) of the Spanish Companies Act. Both reports will be made available to the shareholders and will be announced at the first General Meeting held following the adoption of the resolution for the issue.

c) *The power to develop the basis and methods of conversion and/or exchange established in point 5 above and, in particular, the power to determine the time of the conversion and/or exchange, which can be restricted to a predetermined period, the circumstance of being securities which are mandatorily or voluntarily convertible and/or exchangeable, even on a contingent basis, and, if voluntarily, at the option of the holder of the securities or the issuer, the manner of paying the holder of the securities (by conversion, exchange or even a combination of both techniques, which the issuer can choose at the time of execution) and, in general, any specifications or conditions necessary or appropriate for the issue.*

7. *As long as the conversion into and/or exchange for shares of the convertible and/or exchangeable securities issued in exercise of the power hereby delegated is possible, their holders will have any rights acknowledged to them under the applicable regulations.*

8. *The Board of Directors is likewise authorised to guarantee, on the Company's behalf, the issue of the securities mentioned in point 2 above, issued by the Companies belonging to its Group of Companies.*

9. *At the subsequent General Meetings held by the Company, shareholders will be informed of the use made up to that time, as the case may be, of the delegation of powers referred to in the present resolution.*

10. *Convertible warrants: The rules established in the preceding paragraphs will apply, mutatis mutandis, in the case of the issue of warrants or other*

similar securities which may give rise, directly or indirectly, to the subscription of new shares in the Company, with the delegation containing the broadest powers, with the same scope as in the preceding paragraphs, for deciding all matters it deems appropriate in relation to said class of securities.

11. *Whenever appropriate, the Company will request the listing, when appropriate, on domestic or foreign, official or unofficial secondary markets, organised or not, of the bonds, notes and other securities issued by virtue of this delegation, empowering the Board to take the steps and actions necessary for such listing, before the competent bodies of the various Spanish or foreign securities markets.*

It is expressly noted for the record that, in the event that the de-listing of the securities issued by virtue of this delegation is subsequently requested, the de-listing will be adopted with the same formalities as the request for listing, to the extent applicable, and, in that case, the interests of the shareholders or noteholders who oppose the resolution or do not vote on it will be guaranteed, fulfilling the requirements established in the Spanish Companies Act and related provisions, pursuant to the provisions of the Spanish Securities Market Act (Ley del Mercado de Valores) and its implementing provisions. Furthermore, it is expressly declared that the Company is subject to the existing rules or those which could be established in the future on the Securities Markets and, in particular, on securities trading, maintenance of the listing and de-listing.

The Board of Directors is authorised to delegate, in turn, in favour of the Executive Committee (pursuant to the provisions of Article 249, number 1, of the Spanish Companies Act) the delegated powers referred to in the present resolution.

Any unused parts of the delegation for the issue of securities granted by the General Shareholders' Meeting of the Company at its meeting held on 31 May 2013 will be rendered without effect."

The Board of Directors of Telefónica, at its meeting also held on 30 May 2014, likewise adopted (among others) the following resolution:

"*To delegate to the Executive Committee, pursuant to the delegation made, in turn, in favour of the Board of Directors, according to the resolution adopted by the General Shareholders' Meeting held on 30 May 2014 and included under Point IV of the Agenda, the power to issue bonds, notes, promissory notes and other fixed income securities and hybrid instruments, including preferred stock, in all cases simple, exchangeable and/or convertible; attributing, in this latter case, the power to exclude the shareholders' preferential subscription right and the power to guarantee the issues of the companies of the Group, according to the conditions established in the expressed resolution*".

According to the foregoing, the Executive Committee has the authority to resolve to issue securities which can be converted into shares and, in relation thereto, the authority to carry out an issue of warrants, as well as the additional power to exclude the preferential subscription right of the shareholders with regard to both securities, when the Company's interests so require.

2.2 Description and context of the Issue

Based on the above delegations, the Executive Committee has decided to approve, on this same date, the Issue, for a maximum face value amount of one billion, five hundred million (1.5 bn) euros, excluding the preferential subscription right held by Telefónica's shareholders, as well as the corresponding share capital increase by the amount necessary. The Issue will be implemented by means of two related issues made by Telefónica: (i) one issue of notes mandatorily convertible into and/or exchangeable for shares in Telefónica, S.A. (the "**Convertible Notes**"), and (ii) one issue of warrants over shares in Telefónica, S.A. (the "**Warrants**"); both issues will be subscribed by

Telefónica Participaciones, S.A. or by another subsidiary company 100% owned by it (the "**Subsidiary**"). And simultaneously, the Subsidiary will make another issue of notes mandatorily convertible into and/or exchangeable for shares in Telefónica, S.A. (the "**Indirectly Convertible Notes**"), with terms and conditions which substantially coincide with those of the Convertible Notes and the Warrants, which will be placed on the international market among qualified investors.

Telefónica, S.A. is a Spanish company, incorporated for an indefinite period of time, with Fiscal Identification Number (C.I.F.) A-28/015865 and registered address at Gran Vía nº 28, Madrid (Spain), recorded at the Mercantile Registry of Madrid in Tome 12.534, Folio 21, Sheet M-6164, under Entry no. 1359.

The Company's share capital totals 4,551,024,586 euros (FOUR BILLION, FIVE HUNDRED AND FIFTY-ONE MILLION, TWENTY-FOUR THOUSAND, FIVE HUNDRED AND EIGHTY-SIX EUROS), divided into 4,551,024,586 ordinary shares, each with a face value of 1 euro.

The Company's corporate object can be found in its financial statements as at 31 December 2013 and in its corporate by-laws, which can be consulted on the Company's website (http://www.telefonica.com).

The execution of the Issue using an indirect structure, in which the Subsidiary issues and places the Indirectly Convertible Notes among investors and in which Telefónica undertakes, through the Convertible Notes and the Warrants, to issue and directly deliver to said investors, on behalf of the Subsidiary, those shares which correspond to them under the conversion, is designed to optimise the financial advantages of the transaction and, as a result, the benefit to Telefónica's corporate interest.

The execution of the Issue in the current economic and financial context is fundamental in order to diversify the Company's sources of funding, taking advantage of opportunities arising, so as to secure new resources as alternatives to bank financing. In order to be in a position to benefit from these financing opportunities, it is essential that any transaction to be carried out be done rapidly, avoiding exposure to the markets' high volatility. In this regard, the Company has identified the existence of a possible interest among qualified investors for the subscription of notes which are convertible into and/or exchangeable for shares in the Company. The Executive Committee considers that the most suitable way to take advantage of this interest and to obtain financing with the best financial conditions possible, in the interest of the Company and all of its shareholders, is by using the accelerated bookbuilding mechanism, as is customary in issues of convertible securities.

In the Executive Committee's opinion, the offering and placement of the Indirectly Convertible Notes among qualified investors (and the corresponding "internal" issue of the Convertible Notes and the Warrants in favour of the Subsidiary) results in the most suitable financing procedure for the Company, given the current circumstances, for the following reasons:

(i) the issue of convertible and/or exchangeable notes allows it to continue its process of diversifying the Company's sources of financing, since investors in convertible and/or exchangeable notes constitute a different and alternative source of funds, compared to both bank financing and equities and fixed income securities investors; and

(ii) notes which are mandatorily convertible and/or exchangeable, such as those included in the Issue represent, in financial terms, a deferred mechanism for the issue of shares and the increase of capital, which should enable the Company to build up its equity and reduce its degree of financial leveraging.

In order to execute the Issue, the Company will contract the services of one or more financial entities to carry out an accelerated bookbuilding process on the Indirectly Convertible Notes among qualified investors. The intention is to obtain, through this process, an indication of the interest in Indirectly Convertible Notes and, depending on the results, to set the definitive terms of the Issue, including those of the Convertible Notes and the Warrants.

It is noted for the record that the conditions of the Issue, as well as the Company's ability to formalise it, are in line with the provisions of the Spanish Companies Act and the Company's corporate by-laws, and that the conversion basis and methods are in line, as will be explained below, with the basis and methods determined by the resolution of the General Meeting of 30 May 2014 which approved the delegation to the Board of Directors, with powers of substitution, of the power to issue convertible and/or exchangeable bonds or notes and warrants, among other securities.

2.3 Basis and methods of the conversion or exchange

2.3.1. As stated, the Issue will be implemented by means of the placement, among qualified investors, of the Indirectly Convertible Notes issued by the Subsidiary, which will be convertible into shares in Telefónica, and whose main basis and methods are as follows:

(a) Amount of the issue

The maximum face value amount of the issue of the Indirectly Convertible Notes is 1.5 billion euros, although the definitive amount will be established once the accelerated bookbuilding process has concluded, as is usual practice in these types of transactions. The possibility of making an incomplete subscription is expressly foreseen.

(b) Face value and issue type

The Indirectly Convertible Notes will have a face value per unit of 100,000 euros and will be issued at 100% of their face value, as a minimum.

(c) Interest rate

The Indirectly Convertible Notes will accrue annual fixed interest payable yearly in arrears, at a rate of between 4% and 5.5%. The final interest rate will be determined by mutual accord between the Company and the Lead Managers, depending on the outcome of the bookbuilding process.

(d) Maturity and mandatory conversion into shares in Telefónica, S.A.

The Indirectly Convertible Notes will mature on the third anniversary of the date of their issue (the "**Maturity Date**"). On the Maturity Date, the Indirectly Convertible Notes will be mandatorily converted into shares in Telefónica, S.A., and for this purpose, Telefónica will issue and deliver the corresponding shares to the holders of the Indirectly Convertible Notes, on behalf of the Subsidiary. The Company will have the option of carrying out the conversion of the Indirectly Convertible Notes by means of the delivery of new shares, existing shares or a combination of both.

(e) Price and conversion or exchange ratio

The reference price of the shares in Telefónica, S.A., for the purpose of the conversion or exchange of the Indirectly Convertible Notes, will be calculated using an accelerated bookbuilding process of shares in Telefónica which the Lead Managers of the Issue could carry out on the same day as the Issue launch date (with no intervention whatsoever by Telefónica or the Subsidiary) or, failing that, using a different price-setting mechanism to determine the minimum conversion price. The maximum conversion price, in turn, will include a premium on the minimum price, consisting of an estimated percentage of between 20% and 25%, which will be determined by mutual agreement between the Company and the Lead Managers of the Issue, depending on the outcome of the bookbuilding process.

In any event, the conversion price thus set cannot be lower than the average share price on the trading day on which the Issue is announced, with a discount, as the case may be, which cannot exceed 25% of the resulting value, according to the minimum conversion basis and methods established in the resolution of the Ordinary General Shareholders' Meeting whereby the Board was delegated the authority to issue convertible bonds, but in no case permitted to issue the shares for an amount lower than their face value, pursuant to Article 59.2 of the Spanish Companies Act.

The number of shares to be delivered to the holders of the Indirectly Convertible Notes will be determined by dividing the face value amount of the shares by the applicable conversion price, according to the average share price for the Telefónica shares, during the twenty trading days prior to the third trading day falling before the Maturity Date, with the limit of the above-mentioned minimum and maximum prices in any event.

Anti-dilution mechanisms will be established on the conversion price, as is standard practice in these kinds of transactions, as determined in the terms and conditions of the Indirectly Convertible Notes.

(f) Accelerated conversion

The Indirectly Convertible Notes will be converted in advance upon the occurrence of certain events (such as if the Company's credit rating were downgraded, or if the Company or the Subsidiary were to breach their terms and conditions), and they may also be converted in advance at any time, at the Subsidiary's discretion, during the conversion period established.

The holders of Indirectly Convertible Notes may likewise choose to convert them in advance during the voluntary conversion period, or if certain circumstances arise (such as the launch of a takeover bid over the Company or a change of control), under different conversion conditions in each case.

(g) Applicable law

The Indirectly Convertible Notes will be subject to Spanish law with regard to: (i) their legal status and credit ranking, (ii) the capacity of the Subsidiary and of the Company, as well as the corresponding corporate resolutions, and (iii) the creation of the Syndicate of Noteholders and the appointment of its Commissioner. Except as provided above, the terms and conditions of the Indirectly Convertible Notes (including the non-contractual obligations) will be governed and construed in accordance with UK law.

(h) Listing

A request will be made to list the Indirectly Convertible Notes on a regulated secondary market, multilateral trading system or other organised market, such as the *Freiverkehr* of the Frankfurt Stock Exchange.

(i) Guarantees

The Indirectly Convertible Notes will have the general guarantee of the Subsidiary's assets, as well as a subordinate guarantee from Telefónica (in addition to Telefónica's personal obligation to issue and deliver, on behalf of the Subsidiary, the corresponding shares to the holders of the Indirectly Convertible Notes upon conversion).

2.3.2. Internally, as has been indicated, the Issue will be implemented by means of the issue by Telefónica of the Convertible Notes and the Warrants, which will be subscribed by Telefónica Participaciones, S.A. (or by another subsidiary 100% owned by Telefónica), in order to provide proper coverage by Telefónica to the issue of the Indirectly Convertible Notes and, in particular, to the issue of the shares necessary to enable their conversion. Specifically, the Convertible Notes refer to the minimum number of shares which Telefónica must issue under the Indirectly Convertible Notes in the event that the maximum conversion price applies, whereas any Warrants issued simultaneously would cover any additional shares to be issued by Telefónica under the Indirectly Convertible Notes, up to the limit resulting from the minimum conversion price, in any event.

The basis and methods for the conversion of the <u>Convertible Notes</u> are as follows:

(a) Amount of the issue

The maximum face value amount of the issue of the Convertible Notes is 1.5 billion euros, although the definitive amount will be established once the accelerated bookbuilding process of the Indirectly Convertible Notes has concluded, as is usual practice in these types of transactions. The possibility of making an incomplete subscription is expressly foreseen.

(b) Face value and issue type

The Convertible Notes will have a face value per unit of 100,000 euros and will be issued at 100% of their face value, as a minimum.

(c) Interest rate

The Convertible Notes will accrue annual fixed interest payable yearly in arrears, at a rate of between 4% and 5.5%. The final interest rate will be determined by mutual agreement between the Company and the Lead Managers, depending on the outcome of the bookbuilding process of the Indirectly Convertible Notes.

(d) Maturity and mandatory conversion into shares in Telefónica

The Convertible Notes will mature on the third anniversary of the date of their issue (the "**Maturity Date**"). On the Maturity Date, the Convertible Notes will be mandatorily converted into and/or exchanged for shares in Telefónica, S.A., and for this purpose, Telefónica will issue and deliver the corresponding shares to the holders of the Indirectly Convertible Notes, on behalf of the Subsidiary.

(e) Price and conversion or exchange ratio

The reference price of the shares in Telefónica for the purpose of the conversion or exchange of the Convertible Notes (the "**Conversion Price**") will be the same as that established for the Indirectly Convertible Notes, depending on the outcome of the accelerated bookbuilding process carried out on them by the Lead Managers of the Issue. The conversion price of the Convertible Notes will correspond in any event to the maximum conversion price of the Indirectly Convertible Notes, and will therefore include a premium on such reference price, consisting of an estimated percentage of between 20% and 25%.

In any event, the conversion price thus set cannot be lower than the average share price on the trading day on which the Issue is announced, with a discount, as the case may be, which cannot exceed 25% of the resulting value, according to the minimum conversion basis and methods established in the resolution of the Ordinary General Shareholders' Meeting whereby the Board was delegated the authority to issue convertible bonds, but in no case permitted to issue the shares for an amount lower than their face value, pursuant to Article 59.2 of the Spanish Companies Act.

The number of shares to be issued under the Convertible Notes, for delivery to the holders of the Indirectly Convertible Notes, will be determined by dividing the face value amount of the Convertible Notes by the applicable conversion price.

Anti-dilution mechanisms will be established on the conversion price, as is standard practice in these kinds of transactions.

(f) Accelerated conversion

The Convertible Notes will be converted in advance, if the same circumstances exist as for the Indirectly Convertible Notes. In particular, they will be converted in advance upon the occurrence of certain events (such as if the Company's credit rating were downgraded, or if the Company or the Subsidiary were to breach their terms and conditions), and they may also be converted in advance at any time, at the Company's discretion, during the conversion period established.

The Subsidiary, as holder of the Convertible Notes, may likewise choose to convert them in advance during the voluntary conversion period, or if certain circumstances arise (such as the launch of a takeover bid over the Company or a change of control), under different conversion conditions in each case.

(g) Applicable law

The Convertible Notes will be subject to Spanish law with regard to: (i) their legal status and credit ranking, (ii) the capacity of the Company as well as the corresponding corporate resolutions, and (iii) the creation of the Syndicate of Noteholders and the appointment of its Commissioner. Except as provided above, the terms and conditions of the Convertible Notes (including the non-contractual obligations) will be governed and construed in accordance with UK law.

2.3.3. In relation to the Warrants, their main terms and the basis and methods of the acquisition right inherent to them are as follows:

(a) Characteristics and rights

The Warrants will be issued simultaneously to the Convertible Notes, in the form of one warrant for each convertible note. Therefore, they will be issued without a premium and in exchange for the subscription of the Convertible Notes.

(b) Maturity date

The Warrants will mature on the third anniversary of the date of their issue (the "**Maturity Date**").

(c) Underlying shares

The Warrants will entitle, but not oblige, their holders to receive new or existing shares in Telefónica, which, in the event the Warrants are exercised, will be delivered directly to the holders of the Indirectly Convertible Notes, on behalf of the Subsidiary.

The initial maximum number of shares to be issued under the Warrants will be equal to a percentage of between 16.6667% and 20% of the maximum number of shares to be delivered to Telefónica under the Indirectly Convertible Notes (subject to the corresponding adjustments).

Any shares issued under the Warrants, as the case may be, will be disbursed by offsetting credits against the amount received by the Company for the subscription of the Convertible Notes and the Warrants, pursuant to the provisions of Article 302 LSC. The shares will be issued at the applicable conversion price under the Indirectly Convertible Notes, with the same limits as established for them.

(d) Conditions of exercise

The Warrants will be exercised in the event that the conversion of the Indirectly Convertible Notes occurs at a price lower than the maximum conversion price, in relation to the number of shares necessary in each case and with the limit resulting from the minimum conversion price of the notes in question.

The Warrants may be exercised in advance, if the same scenarios and circumstances exist as for the Indirectly Convertible Notes. In particular, they will be exercised in advance upon the occurrence of certain events (such as if the Company's credit rating were downgraded, or if the Company or the Subsidiary were to breach their terms and conditions). The Subsidiary may likewise choose to exercise them in advance, if the Indirectly Convertible Notes are converted in advance or if certain circumstances exist (such as the launch of a takeover bid over the Company or a change of control).

Anti-dilution mechanisms will be established on the exercise price, as is standard practice in these kinds of transactions.

(e) Applicable law

The Warrants will be subject to Spanish law with regard to: (i) their legal status, the capacity of the Company and the corresponding corporate resolutions. Except as provided above, the terms and conditions of the Warrants (including the non-contractual obligations) will be governed and construed in accordance with UK law.

3. GROUNDS FOR THE EXCLUSION OF THE PREFERENTIAL SUBSCRIPTION RIGHT

3.1 Background

As indicated above, the Ordinary General Shareholders' Meeting of Telefónica held on 30 May 2014, upon resolving to delegate powers to the Board of Directors to issue securities convertible into shares and/or warrants, with authority to confer such powers in favour of the Executive Committee, also resolved to delegate powers to exclude the preferential subscription right in the case of the specific issues carried out under the powers delegated in the first instance. For these purposes, upon calling the abovementioned General Shareholders' Meeting, the proposal to exclude the preferential subscription right was expressly included in the Meeting announcement and the Board of Directors of Telefónica approved and made available to the shareholders a report justifying the proposal to delegate the powers to exclude the said right, in accordance with the provisions of Article 511.2 LSC.

As stipulated in Article 511.1 LSC, in order to exclude the preferential subscription right held by the shareholders in the issue of convertible notes and/or warrants, such exclusion must be necessary in the company's interest.

It is also necessary, in the case of each resolution for the issue of convertible notes and/or warrants excluding the preferential subscription right carried out by virtue of the powers delegated for this purpose, for an administrators' report and auditor's report to be issued in accordance with Article 511.3 LSC (referring to Article 417.2 LSC); that is, a report drawn up by the administrators providing detailed grounds for the exclusion, as well as a report drawn up by an auditor other than the Company's auditor, containing an expert opinion on the admissibility of the data included in the administrators' report and on the suitability of the conversion exchange ratio or the warrant exercise price, and, if applicable, of their adjustment formulas to offset a potential dilution of the financial stake held by the shareholders.

3.2 Grounds

The Executive Committee considers that the issue of the Convertible Notes and Warrants in favour of the Subsidiary, with the corresponding exclusion of the preferential subscription right held by the Company shareholders, thus allowing the simultaneous issue by the Subsidiary of the Indirectly Convertible Notes with a private placement through an accelerated bookbuilding offering ("**ABO**") process between qualified investors, is the most appropriate option and, given the current circumstances, is required, in the company's interests.

This ABO process will consist of a private placement between qualified investors coordinated by one or more financial institutions (the "**Lead Managers**"), which will carry out, during the most appropriate time to be in the market, a bookbuilding process over a short period of time with a view to obtaining indications of interest from potential qualified investors with respect to the Indirectly Convertible Notes. The final terms of the Issue will be established, including those of the Convertible Notes and the Warrants, on the basis of the results obtained from such process, and in line with usual practice in these types of transactions.

The main advantages for the Company derived from this placement mechanism and its appropriateness for the purposes of justifying the exclusion of the preferential subscription right, are as follows:

(i) It is an easy-to-use and flexible mechanism, which increases considerably the Company's margin for manoeuvre and reaction capacity to take advantage of the current market circumstances and, in particular, the potential "windows" or favourable opportunities to carry out transactions of this type, which are more often than not short-term transactions.

(ii) A placement through an ABO can be implemented quickly, generally in less than 24 or 48 hours, which drastically reduces the serious risks deriving from market volatility during the period commencing on the announcement date and ending on the closing date of the Issue, as is the case of issues with preferential subscription rights.

(iii) Moreover, the risk of volatility in share prices is also significantly reduced, which makes the transaction more efficient, due to being able to adjust the conversion price of the shares and consequently obtain the best results for the Company and its shareholders.

(iv) Because placements through an ABO process can be implemented in such a short period of time, this also reduces the risk of arbitration triggered when an issue is announced, since the activities of the investors between the announcement date and the date the terms and conditions are established ultimately have an impact on the latter, increasing the likelihood of speculative transactions, which is reduced by virtue of the ABO system.

(v) An accelerated placement such as the one proposed, containing a mechanism for establishing the terms and conditions of the Issue through a bookbuilding process in a very short period of time and between qualified investors (capable of rapidly assessing the issue and determining the terms and conditions under which they are prepared to acquire the convertible notes), makes it possible to obtain the best financial conditions for the Issue, to the advantage of the Company and all of its shareholders.

(vi) The ABO placement system allows qualified investors to be attracted to the offer, some of which will have acquired, at the time conversion takes place, shareholder permanence.

(vii) Finally, as regards costs and expenses, the Issue entails lower costs compared to those corresponding to an issue with a preferential subscription right, as such costs are limited to placement costs, thereby reducing legal fees and eliminating advertising and marketing costs.

In the event that an issue of convertible notes is carried out with a preferential subscription right, there is also a risk that the issue will not be subscribed by the shareholders in the initially envisaged period and amount. This would mean that a subsequent additional placement is required between non-shareholder investors in conditions expected to be less favourable for the Issuer, where the effective, operating, temporary and even reputation-related costs entailed by it would clearly jeopardise the corporate interests of Telefónica.

It should also be borne in mind that the exclusion of the preferential subscription right is standard practice in the issue of convertible bonds, both in the Spanish market and in international markets, as such securities are extremely complex financial instruments which are not generally suitable for minority investors.

3.3 <u>Determining the Conversion Price</u>

The Conversion Price of the Indirectly Convertible Notes (and accordingly that of the Convertible Notes and Warrants) will be determined once the accelerated bookbuilding process has been completed by the financial institutions in charge of the placement, taking into consideration that:

(a) the conversion price will include a minimum price, referenced to the final price of an accelerated placement of Telefónica shares which the Lead Managers could carry out on the same day as the Issue launch date (without any intervention on the part of Telefónica or the Subsidiary) or to a different price-setting mechanism, as well as a maximum price, which will include a conversion premium relating to the said minimum price;

(b) the conversion premium will be determined on the basis of the accelerated bookbuilding process to be carried out by the Lead Managers in charge of the placement among qualified investors which, following the receipt and analysis of the investment proposals made, will allow the price to be adapted as best as possible to market expectations. The conversion premium will not, under any circumstances, be more than 20% less than the minimum conversion price referred to in paragraph (a) above.

It can therefore be concluded that the issue of mandatorily convertible notes without a preferential subscription right and with a placement carried out through the ABO process (implemented in this case through the Indirectly Convertible Notes and, internally, through the Convertible Notes and the Warrants) is the most favourable option for the company's interests and, as a result, for the shareholders as a whole, since in this way, equity is attracted at the most favourable price possible, the financial risks of the transaction are minimised, and advantage may be taken of the best circumstances in the financial market, given that this issue's main characteristic is rapid execution, with the ensuing benefits in terms of timing and costs. Accordingly, the exclusion of the preferential subscription right suitably fits the purpose sought by it, as such exclusion is thoroughly compensated for and justified by the benefits gained by the Company and the possibility for the shareholders to carry out the transaction in the conditions indicated.

In light of the above, the Executive Committee considers that the exclusion of the preferential subscription right is clearly in the Company's interest and is necessary in line with such interest.

It is noted that the audit reports in relation to the Company's individual and consolidated annual accounts as at 31 December 2013 can be consulted on the Company's website (http://www.telefonica.com). Likewise, it is furthermore noted, for the appropriate purposes, that no relevant events have occurred subsequent to the closing of the annual accounts for the year ending on 31 December 2013 (the latest audited annual accounts available) which might have an impact on the Company's equity or valuation, other than those events which have already been announced by the Company in accordance with the legislation currently in force, which can be consulted on the Company's website and on the website of the Spanish Securities Market Commission (*Comisión Nacional del Mercado de Valores*) ("**CNMV**") (https://www.cnmv.es).

4. AUDITORS' REPORT

The information and data included in this report will be reviewed in a report issued by the auditor other than the Company's auditor appointed by the Madrid Mercantile Registry, in the terms envisaged in Articles 414, 417 and 511 of the LSC (the "**Auditor's Report**"). The Auditor's Report will contain a technical opinion on the admissibility of the data contained in this Report, in particular on the conversion basis and methods, and on the suitability of the conversion relationship for the Convertible Notes and the Warrants and their respective adjustment formulas to offset a potential dilution of the financial stake held by the shareholders.

Specifically, it is stated for the record that, on 8 July 2014, the Madrid Mercantile Registry appointed PriceWaterhouseCoopers Auditores, S.L. ("**PwC**") to issue the corresponding Auditor's Report (an appointment which was subsequently renewed successively on 1 August and 4 September 2014).

For that purpose, the present report will be provided to PwC in order for it to issue its mandatory Auditor's Report, which will be made available, together with this one, to the shareholders at the next General Shareholders' Meeting of Telefónica.

5. ISSUE RESOLUTION

The full text of the resolution to issue notes which are convertible into and/or exchangeable for shares in Telefónica and warrants with the right to acquire Telefónica shares approved by the Executive Committee is the following:

A) ISSUE OF NOTES WHICH ARE MANDATORILY CONVERTIBLE INTO, AND/OR EXCHANGEABLE FOR, SHARES IN TELEFÓNICA, S.A., AND WARRANTS

The Executive Committee of Telefónica, S.A. (the "**Company**"), pursuant to the powers conferred by virtue of the resolution adopted under point IV of the Agenda of the Ordinary General Shareholders' Meeting held on 30 May 2014 delegating to the Board of Directors, with powers of substitution, the authority to issue ordinary or convertible bonds and other similar debt instruments such as warrants, and pursuant to the powers conferred on the same date by the Board of Directors, thereby delegating such authority to the Executive Committee, unanimously resolved to carry out: (i) an issue of notes which are mandatorily convertible into and/or exchangeable for shares in the Company (the "**Convertible Notes**"), for a maximum face value amount of one billion, five hundred million (1.5 bn) euros, and (ii) an issue of warrants over shares in the Company (the "**Warrants**").

The Convertible Notes and the Warrants, which will be issued simultaneously, will be subscribed by Telefónica Participaciones, S.A. or by any other wholly-owned subsidiary of the Company, which will in turn make a similar issue of notes which are mandatorily convertible into and/or exchangeable for a number of shares in the Company, equal to the sum of those issued under the Convertible Notes and the Warrants, which together will not exceed a maximum number of 126,518,218 shares in the Company (subject to the corresponding adjustments), with terms and conditions substantially the same as those of the Convertible Notes and Warrants, to be placed among qualified investors on the international market (the "**Indirectly Convertible Notes**" and, together with the Convertible Notes, the "**Notes**"). The Indirectly Convertible Notes will be mandatorily converted into and/or exchanged for shares in Telefónica, S.A., and for this purpose, Telefónica will directly deliver, to the holders of said notes, the corresponding shares under the Convertible Notes and/or the Warrants, since these shares cannot be subscribed or received by the Subsidiary under any circumstance.

The Issue will be implemented in accordance with the terms and conditions included below (the "**Terms and Conditions**"). This notwithstanding, as indicated, some of the Terms and Conditions will ultimately be determined and may even be amended by the Company and/or the Subsidiary, due to reasons of financial appropriateness or the bookbuilding and placement process for the Indirectly Convertible Notes carried out by the financial entities intervening in the Issue (the "**Lead Managers**").

The essential Terms and Conditions of the Convertible Notes, the Warrants and the Indirectly Convertible Notes will be the following:

(i) CONVERTIBLE NOTES:

1. Issuer: the Convertible Notes will be issued by Telefónica, S.A. and subscribed by Telefónica Participaciones, S.A. or by any other wholly-owned subsidiary, whether Spanish or foreign (the "**Subsidiary**"), which will in turn issue the Indirectly Convertible Notes to be placed among qualified investors; the obligations assumed by the Subsidiary by virtue of this issue will be personally guaranteed by Telefónica, S.A.
2. Amount of the Issue: the maximum face value amount of the Issue is 1.5 billion euros, with the possibility of incomplete subscription.
3. Issue price: the Convertible Notes will be issued at 100% of their face value, as a minimum.

4. Maturity: the Convertible Notes will mature 3 years after their issue date (the "**Maturity Date**").

5. Interest rate: the Convertible Notes will accrue fixed annual interest payable annually in arrears as of the date of issue, at a rate of between 4% and 5.5%.

6. Accelerated conversion: the Convertible Notes will be converted in advance, in the event certain circumstances arise, and they may also be converted at any time, at the Company's discretion, during the conversion period established, in both cases in accordance with the terms and conditions of the Indirectly Convertible Notes; likewise, the Convertible Notes may be converted in advance when the holders of the Indirectly Convertible Notes opt for early conversion during the voluntarily conversion period or in the event that certain circumstances arise, in each case under different conditions of conversion.

7. Mandatory conversion into shares in Telefónica, S.A.: the Convertible Notes will be mandatorily converted into shares in Telefónica, S.A. on the Maturity Date, and for that purpose, the Company will directly deliver, on behalf of the Subsidiary, to the holders of the Indirectly Convertible Notes, the shares which would correspond to the Subsidiary, since it cannot, under any circumstances, subscribe or receive shares in Telefónica, S.A. on its own account. The Company will have the option of carrying out the conversion of the Indirectly Convertible Notes by delivering new or existing shares or a combination of both.

8. Conversion Price: will be the maximum conversion price set for the Indirectly Convertible Notes.

9. Priority of payments: the payment obligations derived from the Notes will be direct, unconditional and subordinate obligations.

10. Anti-dilution mechanism: anti-dilution mechanisms will be established on the Conversion Price, as is standard practice in these kinds of transactions.

11. Applicable law: the Convertible Notes will be subject to Spanish law with regard to: (i) their legal status and credit ranking, (ii) the capacity of the Company and the corresponding corporate resolutions, and (iii) the creation of the Syndicate of Noteholders and the appointment of its Commissioner. Except as provided above, the terms and conditions of the Convertible Notes (including

the non-contractual obligations) will be governed and construed in accordance with UK law.

(ii) WARRANTS:

1. Issuer: the Warrants will be issued by Telefónica, S.A., simultaneously to the Convertible Notes, in the form of one Warrant for each Convertible Note. Therefore, they will be issued without a premium and in exchange for the subscription of the Convertible Notes by the Subsidiary.
2. Maturity: the Warrants will mature 3 years after their date of issue, although they may be exercised early in scenarios and under circumstances equivalent to those envisaged for the Indirectly Convertible Notes.
3. Acquisition of shares in Telefónica, S.A.: the Warrants will grant the right to receive new or existing shares in Telefónica, S.A., which will be directly delivered to the holders of the Indirectly Convertible Notes on behalf of the Subsidiary.
4. Minimum acquisition ratio: zero shares, in the event that the price of the share applicable on the Maturity Date is equal to or higher than the maximum conversion prices set for the Indirectly Convertible Notes.
5. Maximum acquisition ratio: it will be equal to a percentage of between 16.6667% and 20% of the maximum number of shares which Telefónica has to deliver under the Indirectly Convertible Note, depending on the price per share applicable on the Maturity Date and limited in any event to the difference resulting in the number of shares between the minimum and maximum conversion price of the Indirectly Convertible Notes.
6. Anti-dilution mechanism: anti-dilution mechanisms will be established on the acquisition price, as is standard practice in these kinds of transactions.
7. Applicable law: the Warrants will be subject to Spanish law in terms of their legal status, the capacity of the Company and the corresponding corporate resolutions. Except as provided above, the terms and conditions of the Warrants (including the non-contractual obligations) will be governed and construed in accordance with UK law.

(iii) INDIRECTLY CONVERTIBLE NOTES:

1. Issuer: the Indirectly Convertible Notes will be issued by the Subsidiary, whose obligations thereunder will be personally guaranteed by Telefónica, S.A., which will also assume the obligation to issue and deliver the corresponding shares directly to the holders of the Indirectly Convertible Notes, on the Subsidiary's behalf.
2. Amount of the Issue: the maximum face value amount of the Issue is 1.5 billion euros, with the possibility of incomplete subscription.
3. Maturity: the Indirectly Convertible Notes will mature 3 years after their issue date (the "**Maturity Date**").
4. Subscribers of the Issue: the Indirectly Convertible Notes will exclusively target qualified investors, meaning that it will not be necessary to prepare a prospectus for the offering.
5. Face value and representation: the Indirectly Convertible Notes will have a face value per unit of one hundred thousand (100,000) euros and they will be represented by registered share certificates.
6. Issue price: the Indirectly Convertible Notes will be issued at 100% of their face value, as a minimum.
7. Issue date: the issue date will be the same as the subscription and payment date (the "**Closing Date**").
8. Subscription and payment period:

   (i) Subscription period: the subscription of the Indirectly Convertible Notes will be a single, one-time event, and will take place on the Closing Date, subject to the fulfilment of the conditions envisaged in this regard in the Subscription Agreement, subject to UK law, which the Subsidiary and Telefónica, S.A. intend to sign with the Lead Managers (the "**Subscription Agreement**") once the final terms and conditions of the Indirectly Convertible Notes have been set, following the conclusion of the bookbuilding process.

(ii) Payment: the Indirectly Convertible Notes will be paid by subscribers in cash, simultaneously to their delivery on the Closing Date.

9. Interest rate: the Indirectly Convertible Notes will accrue fixed annual interest payable annually, in arrears, as of the Closing Date, at a rate of between 4% and 5.5%. The final interest rate for the Indirectly Convertible Notes will be determined by mutual agreement between the Company and the Lead Managers, depending on the outcome of the bookbuilding process.

10. Conversion into shares in Telefónica, S.A.: the Indirectly Convertible Notes will be mandatorily converted into shares in Telefónica, S.A. on the Maturity Date, and for that purpose, the holders of the same will directly receive the shares which would correspond to the Subsidiary under the Convertible Notes and, if applicable, the Warrants. The Company will have the option of carrying out the conversion of the Indirectly Convertible Notes by means of the delivery of new, existing or a combination of both.

11. Accelerated conversion: the Indirectly Convertible Notes will be converted in advance, in the event that certain circumstances arise, and they may also be converted at any time, at the discretion of the Subsidiary, during the conversion period established; likewise, the holders of the Indirectly Convertible Notes may opt for early conversion during the voluntarily conversion period, or in the event that certain circumstances arise, in each case under different conditions of conversion.

12. Conversion price: the conversion price will include a minimum price, referenced to the final accelerated placement price of the shares in Telefónica, S.A. which the Lead Managers could carry out on the same date as the launch of the Issue (with no intervention whatsoever by Telefónica or the Subsidiary), or to a different price-setting mechanism, and a maximum price, which will include a premium calculated as an estimated percentage of between 20% and 25% of said value, although the final price will be determined by mutual accord between the Company and the Lead Managers, depending on the outcome of the bookbuilding process.

13. Anti-dilution mechanism: anti-dilution mechanisms will be established on the conversion price, as is standard practice in these kinds of transactions.
14. Guarantees: the Indirectly Convertible Notes will have the general guarantee of the Subsidiary's assets, and will also have a subordinate guarantee from the Company (the "**Guarantee**"), with Telefónica's personal obligation to issue and deliver the corresponding shares to the holders of the Indirectly Convertible Notes upon conversion, on the Subsidiary's behalf.
15. Use of the funds: the funds obtained as a result of the Issue will be used to finance the acquisition of E-Plus and for general corporate needs.
16. Lock-up: in the Subscription Agreement, the Company may assume a lock-up undertaking, with the standard content and terms for these kinds of transactions.
17. Priority of payments: the payment obligations derived from the Indirectly Convertible Notes, as well as from the Guarantee, will be direct, unconditional and subordinate obligations.
18. Listing: a request will be made, via the Lead Managers or any other entity hired for that purpose, to list the Indirectly Convertible Notes on a regulated secondary market, multilateral trading system or other organised market, such as the *Freiverkehr* of the Frankfurt Stock Exchange.
19. Applicable law: the Terms and Conditions of the Indirectly Convertible Notes will be governed and construed in accordance with UK law; in the event the Subsidiary is of Spanish nationality, the Indirectly Convertible Notes will be subject to Spanish law in terms of: (i) their legal status and credit ranking, (ii) the capacity of the Subsidiary, as well as the corresponding corporate resolutions; and (iii) the creation of the Syndicate of Noteholders and the appointment of its Commissioner.

It is also noted for the record that, pursuant to Article 510 of the Spanish Companies Act ("**LSC**") and in the first additional provision, section 9 of Act 10/2014 of 26 June, the maximum limit for issues included in Article 405 LSC does not apply to Telefónica, S.A. or the Subsidiary. Moreover, the maximum Issue amount, together with the amount of any other debt securities issued by the Company pursuant to the resolution approving the delegation of authority adopted by the Ordinary General

Shareholders' Meeting held on 30 May 2014, does not exceed the maximum limit of 25 billion euros. Likewise, the amount of the capital increase necessary to carry out the conversion of the Convertible Notes and the acquisition right of the Warrants does not exceed the limit of 20% of the share capital, established in section 6.*a*) of said delegation resolution adopted by the Ordinary General Shareholders' Meeting of Telefónica.

In accordance with Article 403 LSC, and subject to the terms of Article 419 of the same Act, the Convertible Notes and the Indirectly Convertible Notes (in the event they are issued by a Spanish Subsidiary) will avail of a Syndicate of Noteholders, which will be set up once the issue deed has been registered, and which will be governed by the rules attached hereto as Schedule I or, in the case of any aspects not expressly provided for therein, by the legislation in force.

Pursuant to Article 414.1 LSC, it was likewise resolved to increase the share capital by the maximum amount necessary to carry out the conversion of the Convertible Notes and the exercise of the acquisition rights of the Warrants (in the event that the Company does not opt to deliver previously-issued shares), and to exclude the shareholders' preferential subscription right, since this exclusion is justified for corporate interest reasons.

For this purpose, the minimum amount by which it is agreed to increase the share capital, which will correspond to the capital increase linked to the Convertible Notes, will be determined by the quotient obtained by dividing the face value amount of the Indirectly Convertible Notes by the maximum conversion price agreed in the bookbuilding process. Meanwhile, the maximum amount of the capital increase will correspond to the quotient obtained by dividing the face value amount of the Indirectly Convertible Notes by the minimum conversion price agreed in said process, with the difference between the minimum and maximum amount constituting the capital increase linked to the Warrants. The public deeds executed and the corresponding registry entries will record the final amount of the capital increase and, in particular, that of the Convertible Notes, on the one hand, and of the Warrants, on the other.

The amount of the capital increase will be subject to any possible modifications arising as a result of the events of adjustment of the conversion prices contained in the final terms and conditions of the Indirectly Convertible Notes (and of the Convertible Notes and of the Warrants).

It was likewise resolved to approve the corresponding administrators' report explaining the conversion basis and methods and justifying in detail the proposal to exclude the shareholders' preferential subscription right, for the purposes established in Articles 414, 417 and 511 LSC. Both the administrators' report and the auditor's report will be made available to the shareholders and announced at the first General Meeting held following the adoption of the Issue resolution.

B) GRANTING OF POWERS OF EXECUTION

One.- To jointly and as broadly as in law is possible, empower the Chairman of the Board of Directors, Mr Cesar Alierta Izuel; the Managing Director, Mr José María Álvarez-Pallete López; the General Manager of Finance and Corporate Development, Mr Ángel Vilá Boix; the Secretary-General and Secretary of the Board of Directors, Mr Ramiro Sánchez de Lerín García-Ovies; the Financial Director, Mr Miguel Escrig Meliá; the Vice-Secretary General and Director of the Group's Legal Services, Ms María Luz Medrano Aranguren; the Finance Director, Mr Eduardo Álvarez Gómez; the Director of Finance Companies and Variable Income, Mr Carlos David Maroto Sobrado; the Director of Foreign and Securities Exchange Markets, Mr Javier Campillo Díaz; and the Director of Credit Market Relations, Mr Daniel Rodríguez-Malo García, so that any of them, severally, may carry out all actions necessary to ensure the full enforceability of the above resolutions (and, in particular, to amend, clarify, interpret, complete, explain, specify and even modify them), which includes, among others, and by way of example, the following powers:

1. To determine, specify, complete, modify and carry out the above resolutions and, in particular, establish, depending on the outcome of the bookbuilding and placement process of the Indirectly Convertible Notes carried out by the Lead Managers, the final Terms and Conditions of the Issue, in particular of the Convertible Notes and of the Warrants, including, merely by way of

example: the definitive face value amount of the Issue, the issue and conversion or acquisition price, the interest rate, interest accrual periods, face value per unit of the Notes and the Warrants, Closing Date and Maturity Date, prepayment or early conversion scenarios, the terms and conditions of the anti-dilution mechanism, and the remuneration which the Company must pay, if applicable, to the Lead Managers and to any other underwriting and/or placement entity or entities in respect of the Notes, all under the broadest terms, and to likewise agree and/or determine, depending on the outcome of the bookbuilding and placement process of the Indirectly Convertible Notes, the final amount of the Issue and the share capital increases corresponding to the Convertible Notes and the Warrants, declare the total or partial subscription of the Issue and, if appropriate, withdraw from its execution.

2. To modify the previously-established essential Terms and Conditions of the Notes and the Warrants if it becomes necessary or advisable, depending on the outcome of the bookbuilding and placement process of the Indirectly Convertible Notes, due to the indications or recommendations of the Lead Managers, or for any other financial or commercial reason in the interest of best placing the Issue.

3. To determine which subsidiary of Telefónica, S.A. will issue the Indirectly Convertible Notes, acting as the Company's representative in its capacity as the Subsidiary's sole shareholder, exercising all of the rights (for voting and otherwise) which correspond to the Company as shareholder to take any decisions and/or actions as it sees fit, including, in particular -but not limited to- any decisions, actions and/or resolutions the attorney deems advisable in relation to the Issue, and in particular those in relation to the issue of the Indirectly Convertible Notes, executing any documents, whether public or private, of any type (including, but not limited to, minutes and certificates) as necessary or appropriate for said purpose, and to negotiate, sign and execute any agreements and documents as necessary or appropriate in order to document the guarantee which Telefónica, S.A. may provide in favour of the Subsidiary and/or the Noteholders, and any other agreement or document

between Telefónica, S.A. and the Subsidiary, including, in particular, but not limited to, securities and cash lending, as deemed necessary or appropriate to ensure the successful outcome of the Issue.

4. To issue the Notes and the Warrants, after first complying with the legal or any other requirements as necessary, and in accordance with the final terms and conditions of the Issue.

5. To publish any mandatory announcements regarding the Issue which is the subject of these resolutions and to execute the corresponding public deeds in relation to the Issue and, if applicable, the notarial certificates of the subscription and closing of the Issue, and to request their recording at the Mercantile Registry.

6. To negotiate, sign and subscribe, in a public or private document and under any applicable law, any documents or agreements as necessary or appropriate in relation to the formalisation of the Issue -including (among others) the Subscription Agreement and one or more agency agreements regarding payments, exchange/conversion and calculation, as well as the agreement for the provision of services with the auditor appointed by the Mercantile Registry-, making any designations and appointments as necessary or appropriate of the entities or individuals participating in the transaction (Lead Managers, underwriting and/or placement entities, payment and exchange/conversion agents, calculation agent, securities depositories, etc.), under the terms and conditions deemed most appropriate for the Company and to ensure the successful outcome of the Issue.

7. To draft and sign all Relevant Events, as necessary, for the purpose of their publication by the Spanish Securities Market Commission (*Comisión Nacional del Mercado de Valores*) ("CNMV") or by any other competent authority, as well as the appropriate press releases.

8. To execute, one or more times, the share capital increases necessary for the conversion of the Indirectly Convertible Notes, issuing, up to the agreed maximum under the Convertible Notes and the Warrants, new shares as

required and consequently amending the article of the corporate by-laws in relation to the share capital, indicating the terms in which said resolutions adopted are to be carried out, as well as to issue the shares representing the share capital increases resolved, or choose to deliver the previously-issued shares belonging to the Company's treasury stock, and to request that the shares issued as a result of the exercise of the conversion rights over the Notes be listed on the Spanish securities markets, requesting that they be included in the Electronic Trading System (*Sistema de Interconexión Bursátil*) (Continuous Market) and be subject to the applicable regulations.

9. To carry out any actions, steps or procedures, make any declarations or request and sign any certificates, petitions, agreements, supplements, documents or writs as necessary or required, before any public or private bodies, entities or registries, whether Spanish or foreign, in relation to the Issue, being able to clarify, specify, interpret and complete the content of the writs filed and, in general, make decisions on any omissions or defects which might hinder their enforceability.

10. To process the request to list, as the case may be, before the regulated secondary securities market, multilateral trading system or other organised market in which it is decided to list the Indirectly Convertible Notes, and to prepare and sign any documents as necessary or appropriate in relation to the listing, as well as any modifications or additions, issuing the certificates, documents, letters and other instruments which any of the attorneys deems necessary.

11. To choose and appoint the individuals or entities to act as the Commissioners of the Syndicate of Noteholders for the Issue, who will provisionally hold this post until they are confirmed or replaced, as the case may be, by the corresponding General Meetings of Noteholders, and to negotiate, sign and enter into the relevant agreements with said parties.

12. In general, to take any additional measures or arrange for them to be taken, and execute and deliver, or arrange for the execution and delivery of, any instruments, contracts, agreements, statements, certificates, letters,

supplements or additional documents, whether public or private, on behalf of the Company and/or the Subsidiary, to ensure the successful outcome of the purpose and object of the provisions stipulated above.

13. To withdraw from the Issue, as the case may be, or postpone its execution, in the event that market circumstances make this advisable, or if the final terms and conditions which derive from the bookbuilding process are not satisfactory for the Company.

14. To take any actions as necessary and to approve and formalise any public or private documents which are necessary or appropriate to ensure the full enforceability of the above resolution on the Issue of the Notes and the Warrants in respect of any of their aspects and contents and, in particular, to remedy, clarify, interpret, complete, specify, determine and even amend, as the case may be, the resolution adopted and, in particular, to remedy any defects, omissions or errors noted in the verbal or written instructions from the Mercantile Registry, all under the broadest terms possible.

15. To appear before a Notary Public and, in his or her presence, execute the raising to public document status of the above resolutions, signing any public and private instruments as necessary or appropriate until the resolutions are enforceable, making any rectifications or remedying any errors in relation to this resolution.

Two.- To authorise each and every one of the members of the Board of Directors of Telefónica, S.A. so that any one of them, acting severally, may appear before a Notary Public and raise all of the preceding resolutions to public document status, being able to execute any documents necessary for this purpose, including the corresponding public deed regarding the issue of the Convertible Notes and, as the case may be, notarial certificates for the subscription and closing of the issue, and to request that the preceding resolutions, as well as any deeds of correction, rectification or clarification, be recorded at the Mercantile Registry.

SCHEDULE 1
REGULATIONS OF THE SYNDICATE OF NOTEHOLDERS OF THE ISSUE OF MANDATORILY CONVERTIBLE AND/OR EXCHANGEABLE NOTES IN TELEFÓNICA MATURING IN 2017

Please find below the Regulations of the Syndicate of Noteholders for the issue of notes in TELEFÓNICA, S.A., called the "ISSUE OF MANDATORILY CONVERTIBLE AND/OR EXCHANGEABLE NOTES IN TELEFÓNICA, S.A., MATURING IN 2017".

TITLE I

INCORPORATION, NAME, PURPOSE, ADDRESS AND DURATION FOR THE SYNDICATE OF NOTEHOLDERS.

ARTICLE 1.- INCORPORATION

In accordance with the provisions of Chapter IV of Section XI of the Royal Legislative Decree on Capital Companies (*Real Decreto Legislativo 1/2010, de 2 de julio, que aprueba el texto refundido de la Ley de Sociedades de Capital*) (the "**Spanish Companies Act**"), a Syndicate of the holders of the Notes (the "**Noteholders**") will be incorporated, once the public deed of the issue has been recorded at the Mercantile Registry, which comprises the " ISSUE OF MANDATORILY CONVERTIBLE AND/OR EXCHANGEABLE NOTES IN TELEFÓNICA, S.A., MATURING IN 2017".

This Syndicate will be governed by these Regulations, by the Spanish Companies Act, by the applicable provisions of the corporate by-laws of TELEFÓNICA PARTICIPACIONES, S.A.U. (the "**Issuer**") and by any other applicable legislation. The subscription of the Notes which are the subject of this Syndicate implies the express acceptance of these rules by the subscriber.

ARTICLE 2.- NAME

The Syndicate will be named "SYNDICATE OF NOTEHOLDERS FOR THE ISSUE OF MANDATORILY CONVERTIBLE AND/OR EXCHANGEABLE NOTES IN TELEFÓNICA, S.A., MATURING IN 2017".

ARTICLE 3.- PURPOSE

This Syndicate is formed for the purpose of representing and protecting the lawful interest of the Noteholders before the Issuer, by means of the exercise of the rights granted by the applicable laws and the present Regulations, to exercise and preserve them in a collective way and under the representation determined by these regulations.

ARTICLE 4.- ADDRESS

The address of the Syndicate will be Gran Vía, 28, in Madrid.

However, the Noteholders General Meeting is also authorised to hold a meeting, when considered appropriate, in any other place in Madrid that is specified in the notice convening the meeting.

ARTICLE 5.- DURATION

The Syndicate will be in force until the Noteholders have reinstated in their favour any rights deriving from the Notes due to principal, interest, or any other applicable item.

TITLE II

SYNDICATE'S REGIME

ARTICLE 6.- SYNDICATE MANAGEMENT BODIES

The Management bodies of the Syndicate are:

(i) The General Meeting of Noteholders (the "**General Meeting**").

(ii) The Commissioner of the General Meeting of Noteholders (the "**Commissioner**").

ARTICLE 7.- LEGAL NATURE

The General Meeting, duly called and constituted, is the body of expression of the Noteholders' will, subject to the provisions of these Regulations, and its resolutions are binding for all the Noteholders as established by law.

ARTICLE 8. - CONVENING MEETINGS

The General Meeting will be convened by the Board of Directors of the Issuer or by the Commissioner, whenever they may deem it advisable.

Notwithstanding the above, the Commissioner will convene a General Meeting when Noteholders holding at least one twentieth part of the outstanding principal amount of the Notes request it by writing, specifying the purpose of the General Meeting. In such case, the General Meeting will be convened and held within forty-five (45) days following receipt of the notice for this purpose by the Commissioner.

ARTICLE 9.- PROCEDURE FOR CONVENING MEETINGS

The General Meeting will be convened at least fifteen (15) days before the date set for the meeting, by (i) notice published in the website of the Issuer or by (ii) notice to the Noteholders in accordance with the terms and conditions of the Notes.

When the General Meeting is convened in order to consider or resolve matters relating to the amendment of the terms and conditions of the Notes or any other matter considered to be of similar relevance by the Commissioner, it should be convened in the manner set out in the Spanish Companies Act for the General Shareholders' Meeting.

In any case, the notice will state the name of the Issuer and the name of the Syndicate, the name and post of the person or persons who have convened the meeting, the place and the date for the meeting, the agenda for the meeting and the way in which the ownership of the Notes will be proved in order to have the right to attend the General Meeting.

ARTICLE 10.- RIGHT TO ATTEND MEETINGS

Noteholders who have been so at least five days prior to the date on which the meeting is scheduled, will have the right to attend the General Meeting.

The members of the Board of Directors of the Issuer and the fiscal agent of the Issue will have the right to attend the General Meeting, even if they have not been requested to attend.

The Commissioner must attend the General Meeting, irrespective of whether he/she has convened it.

ARTICLE 11.- RIGHT TO BE REPRESENTED

All Noteholders having the right to attend the General Meetings also have the right to be represented by another person. Appointment of a proxy must be in writing and only for each particular General Meeting.

ARTICLE 12.- QUORUM FOR MEETINGS AND TO PASS RESOLUTIONS

The General Meeting will be entitled to pass resolutions if attendees represent at least two thirds of the outstanding Notes. The resolutions will be approved by an absolute majority of the votes corresponding to such amount.

Where two thirds of the outstanding Notes are not present or duly represented at the first meeting of the General Meeting, then the General Meeting may be reconvened to meet a month after the first meeting. In this case the General Meeting will be validly constituted regardless of the number of outstanding Notes present or duly represented and the resolutions may be passed by an absolute majority of the votes corresponding to the attendees.

In the event that there is a change in law affecting this matter, the quorum and majority regime foreseen in this article will apply insofar as the law allows so.

Nevertheless, the General Meeting will be deemed validly constituted to transact any business within the remit of the Syndicate if Noteholders representing all the outstanding Notes are present or duly represented, and provided that they unanimously approve the holding of the General Meeting.

ARTICLE 13.- VOTING RIGHTS

In the meetings of the General Meeting, each Note will confer the right to one vote.

Furthermore, means may be provided, with each convening of a meeting, for communicating remotely and/or electronically, which Noteholders may use to issue their vote. Such means must sufficiently guarantee that each Noteholder or his/her representative, as the case may be, can be properly identified. If such means are made available to the Noteholders, the convening of the General Meeting must contain precise instructions for the exercise of the voting right or, alternatively, indicate a website and/or email address where such instructions and forms or other means necessary for voting can be obtained.

ARTICLE 14.- CHAIRMAN OF THE GENERAL MEETING

The Commissioner will be the chairman of the General Meeting, will chair the discussions, will have the right to bring the discussions to an end when he considers it advisable and will arrange for matters to be put to the vote.

ARTICLE 15.- ATTENDANCE LIST

Before discussing the agenda for the meeting, the Commissioner will complete the attendance list, stating the nature and representation of each of the attendees and the number of Notes, both directly owned and/or represented, with which they attend.

ARTICLE 16.- POWER OF THE GENERAL MEETING

The General Meeting may pass resolutions necessary for:

- the best protection of Noteholders' lawful interests before the Issuer;
- to modify, in accordance with the Issuer, the terms and conditions of the Notes;
- to approve the substitution of any person for the Issuer (or any previous substitute) as principal obligor under the Notes;
- to waive the exercise of faculties or rights under the terms and conditions of the Notes;
- to dismiss or appoint the Commissioner;
- to exercise, when appropriate, the corresponding legal claims; and
- to approve the expenses caused by the defence of the Noteholder's common interest.

ARTICLE 17.- CHALLENGE OF RESOLUTIONS

The resolutions of the General Meeting may be challenged by the Noteholders in accordance with Chapter IX of Section V of the Spanish Companies Act.

ARTICLE 18.- MINUTES

The minutes of the meeting may be approved by the General Meeting, after the meeting has been held or, if not, within a term of fifteen (15) days by the Commissioner and at least one Noteholder appointed for such purpose by the General Meeting.

ARTICLE 19.- CERTIFICATES

The certificates of the minutes of the resolutions of the General Meeting will be issued by the Commissioner.

ARTICLE 20.- INDIVIDUAL EXERCISE OF ACTIONS

The Noteholders will only be entitled to individually exercise judicial or extra judicial claims if such claims do not contradict the resolutions previously adopted by the Syndicate, within its powers, and are compatible with the faculties conferred upon the Syndicate.

ARTICLE 21.- EXPENSES OF THE SYNDICATE

All normal expenses arising in maintaining the Syndicate will be borne by the Issuer, and cannot exceed in any event two percent (2%) of the annual interest accrued by the Notes.

TITLE III

THE COMMISSIONER

ARTICLE 22.- NATURE OF THE COMMISSIONER

The Commissioner will bear the legal representation of the Syndicate and will be the body for liaison between the Syndicate and the Issuer.

ARTICLE 23.- APPOINTMENT AND DURATION OF THE OFFICE

Notwithstanding the initial appointment of the provisional Commissioner, which will require the ratification of the General Meeting, this latter will have the power to appoint the Commissioner and he will exercise his office as long as he is not dismissed by the General Meeting.

ARTICLE 24.- POWERS

The Commissioner will have the following responsibilities:

(i) To protect the common interests of the Noteholders.

(ii) To call and act as chairman of the General Meeting.

(iii) To inform the Issuer of the resolutions passed by the General Meetings.

(iv) To monitor the payment of the principal and the interest.

(v) To carry out all those actions provided for in the terms and conditions of the Notes to be carried out or that may be carried out by the Commissioner.

(vi) To execute the resolutions of the General Meeting.

(vii) To exercise the actions corresponding to the Syndicate.

(viii) In general, the responsibilities granted to him by law and the present Regulations.

TITLE IV

SPECIAL PROVISIONS

ARTICLE 25.- JURISDICTION

For any dispute arising from these Regulations, the Noteholders, by virtue of being so, will submit to the exclusive jurisdiction of the courts and tribunals of the city of Madrid, waiving expressly any jurisdiction that could apply to them.