



[ *the Board of Directors' Committees* ]

Both the Company's Articles of Association and the Regulations of the Board of Directors provide for the existence of an Executive Committee, with overall decision-taking power and consequently with express delegated authority in all powers corresponding to the Board of Directors, except those which cannot be legally or statutorily delegated.

The Regulations empower the Board of Directors to create one or various consultative or sub-committees that are entrusted with the examination and monitoring, on a permanent basis, of certain areas of particular relevance for the Company's corporate governance, or with the performance of monographic analyses of specific aspects or matters when their degree of importance makes this advisable. These Committees do not have the status of corporate bodies. Instead, they are instruments at the service of the Board of Directors, to which they present their conclusions on matters or aspects that they have been asked to investigate.

In terms of these consultative or control committees, and as indicated previously, the Board of Directors, at its meeting on June 26, 2002, approved the reorganisation of this, assigning new jurisdictions to some Directors and renewing the Board's composition in order for this to be formed almost entirely by external or non-executive Directors.

After this reorganisation, Telefónica's Board of Directors has the following sub-committees: the

Audit and Control Committee, the Nominating, Compensation and Corporate Governance Committee, the Human Resources and Corporate Reputation Committee, the Regulation Committee and the Service and Commercial Quality Committee.

## 6.1 Executive Committee

The existence of an Executive Committee enhances the operativity and efficiency of the Board of Directors when exercising its functions, providing it with the necessary support through the work that it performs, particularly since it is formed by less Directors than the Board and meets more frequently than the latter.

Pursuant to the recommendations made in the Olivencia Report, and also in line with those recently published by the Aldama Commission, the relationship between both bodies are based on the principle of transparency, in the sense that the Board is fully aware of the decisions adopted by this Committee. Accordingly, matters considered and agreements adopted by the Executive Committee are always included as a point in the agenda to be discussed at the meetings of the Board of Directors.

As of the date of this Report, the Board of Directors Executive Committee is formed by the following persons:

- Mr. César Alierta Izuel (Chairman)
- Mr. Isidro Fainé Casas (Vice Chairman)
- Mr. Fernando Abril-Martorell Hernández
- Mr. Maximino Carpio García
- Mr. Carlos Colomer Casellas
- Mr. José Maldonado Ramos
- Mr. Antonio Viana-Baptista
- Mr. Gregorio Villalabeitia Galarraga
- Mr. Antonio Alonso Ureba (Secretary)

The Regulation of the Board of Directors provide that this Committee will meet every fortnight on a ordinary basis and as many times as it is called by its Chairman. In 2002, the Committee held twenty meetings, each with an average duration of more than 3 hours. Also noteworthy was the high level of attendance of its members.

As is the case with the meetings of the Board of Directors, they have a pre-established agenda, which is notified at least three days before the date envisaged for the meeting together with the notice of the meeting.

The Group's executive officers frequently attend the Executive Committee meetings in order to present information on matters relating to their respective areas of jurisdiction. Thus, some members of the Company's senior management attended practically all the meetings held during 2002. It is also worth highlighting that during 2002 External advisors gave twenty presentations at the Executive Committee meetings addressing matters included on the agenda.

The Executive Committee dedicates a great deal of time at its meetings to develop and prepare

the issues that will be presented at the next Board meeting. Special consideration is given to certain issues on which the Executive Committee is informed, taking note of their content and scope and adopting, where appropriate, any necessary agreements.

## 6.2 Board sub-committees

### Audit and Control Committee

Article 24 of the Regulations of the Board of Directors establishes the working principles of the Audit and Control Committee as a consultancy or control Committee of the Board of Directors.

The main task of the Audit and Control Committee is to provide support to the Board of Directors in its supervisory functions having the following basic responsibilities:

1. Propose the appointment of the Auditor, the terms and conditions pursuant to which he/she is contracted, the scope of his/her professional mandate and, where appropriate, the revocation or extension of the appointment;
2. Review the Company's accounts, monitor compliance with legal requirements and the correct application of generally accepted accounting principles, and provide notification on proposals to modify the accounting principles and criteria suggested by management;
3. Serve as a communication channel between the Board of Directors and the Auditor, evaluate the results of each audit and the responses of management to the auditor's recommendations, and

mediate and arbitrate in disputes between the former and the latter in connection with applicable principles and criteria in the preparation of the financial statements;

4. Verify the suitability and integrity of the internal control systems adopted in the preparation of the individual and consolidated financial statements.
5. Monitor the fulfilment of the audit contract, taking all necessary steps to ensure that the opinion on the financial statements and the main contents of the auditor's report are drafted in a clear and precise manner.
6. Review the brochures and the periodical financial information that the Company must provide to markets and supervisory bodies; and
7. Ensure compliance with the Internal Code of Conduct for Securities Markets Issues and, in general, with the Company's own rules of governance and make the necessary proposals for their improvement. In particular, the Audit and Control Committee is responsible for receiving information, and, where appropriate, issuing a report on disciplinary measures to the members of the Company's management.

As of the date of the present Report, this Committee is formed by the following members:

- Mr. Antonio Massanell Lavilla (Chairman)
- Mr. Maximino Carpio García.
- Mr. Antonio Fernández Rivero
- Mr. Gonzalo Hinojosa Fernández de Angulo

In accordance with the recommendation contained in the Olivencia Report and corroborated by the Aldama Commission, all members of the Audit and Control Committee are non-executive Directors. Moreover, in compliance with the latest international recommendations in this regard, all the members of this Committee have financial experience and specifically its Chairman has extensive professional experience in finance and accountancy.

The Regulations of the Board of Directors establish that the Audit and Control Committee shall meet regularly according to needs and at least four times per year. During 2002, this Committee held eight (8) meetings, noteworthy for the high level of attendance of all of its members.

The meetings took place in accordance with a pre-established agenda, issued beforehand to the members of the Committee together with the notice of each meeting. The deliberations of this Committee and the agreements and decisions adopted are set forth at the corresponding minutes of each meeting.

The meetings of the Committee are normally attended by the members of the Company's management indicated below and who provide support and assistance to the Committee members in matters to be analysed at each of its meetings:

- General Secretary and Secretary of the Board of Directors of Telefónica.
- General Manager of Corporate Finance.
- General Manager of Audit and Communication.
- Deputy General Manager of Audit and Corporate Inspection.

- Deputy General Manager of Consolidated Financial Information and Accounting Policies.
- Deputy General Manager of Management Control.

Moreover, whenever requested by the Committee itself, other members of the management team of both the Company and its subsidiaries have participated in these meetings in order to provide information on specific matters affecting their respective areas of jurisdiction.

Lastly, the partner (assigned to Telefónica) of the Company's Accounts Auditor has regularly attended the Committee's meetings. Specifically, this person has intervened – only in relation to certain matters included on the agenda – in six of the eight meetings, at the request of this Committee, in order to explain and clarify aspects contained in the audit reports, provide information on his fees and deal with specific questions relating to the Group's information and accounting policies, in relation to the audit work performed.

During 2002, the main analysed questions by this Committee were as follows:

- The Company's internal control systems. During the meetings, this Committee was informed in detail of the actions performed by the Group's Internal Audit units.
- In order to verify the Company's accounts, this Committee reviewed the Company's audit system, consisting in the performance of quarterly reviews of the Company's financial statements in order to ensure the acceptability of the same and the verification of compliance with established legal requirements.

- After the Sarbanes-Oxley Act came into force in the United States, the Committee analysed and reported favourably on the «Regulation on the registration, communication and control of financial/accounting information for Telefónica Group», which was subsequently submitted for consideration and then approved by the Board of Directors.

- Other matters of interest analysed by this Committee were the following: the restructuring performed by virtue of the value adjustments by «Telefónica Móviles, S.A.» with respect to investments and its business in UTMS services in Europe and by «Telefónica DataCorp, S.A.» with respect to the investment in MediaWays; a general analysis of the Sarbanes-Oxley Act and its enacting regulations; accounting legislation applicable to pensions and other personnel commitments; impacts of the evolution of exchange rates on net worth.

In accordance with the provisions established in the new Spanish Financial Law, Telefónica's Board of Directors will propose at the next General Shareholders' Meeting the adoption of the modifications to the Articles of Association required in order to regulate the composition, jurisdictions and functioning of this Committee, based on the current regulations contained in the Regulations of the Board of Directors and incorporating the necessary modifications stipulated by the applicable legal provisions.

#### **Internal Audit**

The Company has a General Internal Audit Department responsible for internal audit matters and for ensuring the efficiency of the inter-

nal audit control of the different units of the Telefónica Group. This person has the following duties:

1. Guarantee the efficiency of the Group's internal control system.
2. Participate in the design of the control system according to risk evaluation and management.
3. Monitor the correct functioning of the system by reviewing the different processes which are critical for controlling business risks.
4. Review and notify control deficits that are detected in policies, methods, processes and procedures and which undermine business efficiency or increase the risk of undesired situations.
5. Review the security, control, efficiency, effectiveness and effective performance of information systems.
6. Any other functions which enhance the performance of the tasks entrusted to this person.

This General Internal Audit Department reports directly to the Audit and Control Committee, thus guaranteeing the adequate performance of all its functions and providing this Committee with continual and unlimited access to reports and work documents of the external auditors whenever it deems necessary.

#### **Nominating, Compensation and Corporate Governance Committee.**

Article 25 of the Regulations of the Board of Directors establishes the principles governing the func-

tioning of the Nominating, Compensation and Corporate Governance Committee as a sub-Committee of the Board of Directors. In July 2002, the name of this Committee was changed to the Nominating, Compensation and Corporate Governance Committee, assuming responsibilities in terms of corporate governance to support and inform the Board of Directors on matters relevant in this area.

The main function of the Nominating, Compensation and Corporate Governance Committee is to safeguard the integrity of the processes used to select the Company's Directors and senior executives, and to advise the Board of Directors on the determination and supervision of their remuneration.

Specifically, this Committee is assigned the following functions:

1. Provide information on proposed appointments of Company Directors and executive officers;
2. Approve the remuneration scales for the Company's senior directors;
3. Approve standard contracts for the Company's executive officers.
4. Determine the remuneration scale of the Executive Chairman or, in his absence, the Chief Operating Officer.
5. Establish the remuneration scale for Directors and review this on a regular basis in order to ensure that this complies with the duties performed by the Directors;

6. Provide information on incentive plans;

7. Prepare an annual report on the Director's and executive officers' remuneration policy.

8. Notify proposed appointments of members of the Executive Committee and other Committees of the Board of Directors; and

9. Prepare and keep a record of the situations of Company Directors and senior directors

The current composition of the Nominating, Compensation and Corporate Governance Committee is as follows:

- Mr. Alfonso Ferrari Herrero (Chairman)
- Mr. Maximino Carpio García
- Mr. Pablo Isla Álvarez de Tejera
- Mr. Gregorio Villalabeitia Galarraga

In accordance with the recommendations made in the Olivencia Report, all the members of this Committee are external or non-executive Directors.

The Nominating, Compensation and Corporate Governance Committee does not have a fixed number of meetings per year. It meets whenever the Board of Directors or its Chairman requests the issuance of a report or the approval of proposals within the scope of its responsibilities and provided that, in the opinion of the Committee's Chairman, this is necessary for the proper development of its functions.

In 2002, this Committee held eight (8) meetings. These were developed in accordance with a pre-esta-

blished agenda, issued beforehand to the Committee members together with the notice calling each meeting and the supporting documentation for each point on the aforementioned agenda for review and analysis by the Directors belonging to the Committee. This Committee's deliberations and the agreements and decisions adopted by it are recorded in the minutes corresponding to each session. A record was also taken of the documentation analysed at the meetings.

Throughout 2002, the Nomination, Compensation and Corporate Governance Committee had knowledge of all appointments of Company senior directors and changes in the management structure of both the Company and any of its subsidiaries, as well as proposed appointments of new members to the Boards of Directors of its Subsidiary companies and notified the abovementioned appointments and changes, in all cases favourably for subsequent approval by the Board of Directors.

This year Nominating, Compensation and Corporate Governance Committee has also reported and clarified possible conflict-of-interest situations affecting Company Board members or senior directors. In terms of remuneration, this Committee also agreed the Chairman's bonus and analysed the Chairman's remuneration. Similarly, the Stock Option plans of the different Group companies were examined and the Committee focused its analysis on companies which required such examination, accordingly.

Upon the request of the Chairman of Telefónica, during the first quarter of 2002, the Nominating, Compensation and Corporate Governance Committee provided information on the bonus of the Company's senior management for the year 2001,



as well as on the modification of the remuneration of senior directors.

In connection with its Corporate Governance new responsibilities, this Committee also began the task of examining the situation of the listed Companies of the Telefónica Group, in relation to the most relevant Corporate Governance recommendations, fostering the creation of sub-committees of the Board. At the end of year 2002, all the Group companies had set up and implemented consultative sub-Committees with responsibilities in the area of Audit and Control.

#### **Human Resources and Corporate Reputation Committee**

The Human Resources and Corporate Reputation Committee (originally the Human Resources Committee) was set up in accordance with the provision contained in Article 26 of the Regulations of the Board of Directors. Subsequently, the Board of Directors, at its meeting held on June 26th, 2002, agreed to assign new responsibilities to the Human Resources Committee in the area of Corporate Reputation, approving the new name of the aforementioned Committee as the Human Resources and Corporate Reputation Committee.

In terms of the object and functions of this Committee in the area of Human Resources, its fundamental mission, without prejudice to other functions that may be assigned to it by the Board of Directors, consists in analysing, informing and offering proposals to the Board for the adoption of appropriate agreements with respect to the Company's personnel policy.

In terms of Corporate Reputation, this Committee's functions include promoting both the development of the Telefónica Group's Corporate Reputation project and fostering the implementation of the Telefónica Group's core values.

This Committee is currently formed by the following Directors:

- Mr. Pablo Isla Alvarez de Tejera (Chairman)
- Mr. Alfonso Ferrari Herrero.
- Mr. Antonio Massanell Lavilla
- Mr. Enrique Used Aznar

In accordance with the recommendations made in the Olivencia Report, all the members which take part of this Committee are external or non-executive Directors.

Since June 2002, the Human Resources and Corporate Reputation Committee has held three (3) meetings, which have been attended by all its members. These meetings took place according to a pre-established Agenda issued beforehand to the Committee members. The meetings were attended by the members of the management team responsible for the corporate areas of Human Resources and Corporate Reputation. The deliberations during the Committee's meetings and the agreements or decisions adopted by it are documented in the minutes corresponding to each meeting.

In 2002 the matters discussed and analysed by this Committee included the following:

- development and implementation of the Telefónica Group's Corporate Reputation plan.

- development plans for Human Resources, directors and talented young employees with great potential; and
- analysis of the Telefónica Group Human Resources management report.

#### **Regulation Committee**

The main objective of the Regulation Committee, is to monitor, through the study, analysis and discussion on an on-going basis, of the main aspects on the regulatory agenda which affect the Telefónica Group at any time. Another mission of this Committee is to act as a communication and information channel between management and the Board of Directors in regulatory matters and, whenever necessary, to notify the Board of Directors of any matters that it deems to be of maximum priority for the Company and which require the taking of decisions or the establishment of a specific strategy.

The current composition of this Committee, following the reorganization approved by Board of Directors of Telefónica at its meeting of June 26<sup>th</sup>, 2002, is as follows:

- Mr. Enrique Used Aznar (Presidente)
- Mr. Jesús Maldonado Ramos
- Mr. José Antonio Fernández Rivero
- Mr. Antonio Alonso Ureba

This Committee is formed by an Executive Director and three non-executive Directors, two of whom are independent.

During 2002, this Committee met four (4) times and its meetings were attended by almost all its members.

The agenda of each meeting was issued beforehand to its members together with the notice calling each meeting and at least five days before the date of the meeting. The Secretary of the Committee recorded the minutes of each meeting.

This Committee's meetings were normally attended by the General Manager and the Deputy General Manager of Corporate Regulation, the Deputy General Secretary and Telefónica's Manager of Telecom Regulation Department.

Similarly, this Committee was attended by some of the most senior representatives of the Regulation divisions of Subsidiary companies domiciled abroad, as well as leading executives from the Group's business lines, in order to provide information on the situation and regulatory problems in their respective areas.

The most significant matters considered by the Regulation Committee in 2002 included the following:

- Regulatory situation of Telefónica de España;
- Regulatory situation of Telefónica Móviles España;
- Most important regulatory issues in Chile;
- Most important regulatory issues in Peru; and
- Implementation of the new European regulatory framework (Directives and Community Directives).

#### **Service Quality and Customer Service Committee.**

The fundamental mission of the Service Quality and Customer Service sub-Committee is the

examination, analysis and regular monitoring of the quality indices of the main services rendered by Telefónica Group companies, as well as the levels of commercial services offered to its clients.

In order for this Committee to confirm and analyse the fulfilment of the established objectives, its Chairman has requested each line of business of the Telefónica Group to provide a summary of their variable targets for 2003. A work method has also been envisaged which will enable the issuance of quarterly reports by each business line in connection with the evolution of its objectives based on established indicators and quality ratios for each of its businesses.

The current composition of this Committee is as follows:

- Mr. Gonzalo Hinojosa Fernández de Angulo (Chairman)
- Mr. Carlos Colomer Casellas
- Mr. José Maldonado Ramos
- Mr. Antonio Massanell Lavilla

In accordance with the recommendations made in the Olivencia Report, all members of this Committee are external or non-executive Directors.

Since June 2002, this Committee has met on two (2) occasions; these meetings lasted for approximately six hours each. The Committee meetings follow a pre-established agenda, which is sent together with the corresponding documentation, to its members fifteen days prior to the date of the meeting. The Secretary of the Com-

mittee records the minutes corresponding to each meeting.

The meetings of this Committee were attended by representatives of the business lines that have implemented quality procedures. Thus, the meetings of this Committee were attended by quality managers and executive directors of Telefónica de España, S.A., Telefónica Móviles España, S.A., Telefónica de Latinoamérica, Telefónica Data España, S.A., Terra Networks, S.A., Grupo Atento Servicios Corporativos, Vía Digital Distribuidora de Televisión Digital, S.A. (DTS), Telefónica Publicidad e Información, S.A. (TPI), as well as the Deputy General Manager of Corporate Reputation of Telefónica.

The main issues analysed in 2002 were as follows:

- Description of the existing Quality Plans;
- Achievement of the quality objectives in the year 2002;
- Projects and objectives for 2003; and
- Quality measurement tools or instruments.