consolidated annual financial statement and management report for 2002

for the year ended december 31, 2002
Telefónica S.A. and Subsidiaries

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AUDITORS' REPORT ON COSOLIDATED FINANCIAL STATEMENTS

Translation of a report originally issued in Spanish based on our work performed in accordance with generally accepted auditing standards in Spain and of consolidated financial statements originally issued in Spain and prepared in accordance with generally accepted accounting principles in Spain (see Note 25). In the event of a discrepancy, the Spanish-language version prevails.

To the Stockholders of Telefónica, S.A.:

1. We have audited the consolidated financial statements of Telefónica, S.A. and of the companies composing the Telefónica Group (see Note 1) comprising the consolidated balance sheet as of December 31, 2002, and the related consolidated statement of operations and notes to consolidated financial statements for the year then ended. The preparation of these consolidated financial statements is the responsibility of the Parent Company's directors. Our responsibility is to express an opinion on the consolidated financial statements taken as a whole based on our audit work performed in accordance with generally accepted auditing standards, which require examination, by means of selective tests, of the documentation supporting the consolidated financial statements and evaluation of their presentation, of the accounting principles applied and of the estimates made.

2. As required by Spanish corporate law, for comparison purposes the directors present, in addition to the 2002 figures for each item in the consolidated balance sheet and consolidated statements of operations and of changes in financial position, the figures for 2001. Our opinion refers only to the 2002 financial statements. Our auditors' report dated March 14, 2002, on the 2001 consolidated financial statements contained an opinion qualified for an uncertainty concerning the Telefónica Group's net investment in Argentina, and in an emphasis paragraph we indicated the intention of management to update and review, on a yearly basis, the business plans of the Group companies that hold third-generation wireless telephony (UMTS) licenses and, where appropriate, to make any value adjustments that might be required.

   In view of the changes in 2002 in the assumptions on which the aforementioned business plans were based, of the findings of reports commissioned from third parties and of the fact that the aforementioned wireless telephony technology is not yet commercially available, the directors of Telefónica Móviles, S.A. announced their decision to temporarily discontinue and restructure this company's business activities in Germany, Italy, Austria and Switzerland, and in 2002 they recorded the related write-down for accounting purposes, as described in Note 1, which gave rise to a charge, net of the related tax effect, of €4,958 million, to the consolidated statement of operations of Telefónica, S.A.

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Deloitte & Touche España, S.L. Inscrita en el Registro Mercantil de Madrid, tomo 13.650, folio 188, sección 8, hoja M-54414.
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3. Also, as a result of the depreciation of the Argentine peso with respect to the U.S. dollar and the euro in 2002, losses of €1,147 million and €355 million were recorded under the consolidated "Stockholders' Equity – Translation Differences in Consolidation" caption and in the consolidated statement of operations, respectively. However, certain uncertainties remain regarding the effect that the evolution of certain economic measures will have on the normal course of operations and on the financing thereof in Argentina (mainly that relating to the establishment of the wireline telephony rates). Accordingly, it is not yet possible to assess whether there will be any additional effects for accounting purposes on the Telefónica Group's net investment in these companies, which, calculated as described in Note 1, amounted to €1,637 million as of December 31, 2002, a substantial reduction with respect to the previous year.

4. In our opinion, except for the effects of any adjustment which might be required if the final outcome of the uncertainty regarding the Group's net investment in the companies located in Argentina described in paragraph 3 above were known, the consolidated financial statements for 2002 referred to above present, in all material respects, a true and fair view of the net worth and financial position of Telefónica, S.A. and of the companies composing the Telefónica Group as of December 31, 2002, and of the results of their operations and of the funds obtained and applied by them in the year then ended, and contain the required information, sufficient for their proper interpretation and comprehension, in conformity with generally accepted accounting principles and standards applied on a basis consistent with that of the preceding year.

5. The accompanying consolidated management report for 2002 contains the explanations which the directors of Telefónica, S.A. consider appropriate about the Group's situation, the evolution of its business and other matters, but is not an integral part of the consolidated financial statements. We have checked that the accounting information in the consolidated management report is consistent with that contained in the consolidated financial statements for 2002. Our work as auditors was confined to checking the consolidated management report with the aforementioned scope, and did not include a review of any information other than that drawn from the accounting records of the consolidated Companies.

DELOITTE & TOUCHE ESPAÑA, S.L.
Inscrita en el R.O.A.C. nº S0692

Eduardo Sanz Hernández
Socio

February 26, 2003

Translation of consolidated financial statements originally issued in Spanish and prepared in accordance with generally accepted accounting principles in Spain (see Note 25). In the event of a discrepancy, the Spanish-language version prevails.

Telefónica Group
Consolidated balance sheets as of december 31, 2002 and 2001

ASSETS (Millions of Euros)

	2002	2001
A) Due from stockholders for uncalled capital	**292.49**	**370.10**
B) Fixed and other noncurrent assets	**50,008.83**	**63,975.75**
I. Start-up expenses	**496.48**	**730.45**
II. Intangible assets (Note 6)	**7,629.57**	**16,959.14**
Research and development expenses	1,179.15	1,049.59
Administrative concessions	6,350.20	15,011.19
Rights on leased assets	84.40	137.69
Other intangible assets	4,321.83	4,087.57
Accumulated amortization and allowances	(4,306.01)	(3,326.90)
III. Property, plant and equipment (Note 7)	**27,099.65**	**36,606.09**
Land and structures	6,159.15	7,097.90
Plant and machinery	3,739.81	3,365.73
Telephone installations	53,758.90	62,975.46
Furniture, tools, etc.	3,132.06	3,851.74
Construction in progress	986.15	3,034.89
Advances on property, plant and equipment	66.15	53.20
Installation materials	162.63	154.12
Accumulated depreciation and allowances	(40,905.20)	(43,926.95)
IV. Long-term investments (Note 8)	**14,783.13**	**9,680.07**
Investments in associated companies	2,081.19	3,099.14
Other investments	932.03	870.78
Other loans	2,225.26	2,038.12
Long-term deposits and guarantees given	160.77	232.98
Taxes receivable (Note 18)	9,679.42	3,757.78
Allowances	(295.54)	(318.73)
C) Consolidation goodwill (Note 5)	**6,364.02**	**9,128.94**
D) Deferred charges (Note 9)	**802.28**	**710.94**
E) Current assets	**10,573.67**	**12,236.84**
I. Due from stockholders for capital calls	**–**	**2.25**
II. Inventories	**449.83**	**754.10**
Inventories	498.64	785.10
Advances	14.81	22.49
Allowances	(63.62)	(53.49)
III. Accounts receivable	**6,029.15**	**8,003.99**
Trade receivables (Note 10)	5,922.88	6,783.24
Receivable from associated companies	148.59	74.00
Sundry accounts receivable	657.05	866.31
Employee receivables	58.08	79.35
Taxes receivable (Note 18)	1,055.37	2,077.48
Allowance for bad debts (Note 10)	(1,663.56)	(1,692.89)
Allowance for sundry accounts receivable	(149.26)	(183.50)
IV. Short-term investments (Note 8)	**3,031.67**	**2,306.53**
Loans to associated companies	303.53	278.51
Short-term investment securities	1,963.87	807.40
Other loans	770.05	1,222.90
Allowances	(5.78)	(2.28)
V. Short-term treasury stock (Note 11)	**334.56**	**260.70**
VI. Cash	**543.91**	**621.88**
VII. Accrual accounts	**184.55**	**287.39**
Total assets (A+B+C+D+E)	**68,041.29**	**86,422.57**

The accompanying Notes 1 to 25 and Exhibits I to VI are an integral part of these consolidated balance sheets.

Translation of consolidated financial statements originally issued in Spanish and prepared in accordance with generally accepted accounting principles in Spain (see Note 25
In the event of a discrepancy, the Spanish-language version prevails.

Telefónica Group
Consolidated balance sheets as of december 31, 2002 and 2001
STOCKHOLDERS' EQUITY AND LIABILITIES (Millions of Euros)

	2002	2001
A) Stockholders' equity (Note 11)	**16,996.00**	**25,861.62**
I. Capital stock	**4,860.66**	**4,671.92**
II. Additional paid-in capital	**11,670.02**	**11,670.02**
III. Revaluation reserves	**2,870.90**	**3,059.64**
IV. Other reserves of the Parent Company	**5,808.90**	**4,298.65**
Unrestricted reserves	4,816.37	3,379.98
Restricted reserves	992.53	918.67
V. Reserves at fully consolidated companies	**4,402.65**	**3,773.35**
VI. Reserves at companies accounted for by the equity method	**(532.51)**	**(440.48**
VII. Translation differences in consolidation	**(6,507.82)**	**(3,278.29**
VIII. Income (Loss) for the year	**(5,576.80)**	**2,106.81**
Income (Loss) of the Parent Company and subsidiaries	(10,844.53)	2,212.29
Income of associated companies	(527.88)	(376.49
Loss attributable to minority interests (Note 12)	5,795.61	271.01
B) Minority interests (Note 12)	**5,612.93**	**7,433.55**
C) Negative consolidation goodwill	**11.36**	**7.95**
D) Deferred revenues (Note 13)	**880.46**	**1,145.75**
E) Provisions for contingencies and expenses (Note 14)	**8,014.91**	**5,862.70**
F) Long-term debt	**21,726.15**	**27,692.41**
I. Debentures, bonds and other marketable debt securities (Note 15)	**12,969.22**	**14,460.86**
Nonconvertible debentures and bonds	12,351.50	14,380.86
Other marketable debt securities	617.72	80.00
II. Payable to credit institutions (Note 16)	**6,912.94**	**8,079.08**
III. Payable to Group and associated companies	**–**	**–**
IV. Other payables	**206.68**	**3,602.8**
Other payables (Note 19)	179.05	3,541.28
Notes payable	27.63	61.52
V. Taxes payable (Note 18)	**1,629.46**	**1,541.08**
VI. Uncalled capital payments payable	**7.85**	**8.59**
G) Current liabilities	**14,681.74**	**18,418.59**
I. Debentures, bonds and other marketable debt securities (Note 15)	**2,625.63**	**2,857.72**
Debentures	1,056.20	944.12
Other marketable debt securities	1,280.48	1,600.27
Interest on debentures and other securities	288.95	313.33
II. Payable to credit institutions	**4,193.27**	**6,298.89**
Loans and other accounts payable (Note 16)	4,072.67	6,163.54
Accrued interest payable	120.60	135.35
III. Payable to associated companies	**22.90**	**30.96**
IV. Trade accounts payable	**5,113.15**	**5,231.44**
Advances received on orders	73.43	137.94
Accounts payable for purchases and services	5,014.13	5,058.77
Notes payable	25.59	34.73
V. Other nontrade payables	**2,289.37**	**3,606.93**
Taxes payable (Note 18)	1,048.52	1,624.15
Other nontrade payables (Note 19)	1,240.85	1,982.78
VI. Accrual accounts	**437.42**	**392.65**
H) Short-term provisions for contingencies and expenses (Note 14)	**117.74**	**–**
Total stockholders' equity and liabilities (A+B+C+D+E+F+G+H)	**68,041.29**	**86,422.57**

The accompanying Notes 1 to 25 and Exhibits I to VI are an integral part of these consolidated balance sheets.

Translation of consolidated financial statements originally issued in Spanish and prepared in accordance with generally accepted accounting principles in Spain (see Note 25). In the event of a discrepancy, the Spanish-language version prevails.

Telefónica Group

Consolidated statements of operations for the years ended december 31, 2002 and 2001

DEBIT (Millions of Euros)

		2002	2001
A)	**Expenses**		
	Variation in inventories	**49.22**	**109.58**
	Procurements	**6,953.59**	**7,111.86**
	Purchases	2,978.44	3,197.71
	Work performed by other companies	3,975.15	3,914.15
	Personnel expenses (Note 20)	**4,793.77**	**5,390.26**
	Depreciation and amortization expense	**6,692.42**	**7,373.98**
	Property plant and equipment (Note 7)	5,370.07	6,194.17
	Intangible assets (Note 6)	1,132.25	1,023.48
	Deferred charges	190.10	156.33
	Variation in operating allowances	**645.58**	**1,023.80**
	Variation in allowance for inventories	37.46	2.42
	Variation in allowance for bad debts (Note 10)	555.64	992.53
	Variation in other allowances	52.48	28.85
	Other operating expenses	**5,070.37**	**5,603.62**
	Outside services	4,564.61	4,945.49
	Taxes other than income tax	412.10	588.82
	Other operating expenses	93.66	69.31
I.	**Operating income**	**5,031.75**	**5,430.28**
	Interest on payables to associated companies	0.10	0.01
	Other interest on accounts payable and similar expenses (Note 20)	1,784.14	1,988.02
	Amortization of deferred interest expenses	43.23	55.43
	Variation in investment valuation allowances	99.63	21.46
	Exchange losses (Note 20)	2,245.17	2,026.88
II.	**Financial income**	**–**	**–**
	Share in losses of companies accounted for by the equity method	536.88	445.70
	Amortization of consolidation goodwill (Note 5)	667.49	845.19
III.	**Income from ordinary activities**	**1,616.82**	**1,821.05**
	Variation in fixed asset and investment valuation allowances (Notes 7 and 8)	136.48	(599.56)
	Losses on fixed assets (Note 20)	9,614.55	232.99
	Losses on disposal of investments in consolidated companies (Note 8)	206.44	3.86
	Extraordinary expenses and losses (Note 20)	6,735.04	1,317.01
IV.	**Extraordinary income**	**–**	**212.83**
V.	**Income before taxes**	**–**	**2,033.88**
	Corporate income tax (Note 18)	(3,340.59)	(816.32)
	Foreign taxes (Note 18)	111.94	1,014.40
VI.	**Income for the year**	**–**	**1,835.80**
	Income attributed to minority interests (Note 12)	182.39	309.39
VII.	**Income for the year**	**–**	**2,106.81**

The accompanying Notes 1 to 25 and Exhibits I to VI are an integral part of these consolidated statements of operations.

Translation of consolidated financial statements originally issued in Spanish and prepared in accordance with generally accepted accounting principles in Spain (see Note 25
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Telefónica Group

Consolidated statements of operations for the years ended december 31, 2002 and 2001

CREDIT (Millions of Euros)

	2002	2001
B) Revenues		
Net sales and services (Note 20)	28,411.30	31,052.60
Variation in work-in-process	31.12	5.67
Capitalized expenses of Group work on fixed assets	496.71	730.37
Other operating revenues	**297.57**	**254.74**
Non-care and other current operating revenues	230.21	194.25
Subsidies	14.71	7.25
Overprovision for contingencies and expenses	52.65	53.24
I. Operating loss	**–**	**–**
Revenues from equity investments	**17.43**	**21.29**
Other companies	17.43	21.29
Revenues from other equity investments and loans (Note 20)	**320.37**	**435.19**
Associated companies	31.07	15.38
Other companies	289.30	419.81
Exchange gains (Note 20)	**1,612.85**	**1,244.20**
II. Financial loss	**2,221.62**	**2,391.12**
Share in the income of companies accounted for by the equity method	9.00	69.21
Reversal of negative consolidation differences	2.06	3.57
III. Loss on ordinary activities	**–**	**–**
Gains on fixed asset disposals	55.56	10.15
Gains on disposals of investments in consolidated companies (Note 8)	99.32	305.95
Capital subsidies (Note 13)	63.79	80.03
Extraordinary revenues (Note 20)	255.96	771.00
IV. Extraordinary loss	**16,217.88**	**–**
V. Loss before taxes	**14,601.06**	**–**
VI. Consolidated loss for the year	**11,372.41**	**–**
Loss attributed to minority interests (Note 12)	5,978.00	580.40
VII. Loss for the year	**5,576.80**	**–**

The accompanying Notes 1 to 25 and Exhibits I to VI are an integral part of these consolidated statements of operations.

Telefónica, S.A. and subsidiaries composing the Telefónica Group

Notes to consolidated financial statements for the year ended december 31, 2002

(1) Introduction and general information

Telefónica Group companies

Telefónica, S.A. and its subsidiaries and investees make up an integrated group of companies ("the Telefónica Group") operating mainly in the telecommunications, media and entertainment industries.

The Parent Company of this Group is Telefónica, S.A. ("Telefónica"), a corporation that was incorporated for an indefinite period of time on April 19, 1924. Its registered office is at calle Gran Vía 28, Madrid (Spain).

Exhibit I hereto lists the subsidiaries, associated companies and investees in which the Telefónica Group has direct or indirect holdings, their lines of business, their location, their net worth and results at year-end, their gross book value, their contribution to the reserves of the Consolidated Group and the method by which they were consolidated.

Corporate structure of the Group

Telefónica's basic corporate purpose, per Article 4 of its bylaws, is the provision of all manner of public and private telecommunications services, and all manner of ancillary or supplementary telecommunications services or the services derived therefrom. All the business activities that constitute the corporate purpose may be performed either in Spain or abroad and may be carried on either wholly or partially by the Company, or through shareholdings or other equity interests in other companies or legal entities with an identical or similar corporate purpose.

The main groups of subsidiaries through which Telefónica carries out its corporate purpose and manages its business areas or basic lines of business are as follows:

– The wireline telephony business and the related supplementary services provided in Spain centered at the Telefónica de España Group.
– The cellular telephony business is centralized in Spain and abroad at the Telefónica Móviles Group.
– The main business activity of the Telefónica Internacional Group is to make and manage investments in the wireline telephony industry in the Americas.
– Telefónica de Contenidos and its subsidiaries group together the Group's interests in the media and entertainment area.
– The main business activity of the Telefónica Datacorp Group is the integral provision of data transmission services for companies.
– Services, content and portals for Internet access, focusing in particular on residential customers and small businesses (SOHO), are provided by the Terra Lycos Group.
– The Atento Group carries on the call center activity.
– The Telefónica Publicidad e Información Group handles the telephone directory business.
– Also, the Emergia Group operates a high-speed fiber optic network with connections within Latin America and Europe and from Latin America to Europe and the U.S.

Certain business activities carried on by the Telefónica Group are currently at the development or start-up phase. In order to be able to take decisions regarding the investments made, management of the various Group companies prepared the related business plans, approved by their stockholders, the results of which enable the recoverability of the investments made to be verified. Since these analyses and studies are based on assumptions, variances may arise and, accordingly, they are analyzed periodically in order to monitor the results obtained and, where appropriate, to make any value adjustments that might be required (see Note 5 and the following section).

The business activities carried on by most of the Telefónica Group companies are regulated by various pieces of legislation, under which authorizations or licenses must be obtained in certain circumstances in order to be able to provide the various services.

Also, certain business activities, such as wireline and wireless telephony, are carried on under regulated rate and price systems.

The Group company Telefónica de España, S.A.U., which carries on its business activities in a new regulatory and legislative framework as a result of the deregulation of the telecommunications industry in Spain initiated in 1987, is a special case.

One of the main problems of the ratemaking system applicable to this company (determined through a resolution adopted by the Government Standing Committee on Economic Affairs on April 19, 2001, and published pursuant to a Ministerial Order dated May 10, 2001, modifying the Government Standing Committee on Economic Affairs resolution dated July 27, 2000, and published pursuant to a Ministerial Order dated July 31, 2000) is that derived from the License Contract entered into with the Spanish State in 1991 in relation to the guarantee to maintain the overall financial balance of the license. Neither the rate imbalance due to the access shortfall nor the interconnection rates for the period from the commencement of market deregulation to the present date have yet been satisfactorily resolved.

The General Telecommunications Law establishes as a general principle that operators may freely set their rates. Transitional Provision Four of the Law provides that the Government Standing Committee on Economic Affairs, acting on the basis of a report issued by the Telecommunications Market Commission, may establish, on a transitional basis, maximum or minimum fixed prices or the methods for establishing them, based on the actual cost of providing the service and on the degree of competition among of operators in the market for the various services.

It also acknowledges the existence of the imbalance in the rates currently in force and the need to rectify this, as well as the possibility of compensating the dominant operator for the access shortfall that might arise for it as a result of this imbalance.

It should be noted in this regard that Telefónica filed a complaint with the European Commission against the Spanish State for its failure to comply with EU legislation establishing the need to resolve the rate rebalancing problem prior to the opening up of the market to free competition. On January 29, 2001, the European Commission delivered a Reasoned Opinion addressed to the Kingdom of Spain, in which it concluded that the Spanish Government had failed to comply with Directives 90/388/EEC and 96/19/EEC by not having authorized Telefónica de España to increase its monthly charges sufficiently to cover costs and by not having provided sufficient information to the Commission. At the end of December 2001 the European Commission decided to refer the infringement proceeding brought against Spain to the High Court of Justice in Luxembourg, which has not yet handed down a decision.

Also, in November 1999 Telefónica, S.A. and Telefónica de España, S.A. filed a claim with the Council of Ministers and the Ministry for Development (now the Ministry of Science and Technology) requesting economic compensation for the losses derived from the breakdown of the financial equilibrium under the 1991 License Contract or, alternatively, for the Government's failure to fulfill the rate rebalancing obligation. This claim has not yet been resolved by the Government.

Also, in November 1999 Telefónica, S.A. and Telefónica de España, S.A. filed a claim with the Spanish Council of Ministers and the Ministry for Development (now the Ministry of Science and Technology) demanding economic compensation for the loss suffered as a result of the failure to maintain of the financial balance of the license contract or, alternatively, the Government's breach of the obligation to restore the rate balance. The Spanish authorities have not yet handed down a decision on this claim.

Salient events in the year

The Terra Lycos Group

The Internet business activity carried on by the Telefónica Group mainly through the Terra Lycos Group has been evolving progressively to adapt to the new circumstances. One of the most noteworthy aspects to be taken into account when analyzing the growth and development of this business in 2002 is the adverse macroeconomic situation in the countries in which the Terra Lycos Group is present. To the negative consequences of this situation for these companies in terms of revenues must be added the additional negative impact of the exchange rates of certain currencies on their income statements. Added to this adverse macroeconomic scenario in 2002 was the worsening in the crisis of online advertising and the Internet market. The political and social instability being experienced by certain of the main countries in which the Terra Lycos Group, fundamentally, is present is also noteworthy. As regards the business model itself, in 2002 there was shift towards a model based on access charges, pay content and customized advertising.

At 2002 year-end the Parent Company carried out a study of the evolution of business plans for the years from 2003 to 2006, and of the estimated forecasts of the subsidiaries on the basis of growth up to 2012. In addition, a specific study on the goodwill arising in the acquisition of Lycos, Inc. was commissioned from a third party. Th objective of these analyses was to determine the recovery of th goodwill, capitalized tax assets, and of other fixed assets in the con solidated balance sheet of the Terra Lycos Group, on the basis of th estimated future value that each of the businesses and countrie will generate, in accordance with the accounting principle of pru dence in valuation.

As a result of these studies, as of December 31, 2002 consolidatio goodwill amounting to €856.65 million was written down and capi talized tax credits amounting to €272.59 million were reversed i the accompanying consolidated financial statements (see Notes 5 and 18).

Also, provisions for intangible assets and property, plant and equip ment amounting to €21.42 million and €32.14 million, respectivel were recorded, and €56.62 million of start-up expenses were writ ten off.

The net impact of these effects and of the write-down of goodwi relating to the agreements entered into by the Terra Lycos Group an Telefónica (see Notes 5 and 23) on the consolidated statement o operations of the Telefónica Group, after taking into account the ta effects and minority interests, amounted to €401.33 million.

The UMTS wireless telephony business

In 2000 and 2001 certain Telefónica Móviles Group companie obtained third-generation wireless telephony (UMTS) licenses i Spain, Germany, Italy, Austria and Switzerland. Since the acquisitio of these licenses, Telefónica Móviles has launched various initiative aimed at enhancing its business plans, as a result of which the Ge man operator Group 3G entered into roaming and infrastructur sharing agreements with another operator in Germany, thereb commencing operations as a GSM Virtual Wireless Network Opera tor at the end of 2001.

However, since then significant technological changes and change affecting the market and its competitors have led Telefónica Móvile to review the assumptions underlying the business plans of it investees in Germany, Italy, Austria and Switzerland and to reconside its short- and medium-term strategy in these countries.

In view of the variances arising in the first six months of operation of Group 3G with respect to the objectives set, the continuing dela in the commercial availability of UMTS technology, the significan downward revisions of the estimated demand for 3G services an the increased penetration of European markets by alread established operators, making it more difficult for new entrants t obtain a critical mass, Telefónica Móviles decided (i) to put on hold it commercial activities in Germany and (ii) to commissio independent experts to assess the business plans of the UMT operators in Germany, Italy, Austria and Switzerland.

Based on the new assessments obtained, and to ensure that th investments are correctly valued at all times, Telefónica Móvile decided to eliminate the risk exposure in its books relating to th investments in Germany, Austria and Switzerland. Regarding th investment in Italy, Telefónica Móviles estimated the value of th UMTS license of Ipse 2000, S.p.A. at €300 million (risk exposure o €138 million for the Telefónica Group). In the first three countrie the coverage requirements laid down in the licenses might come into force earlier than in Italy and, accordingly, in view of the delay in the commercial viability of the technology with respect to the initial estimates, Telefónica Móviles, in accordance with the accounting principle of prudence in valuation, wrote down these investments for accounting purposes. In Italy the license terms and conditions make it possible to implement business plans with lower investments than in the other countries, since assignment of the right to use the spectrum is envisaged. For these reasons, based on the business plans analyzed to date, it should be possible to recover the remaining value assigned to the license. Also, license awardees which were not operating formerly in Italy received 5 mHz of additional spectrum for g827 million and could avail themselves of a deferred payment arrangement. Ipse 2000 has requested the return of this additional spectrum and the modification of the related payment. The latter amount was included in the value of the license prior to the write-down indicated below.

Telefónica Móviles is continuing to make every effort to obtain value from the aforementioned investments and, although future revenues may be obtained from the operation of these licenses, the Group, in view of the current uncertainty, in accordance with the accounting principle of prudence in valuation, recorded a net loss of g4,958.22 in the consolidated financial statements of the Telefónica Groups as of December 31, 2002, which includes mainly asset write-downs, labor force restructuring expenses and expenses relating to the termination of contracts.

The detail, by caption, of the effect of the write-downs and restructuring expenses arising from the decisions adopted on the 2002 consolidated statement of operations and consolidated balance sheet of the Telefónica Group is as follows:

Millions of Euros

Losses on intangible assets (Note 6)	9,445.01
Losses on property, plant and equipment	81.18
Write-off of goodwill (Note 5)	61.22
Provisions for contingencies and expenses (*) (Note 20)	2,753.90
Income/Loss of companies accounted for by the equity method	34.39
Corporate income tax (Note 18)	(2,837.16)
Loss attributed to minority interests (Note 12)	(4,580.32)
Total effect	**4,958.22**

(*) Including g1,892.44 million relating to the investment of the associated company Ipse 2000 since as of the date of preparation of these consolidated financial statements this company had not recorded the value adjustment to its assets. The remainder relates to the absorption of losses of minority interests (g382.44 million - see Exhibit IV) and to the assumption of various commitments based on the decisions adopted.

Devaluation in Argentina

In view of its international presence, the Telefónica Group, like other corporations, has been affected by the economic situation in Argentina through the various Group companies operating there. As of December 31, 2002 and 2001, the Telefónica Group's exposure at the various Argentine companies amounted to g968.12 million and g3,124.83 million, respectively, including the related goodwill, intercompany financing and the asset value assignable to those investments (after inclusion of the losses of these companies before the related tax effect, which amounts to g669.01 million and g457.5 in 2002 and 2001, respectively). The most significant exposure as of December 31, 2002, related to Telefónica de Argentina, S.A., amounting to g809.23 million (g2,128.68 million in 2001) and Telefónica Móviles Argentina amounting to g112.53 million (g507.66 million in 2001). Also noteworthy in 2001 were the Telefónica de Contenidos Group companies (g413.71 million).

As of December 31, 2001, there was no explicit Argentine peso/euro exchange rate that could be taken as representative. Also, pursuant to an executive decision, in early 2002 the Argentine peso was devalued with respect to the euro, an event to which the market reacted subsequently.

Taking into account Spanish accounting legislation, the express communications from the Spanish Accounting and Audit Institute regarding the way in which this devaluation should be treated at 2001 year-end and the international accounting rulings in force, in preparing its consolidated financial statements for 2001 the Telefónica Group used peso/euro and peso/U.S. dollar exchange rates of ARP 1.5149/g1 and ARP 1.7/US$ 1 at year-end as the first representative exchange rates prevailing in the market after December 31, 2001, following the aforementioned devaluation. At 2002 year-end, with the normal currency exchange market re-established, the exchange rate used was ARP 3.5341/g1 (ARP 3.37/US$ 1). These exchange rates were used to include in the consolidated financial statements the assets and liabilities of the Argentine subsidiaries and associated companies and to assess the status of their assets as regards their solvency, the value of their investments, their viability, the recoverability of goodwill, etc.

In accordance with the foregoing, these consolidated financial statements reflect an adverse impact on consolidated earnings and on the "Stockholders' Equity - Translation Differences in Consolidation" caption of g354.68 million and g1,147.09 million, respectively, in 2002 (g369.00 million and g1,424.10 million, respectively, in 2001).

The matters still not resolved include the necessary renegotiation with the Argentine Government of the future rates due to the effect of the provisions of Law 25.561. Accordingly, although the book value of the fixed assets was maintained on the basis of estimates based on the information currently available, neither the results of the negotiations relating to rate levels nor, therefore, the future sales revenues and net cash flows can be predicted.

Given that the aforementioned circumstances had not occurred at the date of preparation of these consolidated financial statements and that it is not certain that they will occur, it was not possible to quantify their effect, if any, on the consolidated financial statements as of December 31, 2002.

(2) Basis of presentation of the consolidated financial statements

a) True and fair view

The accompanying consolidated financial statements of the Telefónica Group were prepared from the accounting records of Telefónica, S.A. and of each of the companies composing the Telefónica Group. The respective individual financial statements were prepared in accordance with the accounting principles and standards regulated in Spain by the Commercial Code as implemented by the Spanish National Chart of Accounts and in the applicable regulations in the different countries in which the companies composing the Consolidated Group are located. The accompanying consolidated financial statements are presented in accordance with the regulations for the preparation of consolidated financial statements, as approved by Royal Decree 1815/1991, and, accordingly, they give a true and fair view of the net worth, financial position, results of operations and funds obtained and applied in 2002.

b) Accounting policies

The consolidation methods applied were as follows:

– The companies over which effective control is exercised or in relation to which the Company has entered into agreements with the other stockholders were fully consolidated.
– The companies which are managed jointly with third parties were proportionally consolidated.
– The companies in which there is significant influence but not ownership of a majority of the voting rights in their governing bodies or joint management with third parties are accounted for by the equity method.
– The investees which are either not included in the foregoing points or which, although included, do not have a material impact on the consolidated financial statements, are carried at the lower of cost or market.

In certain circumstances, at some of the Group's investees a qualified majority of the voting rights may be required to adopt certain resolutions, and this was taken into account when selecting the consolidation method.

All material accounts and transactions between the consolidated companies were eliminated in consolidation.

In the case of Group companies whose accounting and valuation methods differed from those of Telefónica, adjustments were made in consolidation in order to present the consolidated financial statements on a uniform basis with the financial statements of the Parent Company.

The margins included in the invoices issued by subsidiaries to other Telefónica Group companies for capitalizable assets or services were eliminated in consolidation.

The consolidated statement of operations includes the revenues and expenses of the companies that are no longer in the Group up to the date on which the related holding was sold or the company was liquidated, and those of the new companies included in the Group from the date on which the holding was acquired or the company was formed through year-end.

The equity of minority interests in the net worth and results of the fully consolidated subsidiaries is recorded under the "Minority Interests" and "Income/Loss Attributed to Minority Interests" captions, respectively (see Note 12).

In accordance with standard practice in Spain, the accompanyin consolidated financial statements do not include the tax effect, i any, of transferring the reserves of the consolidated subsidiaries an of the companies accounted for by the equity method to the Paren Company's accounts, since it is considered that such reserves will b used to finance these companies' operations and that those tha may be distributed would not give rise to a material additional ta cost.

c) Comparative information and changes in the scope of consolidation

Comparative information

The figures in these consolidated financial statements and in th consolidated management report are expressed in millions of euro unless indicated otherwise.

There were no changes in the structure of the consolidated balanc sheet and consolidated statement of operations with respect t those presented in the previous year. Also, there were no changes i accounting principles with respect to 2001 with a significant effect However, as indicated in Note 1, in 2002 significant accountin write-downs were made based on the analyses performed.

Changes in the scope of consolidation

The main variations in the scope of consolidation in 2002 were a follows (the full detail of all the variations in 2002 and 2001 i included in Exhibit II):

2002

Telefónica

In March 2002, under the last part of the agreement entered into i the previous year between Iberdrola, S.A. and Telefónica in relation t Iberdrola's investments in Brazilian operators, Telefónica acquired a 3.38% holding in Tele Leste Celular Participaçoes, S.A. in exchange fo 799,411 shares of Telefónica which had hitherto been held as treasury stock earmarked for that purpose (see Note 11). Subsequently, i May 2002 Telefónica made nonmonetary contributions of this holding to Telefónica Móviles (in exchange for 26,801,494 shares of Telefónica Móviles) in addition to holdings of 7% in TBS Celular Participaçoes, S.A., 7% in Sudestecel Participaçoes, S.A., 3.38% in Tele Lest Celular Participaçoes, S.A. and 62.02% in Iberoleste Participaçoes, S.A Also, Telefónica sold 0.66% of Celular Participaçoes, S.A. for g11.5 million.

Following this transaction, the Telefónica Group's owned the following direct and indirect holdings in these Brazilian companies 40.91% in TBS Celular Participaçoes, S.A., 83.56% in Sudestecel Participaçoes, S.A., 27.71% in Tele Leste Celular Participaçoes, S.A. and al the shares of Iberoleste Participaçoes, S.A. All these companies, an Celular CRT Participaçoes, S.A. were fully consolidated in the Telefónica Group's consolidated financial statements (Tele Leste Celular Participaçoes, S.A. was accounted for by the equity method in the Telefónica Group's 2001 consolidated financial statements) throug December 31, 2002, the date on which their respective balanc sheets were proportionally consolidated through the joint ventur Brasilcel, N.V., as indicated in the section on Telefónica Móviles.

In January Telefónica, S.A. acquired 50,000 shares of Telefónic Móviles, S.A. for g0.41 million. Following this acquisition and th above-mentioned contributions, the Telefónica Group owns direct and indirect holdings of 92.43% in Telefónica Móviles, S.A., which continues to be fully consolidated in the Telefónica Group.

In 2002 Telefónica acquired 717,465 shares of the subsidiary Terra Networks, S.A. for €5.53 million, bringing the Telefónica Group's direct and indirect holding in this company, which continues to be fully consolidated, to 38.58%.

In December Telefónica Capital, S.A., a wholly-owned subsidiary of Telefónica, S.A., sold 28,736 shares of Fonditel, Entidad Gestora de Fondos de Pensiones, S.A. for €6.14 million. Also, Telefónica, S.A's wholly-owned subsidiary Seguros de Vida y Pensiones Antares, S.A., which owned 9,881 shares of Fonditel, sold these shares to Telefónica Capital for €2.11 million. As a result of these transactions, the Telefónica Group's direct and indirect holding in Fonditel was reduced from 81% in 2001 to 70% in 2002. The company continues to be fully consolidated in the Telefónica Group.

In December, by virtue of its commitments to the Tyco Group, Telefónica, S.A. acquired 17,872,341 shares of the Dutch company Emergia Holding, N.V. for €47.09 million. The Telefónica Group thereby became the sole stockholder of this company, which continues to be fully consolidated in the Group.

Telefónica Datacorp Group

In January Telefónica DataCorp acquired all the shares of the German company HighwayOne German for €1.38 million. Subsequently, as part of the reorganization of the Telefónica Group by business line, Telefonica Deutschland GmbH, a subsidiary of Telefónica Datacorp, was made the head of this business in Germany following its merger with HighwayOne Germany, GmbH and Mediaways GmbH. This company is fully consolidated in the Telefónica Group.

On July 16, 2002, the holding in the Austrian company European Telecom International, GmbH, a wholly-owned subsidiary of Telefónica Datacorp, S.A.U., was sold, giving rise to a loss for the Telefónica Group of €38.79 million. This company, which had been fully consolidated in 2001, was excluded from the consolidated group.

The Datacorp Group, through its subsidiary Telefónica Data de Brasil Ltd., subscribed to the capital increase carried out by Telefónica Data Brasil Holding, S.A., contributing the loans previously granted amounting to 482.9 million reais, thereby increasing the Telefónica Group's holding in this company from 87.48% to 93.98%.

The 34%-owned investee of Telefónica Datacorp, S.A., the Italian company Atlanet, S.p.A, which through June 30, 2002, was fully consolidated, has since that date been accounted for by the equity method because it no longer fulfills the management control requirements for full consolidation.

Telefónica Móviles Group

In 2002, after contributing as consideration a total of 7,333,180 shares of Telefónica Móviles and carrying out capital increases amounting to €27.66 million, Telefónica Móviles became the owner of all the shares of TES Holding, S.A. de C.V., Telca Gestión, S.A. de C.V., TCG Holding, S.A., Telca Gestión Guatemala, S.A., Paging de Centroamérica, S.A. and Telefónica de Centroamérica, S.L.

On September 10, 2002, having obtained authorizations from the various Mexican authorities, Telefónica Móviles acquired a 65.23% holding in Pegaso Telecomunicaciones, S.A. de C.V. (Pegaso) for €92,870 million. Subsequently, in order to strengthen its net worth position, Pegaso carried out a capital increase in which Telefónica Móviles, S.A. paid €211,454 thousand corresponding to its 65.23% holding. The agreements entered into with the Pegaso Group contained a commitment to contribute the holdings of the two companies in the Pegaso Group and in the northern Mexican companies to a new Mexican company of which the two groups would be stockholders. This transaction was implemented through the sale of their holdings to Telefónica Móviles Mexico, followed by the conversion of the debt into equity by the creditors, Telefónica Móviles has a holding of 92% in this new Mexican company with a book value of €995.60 million.

On October 21, 2002, Telefónica Móviles, S.A. acquired from Portugal Telecom SGPS, S.A. a 14.68% holding in Telesp Celular Participações, S.A. for €200.31 million.

On December 27, 2002, once Brazilian legislation had been complied with, Telefónica Móviles, S.A. and PT Móveis Serviços de Telecomunicações, SGPS, S.A. (PT Móveis) formed the joint venture Brasilcel, N.V., 50% owned by each company, through the contribution of all the shares directly or indirectly held by the two groups in the wireless communications companies in Brazil, the detail being as follows:

	% Contributed		
Companies Contributed	Telefónica Móviles	PT Móveis	Total
Celular CRT Participações, S.A.	40.90%	7.58%	48.48%
Tele Leste Celular Participações, S.A.	27.70%	–	27.70%
Tele Sudeste Celular Participações, S.A.	83.56%	–	83.56%
Telesp Celular Participações, S.A.	14.68%	50.44%	65.12%

The value of the contribution to Brasilcel, N.V. of the wireless assets owned by Telefónica Móviles, S.A. was €1,898 million. Its balance sheet was proportionally consolidated in the consolidated financial statements and the results for the whole year of the Brazilian companies contributed by Telefónica Móviles were recorded in the consolidated statement of operations when this transfer was made (on December 27, 2002).

Telefónica de Contenidos Group

In September all the shares of the Uniprex Onda Cero Group and of Cadena Voz de Radiodifusión, S.A. owned by Telefónica de Contenidos, S.A. were sold to the Antena 3 de Televisión Group, giving rise to gains of €35.82 million. In 2002 the two companies, which in 2001 were fully consolidated in the Telefónica Group, were included in the Antena 3 de Televisión Group and accounted for by the equity method.

In April Telefónica de Contenidos sold 4.11% of its holding in Hispasat, S.A., giving rise to gains of €26.10 million. Telefónica de Contenidos, which owns a 13.23% holding in Hispasat, S.A., continues to account for this company by the equity method in its consolidated financial statements.

In June 2002 Telefónica de Contenidos sold its holding in Prime Argentina, S.A., which owns the Azul Televisión channel, for US$ 12 million, giving rise to a loss of g162.78 million. This company, which was accounted for by the equity method in the Telefónica Group's consolidated financial statements, has been excluded from consolidation.

T.P.I. Group
On February 11, 2002, Telefónica Publicidad e Información, S.A. acquired all the shares of T.P.I. Perú, S.A.C., from Telefónica Internacional, S.A. for g36.28 million. The Telefónica Group's effective holding in this company, which continues to be fully consolidated, decreased from 97.07% to 59.90%.

Terra Group
In August Terra Networks, S.A., through its wholly-owned U.S. subsidiary Lycos, Inc., sold all its holding (44.82%) in Lycos Korea, Inc., obtaining gains in consolidation of g10.62 million. Also, in September, Lycos Inc. sold its minority holding in the Canadian company Sympatico Lycos Inc., obtaining gains in consolidation of g8.49 million. In December the Terra Group sold all its holding in Lycos Japan, K.K., incurring a loss on the sale of g2.47 million. All these companies, which were accounted for by the equity method in the Telefónica Group's consolidated financial statements, have been excluded from the consolidated group.

(3) Proposed allocation of the loss of the controlling company

The proposed allocation of 2002 loss that the Board of Directors of the Parent Company will submit for approval by the Stockholders' Meeting is that the loss, amounting to g4,478.69 million, be offset with a charge to the following equity accounts:

Millions of Euros	
Revaluation reserves	1,316.67
Voluntary reserves	1,645.80
Additional paid-in capital	1,516.22
Total allocation	**4,478.69**

(4) Valuation standards

The main valuation methods used in preparing the 2002 consolidated financial statements were as follows:

a) Consolidation goodwill

The accompanying consolidated balance sheets include consolidation goodwill, net of amortization, arising from the positive difference in consolidation between the amounts paid to acquire the shares of the subsidiaries consolidated or accouted for by the equity method and their underlying book values plus the unrealized gains allocable to these companies' assets at the acquisition date.

The amortization periods are those for which the estimated income attributable to the Group of the companies at which goodwill exists is at least equal to the unamortized amount of the goodwill relating to these companies. Generally speaking, the amortization period is 20 years (see Exhibit III).

Positive consolidation differences allocable to the assets of the acquired company give rise to an increase in the related assets up to the limit of their market value, once the related appraisal has been performed.

b) Translation methods (year-end exchange rate method)

The financial statements of the Group companies abroad were translated to euros at the exchange rates ruling at year-end, except for:

1. Capital stock and reserves, which were translated at historical exchange rates.

2. Income statement accounts, which were translated at the average exchange rates for the year.

The exchange difference arising from application of this method is included under the "Stockholders' Equity - Translation Differences in Consolidation" caption in the accompanying consolidated balance sheets, net of the portion of said difference relating to minority interests, which is recorded under the "Minority Interests" caption on the liability side of the accompanying consolidated balance sheets.

The companies using accounting methods that include inflation adjustments apply the accounting standards in force in their respective countries, which consist of valuing monetary assets and liabilities at face value and adjusting the historical cost of nonmonetary assets and liabilities by the inflation from the date of inclusion of the asset or liability in the company's balance sheet to year-end. Therefore, the effect of the inflation for the year on the monetary assets and liabilities is included in the statement of income for the year under the "Exchange Losses" or "Exchange Gains" captions. The amounts thus adjusted are translated to U.S. dollars at the year-end exchange rates and the subsequent translation to euros is made by the year-end exchange rate method described in paragraphs 1 and 2 above.

The accompanying consolidated financial statements do not include an adjustment for inflation at the Argentine subsidiaries, although under Argentine accounting regulations these companies are required to record such an adjustment. The uniformity adjustment made is due to the fact that as of December 31, 2002, the indicators established by international accounting regulations in order to determine whether a country can be considered to be highly inflationary for the purposes of recording the adjustment for inflation were not being met. Salaries, prices and interest rates, in particular, were not tied to the CPI, and the cumulative three-year CPI increase is not close to 100%, due largely to the measures to control it taken by the government.

c) Start-up expenses

Start-up expenses, which comprise mainly incorporation, capital increase and preopening expenses and expenses relating to initial public offerings, are recorded at cost and are amortized on a straight-line basis over five years. In 2002, as indicated in Note 1 on the Internet businesses, in accordance with the accounting principle of prudence in valuation, g56.62 million were written off with a charge to extraordinary expenses (see Note 20)

d) Intangible assets

This caption in the accompanying consolidated balance sheets relates mainly to the following items:

Research and development expenses
These relate to the costs incurred in developing new products to be marketed or used for the Group's own network, which are generally amortized by the straight-line method over three years from the date of completion. Costs incurred in projects which are not viable for the future are charged to the consolidated satement of operations for the year in which this circumstance becomes known.

Rights on leased assets
The rights under financial lease contracts are recorded at the cost of the related assets, and the total debt for lease payments plus the amount of the purchase option are recorded as a liability. The difference between the two amounts, which represents the interest expenses on the transaction, is recorded as a deferred expense and is allocated to income each year by the interest method. The rights under the existing contracts, which relate mainly to computer hardware, are generally amortized on a straight-line basis over five years, which coincides with the years of useful life of the hardware.

Software licenses and developments
These items are recorded at cost and are amortized on a straight-line basis over three years.

Administrative concessions
This caption relates to the acquisition cost of the licenses for the provision of telephony services granted to the Group by various public authorities, and to the value assigned to the licenses held by certain companies at the time they were acquired by the Telefónica Group.

Amortization starts to be taken when commercial operation of these licenses commences and continues to be taken over the term thereof based on the estimated capacity to generate revenues in each period, which normally coincides with the number of lines installed or the average revenues per customer, depending on the type of services provided under the license.

The acquisition cost includes the expenses incurred directly for obtainment of these licenses and, in the case of the licenses to operate the Universal Mobile Telecommunications System (UMTS) obtained in Spain, Germany, Italy, Austria and Switzerland, the financial expenses incurred from the granting of the license through June 30, 2002, since from that date, due to the circumstances discussed in Note 1, the Group decided not to capitalize any further expenses in this connection.

As indicated in Notes 1 and 6, the Telefónica Group has taken certain decisions regarding its future strategy in the UMTS business, as a result of which it has significantly reduced the value of these licenses based on expectations of how this business activity will evolve in the future.

Other intangible assets
This caption includes, among other items, the costs incurred in acquiring capacity and rights to use other operators' cables, mainly underwater cables. These rights are amortized over the duration of the rights acquired.

e) Property, plant and equipment

Property, plant and equipment is carried at cost revalued pursuant to the applicable enabling legislation (see Note 7). If the regulations applicable in a particular country so require, the property, plant and equipment is valued at cost adjusted for inflation (see Note 4-b).

Cost includes external costs plus internal costs comprising warehouse materials used, direct labor used in installation work and the allocable portion of the indirect costs required for the related investment. The latter two items are recorded as a revenue under the "Capitalized Expenses of Group Work on Fixed Assets" caption.

The interest and other financial expenses incurred during the construction of property, plant and equipment in connection with the start-up of a new activity, when the construction period exceeds one year, and the exchange differences arising over this period on long-term loans to finance these assets, are generally not capitalized. No expenses were capitalized in this connection in 2002. €18.27 million were capitalized in this connection in 2001, mainly in relation to the construction of the underwater cable in Latin America, a project that was completed in 2001.

The costs of expansion, modernization or improvements leading to increased productivity, capacity or efficiency or to a lengthening of the useful lives of the assets are capitalized.

Upkeep and maintenance expenses are expensed currently.

The Group records the necessary value adjustments to reduce the cost of each item of property, plant and equipment to its market value at each year-end, provided that the book value of the asset is not recoverable through the generation of sufficient revenues to cover all the costs and expenses, including depreciation.

An allowance must be recorded for lasting decline in value that is deemed to be reversible. This allowance will be deducted in the valuation of the asset in question; in this case the lower value will not be maintained if the causes which prompted the value adjustment have ceased to exist.

When the decline in value of the assets is irreversible and differs from the result of systematic depreciation, the loss and the decline in value of the related asset will be directly recorded.

The companies depreciate their property, plant and equipment by the straight-line method at annual rates based on the years of estimated useful life of the assets, calculated in accordance with technical studies which are reviewed periodically based on technological advances and the rate of dismantling, as follows:

	Years of Estimated Useful Life
Buildings and structures	25-50
Plant and machinery	10-15
Telephone installations, networks and subscriber equipment	5-25
Furniture, office equipment and other	2-10

The increases in value resulting from revaluations are depreciated over the years of residual useful life of the revalued assets.

f) Long- and short-term investments

Shareholdings which were not consolidated are recorded in the consolidated balance sheet at the lower of cost or market.

The market value was determined as follows:

1. Listed securities:
   The market value was taken to be the lower of average market price in the last quarter or market price at year-end.

2. Unlisted securities and holdings in companies accounted for by the equity method:
   The market value was taken to be the underlying book value at year-end plus the unrealized gains disclosed at the time of the acquisition and still existing at year-end.

Unrealized losses (cost higher than market value at year-end) are recorded under the “Allowances” caption.

g) Deferred charges

This caption in the accompanying consolidated balance sheets includes mainly the following items:

Supplementary pension payments to retired employees (shortfall)
These relate to the shortfall in the provisions recorded for the commitments assumed by Telefónica de España to retired employees as of June 30, 1992. Since then, the shortfall has been allocated to income over 15 years by the straight-line method, in accordance with the communication received from the Spanish Accounting and Audit Institute (ICAC) dated March 1, 1993, at a rate of g61.59 million per year. On November 1, 1997, coverage of these commitments was externalized, and on November 1, 2002, they were adapted pursuant to Private Insurance Law 30/1995 and Royal Decree 1588/1999 approving the regulations on the instrumentation of employers' pension commitments to employees and beneficiaries (see Notes 9 and 14).

Debt arrangement expenses
These relate to long-term debt arrangement expenses and issuance premiums on debentures and bonds and preferred shares and are amortized by the interest method on the basis of the principal amounts outstanding.

Executive loyalty-building program
This caption relates to the unaccrued costs relating to the Telefónica Group's Top and EN-SOP stock option plans (see Notes 9 and 20).

Interest on long-term promissory notes
This relates to the difference between the face value and the effective value of the promissory notes issued at over one year. This interest is charged to income by the interest method.

Interest on financial lease contracts
This relates to the interest expenses on financial lease contracts, which are charged to income by the interest method (see Note 4-d).

Externalization of pension commitments
As a result of Telefónica de España's externalization of its pension commitments pursuant to Private Insurance Law 30/1995, Law 50/1998 on Tax, Administrative, Labor and Social Security measures, Royal Decree 1588/1999 enacting the regulations on the instrumentation of employers' pension commitments to employees and beneficiaries, and Additional Provision Twenty-Five of Law 14/2000 on Tax, Administrative, Labor and Social Security measures for 2001, the differences arising due to the change in the actuarial assumptions needed to externalize the aforementioned commitments were recorded under the “Deferred Charges” caption (see Note 9).

h) Inventories

Warehouse materials for installation in investment projects and consumables and replacement parts are valued at the lower of weighted average cost, adjusted by the effect of inflation in the countries whose local legislation so requires (see Note 4-b), or market.

Obsolete, defective or slow-moving inventories have been reduced to realizable value. The allowance for decline in value of inventories is recorded on the basis of inventory age and turnover.

i) Treasury stock

Treasury stock is valued at the lower of cost, comprising the total amount paid for acquisition, or market. Since these shares were acquired without any prior resolution having been adopted by the Stockholders' Meeting to reduce capital, they are assumed to be intended for subsequent sale or, alternatively, for a possible capital reduction, and, accordingly, market value is taken to be the lowest of average official market price in the last quarter of the year, year-end market price, or the related underlying book value. A provision was recorded with a charge to the consolidated statement of operations for the difference between the acquisition cost and the lower of the year-end market price or the average market price in the last quarter, and with a charge to reserves for the difference between the aforementioned market value and the related underlying book value.

j) Capital subsidies

Capital subsidies are valued at the amount granted and are allocated to income on a straight-line basis over a maximum period of ten years, which does not differ materially from the estimated useful life of the subsidized assets.

Most of the aforementioned subsidies were granted to Telefónica de España and the conditions under which the subsidies were granted are being met (see Note 13).

k) Foreign currency transactions

Fixed-income securities and receivables and payables denominated in foreign currencies are translated to euros at the exchange rates ruling at the transaction date, and are adjusted at year-end to the exchange rates then prevailing.

Exchange differences arising on adjustment of foreign currency fixed-income securities and receivables and payables to year-end exchange rates are classified by currency and due date, and for this purpose currencies which, although different, are officially convertible are grouped together.

The positive net differences in each group of currencies are recorded under the "Deferred Revenues" caption on the liability side of the consolidated balance sheet, unless exchange losses in a given group have been charged to income in prior years, in which case the net positive differences are credited to period income up to the limit of the negative net differences charged to income in prior years.

The positive differences deferred in prior years are credited to income in the year in which the related accounts receivable and payable fall due or are repaid early, or as negative exchange differences for the same or a higher amount are recognized in each homogeneous group.

Exchange gains or losses arising from specific-purpose financing of foreign currency investments in investee companies to hedge the exchange risk to which these investments are exposed are recorded under the "Translation Differences in Consolidation" caption in the consolidated balance sheet.

These transactions are deemed to be hedging transactions when they meet certain requirements, most notably that the foreign currency in which the financing is denominated is the same as, or largely matches, the functional currency of the investment and of the flows generated by it, and that the timing of recognition of the anticipated revenues from dividends and management fees matches the loan repayment schedule.

l) Pension and other commitments to employees

At year-end the Group records in the consolidated balance sheet the provisions required to cover the accrued liability for the existing commitments that have not been externalized, based on actuarial calculations using an appropriate discount rate. The liabilities recorded under "Preretirements, Social Security Expenses and Voluntary Severances" were calculated individually and discounted to present value at a rate of 4%.

The Group's main commitments in this connection are detailed in Note 14.

m) Technical reserves

This caption relates mainly to the net level premium reserves, which represent the amount by which the present value of life insurance, pension and reinsurance commitments exceed the net premiums to be paid by the policyholders to the subsidiaries Seguros de Vida y Pensiones Antares, S.A. and Casiopea Reaseguradora, S.A. These reserves are credited when the commitments covered are paid.

n) Accounts payable

Accounts payable are recorded at repayment value, except for zero-coupon debenture and bond issues, which are recorded in the consolidated balance sheet at issue value plus the related accrued interest (see Note 15).

o) Derivatives

Transactions whose purpose and effect is to eliminate or significantly reduce exchange, interest rate or market risks on asset and liability positions or on other transactions are treated as hedging transactions. The gains or losses arising during the life of these derivatives are accrued and taken to the income statement symmetrically to the gains or losses on the hedged asset (see Note 17).

Transactions which, exceptionally, were not assigned to hedge risks, are not treated as hedging transactions. In transactions of this kind, the differences in market price are recorded for accounting purposes when the transactions are canceled or finally settled. However, if potential losses are anticipated at year-end, the related provision is recorded with a charge to the consolidated statement of operations. Similarly, transactions aimed at reducing the exchange risk relating to the income contributed by Latin American subsidiaries are not treated as hedging transactions.

p) Corporate income tax and other taxes

These captions in the consolidated statements of operations include all the debits and credits arising from Spanish corporate income tax and similar taxes applicable to the Group companies abroad.

The expense for corporate income tax of each year is calculated on the basis of book income before taxes, increased or decreased, as appropriate, by the permanent differences from taxable income, defined as those arising between taxable income and book income before taxes that are not reversed in subsequent periods.

Tax relief and tax credits, excluding tax withholdings and prepayments, are deducted from the corporate income tax charge in the year in which they are definitively taken, except in the case of investment tax credits earned since 1996, which, at the time when they are taken, are deferred over the average life of the assets which gave rise to them.

Also, pursuant to an ICAC resolution dated March 15, 2002, the Telefónica Group recorded the tax assets relating to the tax relief and tax credits not yet taken for tax purposes regarding which there is no doubt, in accordance with the accounting principle of prudence in valuation, that they can be deducted in the future (see Note 18).

The difference between the accrued tax expense and the tax paid is due to the above-mentioned deferral, to capitalized tax credits not yet taken and to revenue and expense recognition timing differences giving rise to deferred tax assets and liabilities, provided that they have a certain reversal period (see Note 18).

q) Recognition of revenues and expenses

Revenues and expenses are recognized on an accrual basis, i.e. when the actual flow of the related goods and services occurs, regardless of when the resulting monetary or financial flow arises.

The revenues from telephony and other services are recognized on an accrual basis. Unbilled revenues from the beginning of the billing cycle to the end of each month are estimated or recorded as soon as they are known. The differences between the estimated revenues and those subsequently billed are not material and are recognized in the following period. In accordance with the accounting principle of prudence, only realized income is recorded at year-end, whereas foreseeable contingencies and losses, including possible losses, are recorded as soon as they become known (see Notes 10 and 20).

(5) Consolidation goodwill

The variations in the “Consolidation Goodwill” caption and in the related accumulated amortization in 2002 and 2001 were as follows:

Millions of Euros

Balance at 12/31/00	**7,714.80**
Additions	3,018.72
Amortization	(845.19)
Write-offs	(249.00)
Net retirements	(461.93)
Net transfers	161.89
Translation differences	(210.35)
Balance at 12/31/01	**9,128.94**
Additions	1,121.54
Amortization	(667.49)
Write-offs	(2,259.81)
Net retirements	(277.64)
Net transfers	(236.94)
Translation differences	(444.58)
Balance at 12/31/02	**6,364.02**

The goodwill arising on the acquisition of companies abroad is translated to euros at the exchange rates prevailing at the time the goodwill arises, except for goodwill arising on the acquisition of companies by foreign companies, which is recorded in local currency and is affected by exchange rate fluctuations. The resulting differences are recorded under the “Translation Differences in Consolidation” caption.

Per the estimates and projections available to the directors, the projected income attributable to the Group that will be earned by the companies at which goodwill had arisen at year-end is at least equal to the unamortized balance of the related goodwill in the related periods.

The detail of the balances of the goodwill and the related accumulated amortization at each company, and of the variations therein is shown in Exhibit III.

Based on these estimates and projections, in 2001 g249 million of goodwill relating to the investment in Mediaways, GmbH was written off, and this amount is recorded under the “Extraordinary Expenses and Losses” caption in the accompanying consolidated statement of operations (see Note 20).

In 2002 the existing estimates and projections were once again reviewed, and g2,259.81 million of goodwill was written off in accordance with the accounting principle of prudence in valuation, based on the analyses made both in-house and by third parties of the projected cash flows for the coming years (see Note 20). The goodwill written off included most notably g856.66 million relating to the investment in the Terra Lycos Group (see Note 1), g530.00 million relating to the investment in Mediaways, GmbH, g154.47 million relating to the investment in I.O. Box, g173.38 million relating to the investment in Pearson Plc., g59.14 million relating to the investment in Atlanet, S.p.A. (see Note 1) and g49.65 million relating to the investment in Emergia, N.V.

The goodwill written off by the Terra Lycos Group also included the retirement of g256.67 million under the agreement entered into on May 16, 2000, by Lycos Inc., Terra Networks, S.A., Telefónica, S.A. and Bertelsmann, AG, which was subsequently amended by a new contract whereby Telefónica, S.A. replaces Bertelsman AG. In 2001 g40[illegible] million of goodwill arising in the acquisition of Lycos, Inc. were allocated to this contract, which, as mentioned, was modified. Accordingly, the signing of the new contract is the logical result, on the one hand, of the changes which have taken place in the Internet businesses, particularly as a result of the development of broadband and, on the other, of the need to adapt the range of products and services envisaged to the specific needs of the Telefónica Group in the markets in which it is present. This certain creation of value for the Terra Lycos Group, as reflected in a study carried out by a third party, was written off in the accompanying consolidated financial statements since it was generated in the context of the Telefónica Group.

2002

The main additions to consolidation goodwill in 2002, related to the following companies:

Millions of Euros

Telefónica Móviles México Group	598.44
Brasilcel, N.V. Group	268.69
Endemol Group	89.98
Telefónica Centroamérica Guatemala	41.40
Emergia, N.V.	49.65
Other companies	73.38
Total	**1,121.54**

2001

The main additions to consolidation goodwill in 2001, related to the following companies:

Millions of Euros

Mediaways, GmbH	1,474.66
Endemol Group	268.61
Data Brasil Group	233.55
Grupo Corporativo del Norte, S.A.	230.51
Celular de Telefonía, S.A. de C.V.	137.86
Investees of G. Corporativo del Norte, S.A. and other companies acquired	135.14
Uno-e Bank, S.A.	130.25
Telefónica Móviles, S.A.	113.21
Portugal Telecom, S.A.	76.00
Other companies	218.93
Total	**3,018.72**

In 2002 there were no significant retirements of goodwill due to sales of holdings. However, due to changes in the consolidation method (see Note 2-c) there was a 50% reduction (g243.65 million) in the goodwill relating to the wireless operators in Brazil following the joint venture agreement with Portugal Telecom, S.G.P.S., S.A. leading to the formation of Brasilcel, which was proportionally consolidated at 2002 year-end.

Notable in 2001 was the retirement amounting to g265.38 million due to the sale of the investment in Cablevisión, S.A.

(6) Intangible assets

The detail of the balances of the intangible asset accounts and of the variations therein in 2002 and 2001 is as follows:

Millions of Euros

	Balance at 12/31/01	Additions	Retirements	Inclusion of Companies	Exclusion of Companies	Translation Differences	Transfers	Balance at 12/31/02
Cost:								
Research and development expenses	1,049.59	94.42	(0.08)	–	–	(0.64)	35.86	1,179.15
Administrative concessions	15,011.19	177.72	(9,423.12)	1,053.78	(443.57)	(246.47)	220.67	6,350.20
Rights on leased assets	137.69	10.40	(3.76)	–	–	(20.96)	(38.97)	84.40
Software licenses and developments	2,309.13	423.40	(61.84)	127.24	(49.20)	(175.38)	557.84	3,131.19
Other intangible assets	1,778.44	400.64	(119.32)	9.02	(1.49)	(145.40)	(731.25)	1,190.64
Total intangible assets, gross	**20,286.04**	**1,106.58**	**(9,608.12)**	**1,190.04**	**(494.26)**	**(588.85)**	**44.15**	**11,935.58**
Accumulated amortization:								
Research and development expenses	862.72	146.01	(0.08)	–	–	(0.64)	(2.06)	1,005.95
Administrative concessions	745.22	240.03	(3.49)	97.85	(31.20)	(30.56)	(23.88)	993.97
Rights on leased assets	61.00	20.88	(4.92)	–	–	(5.27)	(41.77)	29.92
Software licenses and developments	1,133.94	603.45	(47.06)	53.43	(16.00)	(65.94)	105.32	1,767.14
Other intangible assets	504.37	123.71	(44.24)	0.43	(0.14)	(61.76)	(53.67)	468.70
Total accumulated amortization	**3,307.25**	**1,134.08**	**(99.79)**	**151.71**	**(47.34)**	**(164.17)**	**(16.06)**	**4,265.68**
Allowances for decline in value	**19.65**	**27.56**	**(4.78)**	**2.68**	**–**	**(6.60)**	**1.82**	**40.33**
Intangible assets, net	**16,959.14**	**(55.06)**	**(9,503.55)**	**1,035.65**	**(446.92)**	**(418.08)**	**58.39**	**7,629.57**

Millions of Euros

	Balance at 12/31/00	Additions	Retirements	Inclusion of Companies	Exclusion of Companies	Translation Differences	Transfers	Balance at 12/31/01
Cost:								
Research and development expenses	1,108.16	170.79	(6.62)	–	–	3.64	(226.38)	1,049.59
Administrative concessions	17,855.95	472.82	(35.22)	80.14	(33.84)	(157.03)	(3,171.63)	15,011.19
Rights on leased assets	150.81	27.76	(10.28)	–	–	(4.09)	(26.51)	137.69
Software licenses and developments	1,666.79	606.44	(16.09)	21.07	(8.38)	(0.96)	40.26	2,309.13
Other intangible assets	1,238.45	372.28	(89.56)	50.71	(8.01)	(44.61)	259.18	1,778.44
Total intangible assets, gross	**22,020.16**	**1,650.09**	**(157.77)**	**151.92**	**(50.23)**	**(203.05)**	**(3,125.08)**	**20,286.04**
Accumulated amortization:								
Research and development expenses	717.72	174.63	(4.70)	–	–	1.40	(26.33)	862.72
Administrative concessions	507.44	247.67	(5.73)	21.26	(18.84)	(5.49)	(1.09)	745.22
Rights on leased assets	56.27	15.88	(2.93)	–	–	(1.61)	(6.61)	61.00
Software licenses and developments	740.93	402.90	(4.31)	4.55	(3.02)	1.02	(8.13)	1,133.94
Other intangible assets	302.90	188.40	(41.53)	41.59	(13.31)	(17.23)	43.55	504.37
Total accumulated amortization	**2,325.26**	**1,029.48**	**(59.20)**	**67.40**	**(35.17)**	**(21.91)**	**1.39**	**3,307.25**
Allowances for decline in value	**1.80**	**25.29**	**(0.31)**	**–**	**–**	**(7.13)**	**–**	**19.65**
Intangible assets, net	**19,693.10**	**595.32**	**(98.26)**	**84.52**	**(15.06)**	**(174.01)**	**(3,126.47)**	**16,959.14**

The inclusions and exclusions of companies in 2002 include the effect of proportionally consolidating the joint venture Brasilcel, N.V. (see Note 2-c), which affected the net inclusions and exclusions by g754.48 million and g446.90 million, respectively. Also, the inclusion of Pegaso gave rise to net inclusions of g274.13 million.

The "Administrative Concessions" caption includes mainly the following items :

– Licenses for the provision of UMTS services in Spain, Germany and Austria acquired in 2000 and the addition in 2001 of the license granted in Switzerland. As indicated in Note 1, the "Retirements" column for 2002 includes g9,445.01 relating to the effect of the value adjustments required in intangible asset captions, including the financial costs capitalized to date. The amount capitalized in 2002 includes g96.64 million relating to the financing obtained by Telefónica and Telefónica Móviles and g68.05 million relating to the financing granted by other stockholders of the companies that hold UMTS licenses (g271.39 million and g236.39 million, respectively, in 2001). The "Transfers" column for 2001 includes the effect of accounting for Ipse 2000, which holds the UMTS license in Italy, by the equity method (see Note 2-c).

– A 25-year concession granted by the Peruvian State to Telefónic del Perú, S.A.A. when this company was acquired in April 1994 b Telefónica Internacional.

– Licenses to operate wireline and wireless communications servic es of the companies awarded in the privatization in July 1998 o the Telebras system (Telesp, Tele Sudeste and Tele Leste) and th inclusion of Telesp Celular in 2002. A portion of the price paid fo these companies was assigned as an addition to the value o these assets when they were acquired. The term of these license is 27 years.

– 25-year DCS 1800 MHz licenses recorded at the amount paid t the Spanish Government plus the amount set aside to defray th costs relating to the radio spectrum cleaning process required fo the implementation and development of these licenses.

– Licenses for the provision of the Personal Communications Ser vice in Argentina, which are being amortized over 20 years.

The projections that the directors have regarding business perform ance and the income to be generated by these concessions are a least equal to the unamortized balance thereof.

(7) Property, plant and equipment

The detail of the balances of property, plant and equipment accounts, of the related accumulated depreciation and of the variations therein and variations therein in 2002 and 2001 are as follows:

Millions of Euros

	Balance at 12/31/01	Additions	Retirements	Inclusion of Companies	Exclusion of Companies	Translation Differences	Transfers	Balance at 12/31/02
Cost:								
Land and structures	7,097.90	33.19	(82.23)	43.13	(19.11)	(1,073.88)	160.15	6,159.15
Plant and machinery	3,365.73	51.51	(76.38)	49.84	(25.28)	(644.61)	1,019.00	3,739.81
Telephone installations	62,975.46	298.60	(1,015.08)	1,371.18	(512.54)	(11,355.68)	1,996.96	53,758.90
Furniture, tools, etc.	3,851.74	162.99	(304.73)	146.12	(48.63)	(700.23)	24.80	3.132.06
Total property, plant and equipment in service	**77,290.83**	**546.29**	**(1,478.42)**	**1,610.27**	**(605.56)**	**(13,774.40)**	**3,200.91**	**66,789.92**
Construction in progress	3,034.89	2,159.47	(57.83)	43.52	(39.42)	(777.66)	(3,376.82)	986.15
Advances on property, plant and equipment	53.20	22.30	(2.78)	2.96	(0.17)	(7.70)	(1.66)	66.15
Installation materials	154.12	91.59	(16.42)	–	–	(47.52)	(19.14)	162.63
Property, plant and equipment, gross	**80,533.04**	**2,819.65**	**(1,555.45)**	**1,656.75**	**(645.15)**	**(14,607.28)**	**(196.71)**	**68,004.85**
Accumulated depreciation:								
Structures	2,332.44	214.76	(28.94)	8.32	(2.34)	(296.93)	(107.18)	2,120.13
Plant and machinery	1,196.20	524.78	(87.54)	10.98	(12.51)	(240.74)	149.70	1,540.87
Telephone installations	37,976.28	4,176.61	(921.32)	447.30	(267.26)	(6,469.24)	275.15	35,217.52
Furniture, tools, etc.	2,327.03	453.67	(251.41)	58.88	(22.20)	(393.01)	(231.65)	1.941.31
Total accumulated depreciation	**43,831.95**	**5,369.82**	**(1,289.21)**	**525.48**	**(304.31)**	**(7,399.92)**	**86.02**	**40,819.83**
Allowances for decline in value	**95.00**	**51.94**	**(52.60)**	**0.53**	**–**	**(8.63)**	**(0.87)**	**85.37**
Property, plant and equipment, net	**36,606.09**	**(2,602.11)**	**(213.64)**	**1,130.74**	**(340.84)**	**(7,198.73)**	**(281.86)**	**27,099.65**

Millions of Euros

	Balance at 12/31/00	Additions	Retirements	Inclusion of Companies	Exclusion of Companies	Translation Differences	Transfers	Balance at 12/31/01
Cost:								
Land and structures	7,203.17	117.58	(11.65)	38.40	(1.48)	(475.87)	227.75	7,097.90
Plant and machinery	1,729.40	301.54	(44.08)	93.75	(19.53)	(43.11)	1,347.76	3,365.73
Telephone installations	62,140.40	1,931.93	(1,250.94)	677.09	(41.95)	(4,599.51)	4,118.44	62,975.46
Furniture, tools, etc.	3,498.37	580.25	(214.90)	145.52	(40.22)	(276.58)	159.30	3,851.74
Total property, plant and equipment in service	**74,571.34**	**2,931.30**	**(1,521.57)**	**954.76**	**(103.18)**	**(5,395.07)**	**5,853.25**	**77,290.83**
Construction in progress	5,669.76	3,551.30	(186.61)	67.35	(53.03)	(213.14)	(5,800.74)	3,034.89
Advances on property, plant and equipment	53.02	9.90	(9.96)	20.23	(20.68)	(13.27)	13.96	53.20
Installation materials	351.24	278.30	(42.17)	0.32	(6.53)	(159.41)	(267.63)	154.12
Property, plant and equipment, gross	**80,645.36**	**6,770.80**	**(1,760.31)**	**1,042.66**	**(183.42)**	**(5,780.89)**	**(201.16)**	**80,533.04**
Accumulated depreciation:								
Structures	2,147.42	236.59	(5.13)	15.45	65.78	(145.60)	17.93	2,332.44
Plant and machinery	1,012.04	231.96	(24.08)	40.87	(22.45)	(56.32)	14.18	1,196.20
Telephone installations	35,974.46	5,210.54	(1,100.10)	201.15	30.88	(2,488.49)	147.84	37,976.28
Furniture, tools, etc.	2,074.89	548.01	(103.11)	88.43	(50.13)	(196.97)	(34.09)	2,327.03
Total accumulated depreciation	**41,208.81**	**6,227.10**	**(1,232.42)**	**345.90**	**24.08**	**(2,887.38)**	**145.86**	**43,831.95**
Allowances for decline in value	**714.62**	**24.95**	**(669.25)**	**–**	**(0.91)**	**(9.26)**	**34.85**	**95.00**
Property, plant and equipment, net	**38,721.93**	**518.75**	**141.36**	**696.76**	**(206.59)**	**(2,884.25)**	**(381.87)**	**36,606.09**

The inclusions and exclusions of companies in 2002 include the effect of proportionally consolidating the joint venture Brasilcel, N.V. (see Note 2-c), which affected the net inclusions and exclusions by g492.80 million and g340.75 million, respectively. Also, the inclusion of Pegaso gave rise to net inclusions of g625.50 million.

The retirements from "Telephone Installations" relate mainly to the dismantling of telephony plant (see Note 20) with a gross cost of g1,010.54 million in 2002.

Noteworthy in both 2002 and 2001 were the investments made by Group companies, mainly in wireline telephony both in Spain and Latin America and in wireless telephony, which represent most of the additions to and related subsequent transfers from the "Construction in Progress" caption.

The "Translation Differences" column includes both the effect of the variation in exchange rates on the beginning balances and the monetary adjustment applied by certain companies to their balances to adjust for inflation, in accordance with the accounting practices in their respective countries. The effect of exchange rates on the period variations is included in the appropriate column for each variation. As indicated in Notes 1 and 4-b, the effect of the devaluation of the Argentine peso and the performance of the Brazilian real in both years should be noted.

As of December 31, 2002, the following items had been fully depreciated:

Millions of Euros

Buildings and structures	162.65
Plant, machinery and tools	728.09
Telephone installations	15,198.67
Other property, plant and equipment	996.47
Total	**17,085.88**

Telefónica de España's fixed assets used to provide services currently regulated by a concession cannot be mortgaged without prior administrative authorization.

The Telefónica Group companies have taken out insurance policies to reasonably cover the possible risks to which their property, plant and equipment used in operations are subject. These policies include certain franchises for local and domestic long-distance networks and subscriber equipment.

On December 31, 1996, Telefónica de España revalued its property, plant and equipment pursuant to Royal Decree-Law 7/1996. The Company had previously revalued its assets pursuant to the enabling legislation specifically applicable to Telefónica de España. The net increase in value resulting from these revaluations is being depreciated over the tax periods in the remaining useful lives of the revalued assets. The effect of this depreciation on the accompanying consolidated statement of operations is not material.

The detail, as of December 31, 2002, of the property, plant and equipment owned by consolidated Group companies located abroad is as follows:

Millions of Euros

Cost	27,179.93
Accumulated depreciation	(13,424.89
Total	**13,755.04**

Allowances for decline in value

The telecommunications market in Spain became fully deregulated on December 1, 1998. In 1999 certain regulatory measures were adopted, the main consequence of which was to accelerate the opening up to competition of the basic telephony service in Spain. These measures include most notably the approval of reductions in the regulated rates for local, long-distance and wireline-to-wireless services, although, per Group management estimates, the envisaged increase in monthly charges will not enable the effects of the current rate imbalance to be eliminated at medium term. Also approved on the same date were significant reductions in regulated circuit lease prices, to which must be added the entry into force in 2000 of obligatory operator pre-selection and number portability. In July 1999 the general application of the prices and conditions of the Reference Interconnection Offer (RIO), of particular relevance to wireless operators, came into force. Lastly, measures were taken to bring forward the introduction of competition in the local loop through application of ADSL technology and the immediate award of radio spectrum licenses for use in the local loop (LMDS technology).

The Group has analyzed the impact at Telefónica de España of these measures on the recoverability of the value of certain assets, the investment in which was made in the past taking into account the prevailing regulatory framework, and above all, in fulfillment of the obligations for the provision of the universal service provided for in the State Contract entered into in 1991. As a result, in 1999 the Company recorded a provision of g1,322.56 million with a charge to extraordinary expenses.

In subsequent years the related allowance was revalued and reversed as the estimated losses were allocated to the consolidated statement of operations, after including in the consolidated financial statements the losses arising as a result of the difference between the revenues, expenses and depreciation relating to these assets. Accordingly, g36.83 million and g668.41 million were reversed in 2002 and 2001, respectively, and these amounts were recorded under the "Variations in Fixed Asset and Control Portfolio Allowances". As of December 31, 2002, the allowance amounted to g3.44 million.

(8) Long-term investments

The detail of the balances of the long-term investments and of the related investment valuation allowances as of December 31, 2002 and 2001, and of the variations therein in the years then ended, is as follows:

Millions of Euros

	Investments in Associated Companies	Other Investments	Other Loans	Guarantees and Deposits Given	Taxes Receivable (Note 18)	Allowances	Total
Balance at 12/31/00	**2,301.63**	**1,382.91**	**1,594.09**	**35.84**	**2,666.11**	**(84.07)**	**7,896.51**
Additions	353.70	30.43	656.70	273.24	1,582.81	(68.85)	2,828.03
Sale of companies	(365.65)	(10.54)	(145.87)	(19.60)	(423.83)	2.07	(963.42)
Inclusion of companies	8.63	–	34.11	0.10	9.23	–	52.07
Exclusion of companies	(2.43)	(50.14)	(25.60)	(0.02)	(39.79)	0.52	(117.46)
Translation differences	(6.70)	(3.40)	(104.80)	0.85	(98.43)	9.96	(202.52)
Losses	(376.50)	–	–	–	–	–	(376.50)
Dividends	(48.27)	–	–	–	–	–	(48.27)
Transfers	1,234.73	(478.48)	29.49	(57.43)	61.68	(178.36)	611.63
Balance at 12/31/01	**3,099.14**	**870.78**	**2,038.12**	**232.98**	**3,757.78**	**(318.73)**	**9,680.07**
Additions	169.84	2.36	687.81	136.77	6,919.83	(75.29)	7,841.32
Sale of companies	(10.38)	(18.09)	(292.45)	(227.24)	(978.06)	17.63	(1,508.59)
Inclusion of companies	0.40	–	236.18	2.29	17.21	–	256.08
Exclusion of companies	(4.72)	–	(48.11)	(1.45)	(34.90)	0.45	(88.73)
Translation differences	(295.91)	(30.32)	27.75	(10.34)	(265.65)	13.12	(561.35)
Losses	(527.88)	–	–	–	–	–	(527.88)
Dividends	(58.16)	–	–	–	–	–	(58.16)
Transfers	(291.14)	107.30	(424.04)	27.76	263.21	67.28	(249.63)
Balance at 12/31/02	**2,081.19**	**932.03**	**2,225.26**	**160.77**	**9,679.42**	**(295.54)**	**14,783.13**

The additions to and retirements from the "Investments in Associated Companies" and "Other Investments" accounts reflect the amount of the investments detailed in the variations in the consolidated Group as of December 31, 2002 and 2001, described in Exhibit II. The transfers of associated companies in 2001 relate mainly to Ipse 2000, which holds the Italian UMTS license (see Note 2-c).

The "Other Loans" caption includes the investment of the net level premium reserves of the Group's insurance companies, mainly in government debentures, government debt securities and long-term deposits amounting to g823.44 million and g743.55 million as of December 31, 2002 and 2001, respectively, which earn average returns of between 4.52% and 5.30% (2.98% in the case of money market assets). The "Short-Term Investments - Short-Term Investment Securities" caption in the consolidated balance sheet as of December 31, 2002, includes g405.90 million (g117.71 million in 2001) recorded to cover commitments, which are accounted for as "Technical Reserves" (see Note 14).

As of December 31, 2002, the Telefónica Group had granted long-term loans totaling g811.76 million to the associated company DTS Distribuidora de Televisión Digital, S.A. (Vía Digital), and this amount is recorded under the "Other Loans" caption. Also, the short-term "Accounts Receivable - Receivable from Associated Companies" caption included balances receivable totaling g45.50 million relating to loans and trade accounts receivable.

The "Taxes Receivable" caption includes the long-term deferred tax assets, which are grouped together under the "Long-Term Investments" caption on the asset side of the consolidated balance sheet in accordance with an ICAC Resolution on Valuation Standard 16 of the Spanish National Chart of Accounts, and the tax credits taken in the year (see Note 18).

In 2002 the Telefónica Group sold the following investments in various companies with the results detailed below:

	Percentage of Capital Stock Sold	Millions of Euros Gain (Loss)
Subsidiaries and associated companies:		
European Telecom International, GmbH	100%	(38.79)
Uniprex Onda Cero Group	100%	35.82
Hispasat, S.A.	4.11%	26.10
Azul Televisión	100%	(162.78)
Sonda Group	25%	(1.62)
Lycos Korea	44.82%	10.62
Sympatico Lycos	27%	8.49
Other		15.04
Net loss		**(107.12)**

The Group and associated companies listed on stock markets are as follows:

- Telefónica, S.A.
- Telefónica Móviles, S.A.
- Telefónica Publicidad e Información, S.A.
- Terra Networks, S.A.
- Lycos Europe, N.V.
- Amper, S.A.
- Compañía de Telecomunicaciones de Chile, S.A.
- Telefónica de Argentina, S.A.
- Telefónica del Perú, S.A.A.
- Compañía Anónima Nacional de Teléfonos de Venezuela, C.A. (CANTV)
- Portugal Telecom, S.A.
- Telecomunicaçoes de Sao Paulo, S.A. (Telesp)
- Tele Sudeste Celular Participaçoes, S.A.
- Telesp Celular Participaçoes, S.A.
- Tele Leste Celular Participaçoes, S.A.
- Celular CRT Participaçoes, S.A.
- Pearson P.L.C.
- Infonet Services Corporation.
- Telefónica Móviles El Salvador, S.A. de C.V.
- Telefónica Data Brasil Holding, S.A.
- CTC Transmisiones Regionales, S.A. (CTC Mundo)
- Fastibex, S.A.
- Telefónica Móviles Argentina, S.A.
- Telefónica Holding de Argentina, S.A.
- Telefónica Data Argentina, S.A.
- Telefónica Data Perú, S.A.A.
- Telefónica Móviles Perú Holding, S.A.A.

Short-term investments

This caption in the accompanying consolidated balance sheet as o
December 31, 2002, includes basically the following items:

- The investment in short-term assets of cash surpluses arising a
  Telefónica, which amounted to g1,274.37 million (g11.40 millio
  in 2001), and the investments made with the net level premium
  reserves of the Group’s insurance companies, which amounted t
  g448.90 million (g276.23 million in 2001).

- The short-term investments of the Terra Lycos Group recorde
  under the “Short-Term Investment Securities” caption, which
  amounted to g367.79 million (g591.59 million in 2001).

- The investments relating to the Telefónica Internacional Grou
  recorded under the “Other Loans” caption, which amounted t
  g493.46 million (g706.99 million in 2001).

(9) Deferred charges

The breakdown of the balance of this caption and the amortization schedule are as follows:

Millions of Euros

	2003	2004	Maturity 2005	2006	2007	Subsequent Years	Balance at 12/31/02	Balance at 12/3101
Supplementary pension payments to retired employees (shortfall) (Notes 4-g and 14)	63.52	63.43	61.59	61.59	30.79	–	280.92	338.73
Debt arrangement expenses	5.36	38.97	33.65	24.44	17.95	99.90	220.27	119.30
Executive loyalty-building program (Notes 4-g and 20)	14.62	0.93	–	–	–	–	15.55	23.89
Interest on long-term promissory notes	7.31	7.00	7.01	7.05	7.13	23.29	58.79	69.34
Interest on financial lease contracts	2.15	1.45	0.63	0.47	0.49	7.71	12.90	13.56
Externalization of commitments(Note 4-g)	12.60	11.76	10.44	8.91	7.47	18.64	69.82	–
Other deferred charges	37.45	25.68	16.12	10.48	8.40	45.90	144.03	146.12
Total	**143.01**	**149.22**	**129.44**	**112.94**	**72.23**	**195.44**	**802.28**	**710.94**

(10) Trade receivables

The detail of the balances of this caption as of December 31, 2002 and 2001, is as follows:

Millions of Euros

	Balance at 12/31/02	Balance at 12/31/01
Trade receivables billed	3,607.81	3,005.49
Doubtful trade receivables	773.53	1,606.11
Other receivables	45.73	47.16
Services billed	**4,427.07**	**4,658.76**
Unbilled services	1,495.81	2,124.48
Trade receivables	**5,922.88**	**6,783.24**
Allowance for bad debts	(1,663.56)	(1,692.89)
Net total	**4,259.32**	**5,090.35**

The “Unbilled Services” account includes the connection, monthly and meter service charges not yet billed by the Group operators. This amount arises because these companies’ subscriber billing schedules do not coincide with December 31 (see Note 4-q).

The balance of the public-sector trade receivables in the countries in which the Group operates amounted to g352.86 million as of December 31, 2002 (g410.16 million as of December 31, 2001).

In 2002 provisions totaling g555.64 million were recorded to the allowance for bad debts.

(11) Stockholders' equity

The detail of the balances of equity accounts and of the variations therein in 2002 and 2001 is as follows:

Millions of Euros

	Balance at 12/31/00	Distribution of 2000 Income	Other Variations	Capital Increase	Balance at 12/31/01	Distribution of 2001 Income	Other Variations	Capital Increase	Balance at 12/31/02
Capital stock	4,340.71	–	–	331.21	4,671.92	–	–	188.74	4,860.66
Additional paid-in capital	10,987.99	–	–	682.03	11,670.02	–	–	–	11,670.02
Revaluation reserves	3,235.66	–	–	(176.02)	3,059.64	–	–	(188.74)	2,870.90
Unrestricted reserves	3,787.48	(57.11)	(350.39)	–	3,379.98	329.65	1,106.74	–	4,816.37
Reserve for treasury stock	198.19	–	62.51	–	260.70	–	73.86	–	334.56
Other restricted reserves	657.97	–	–	–	657.97	–	–	–	657.97
Consolidation reserves	1,200.25	2,561.92	(429.30)	–	3,332.87	1,777.16	(1,239.89)	–	3,870.14
Translation differences in consolidation	(982.51)	–	(2,295.78)	–	(3,278.29)	–	(3,229.53)	–	(6,507.82
Income (Loss) for the year	2,504.81	(2,504.81)	2,106.81	–	2,106.81	(2,106.81)	(5,576.80)	–	(5,576.80
Total	**25,930.55**	**–**	**(906.15)**	**837.22**	**25,861.62**	**–**	**(8,865.62)**	**–**	**16,996.00**

The "Other Variations" column for 2002 relating to the "Unrestricted Reserves" and "Consolidation Reserves" accounts relates mainly to the dividends paid to the Parent Company by its subsidiaries.

a) Capital stock

As of December 31, 2002, Telefónica, S.A.'s capital stock amounted to €4,860,661,286 and consisted of 4,860,661,286 fully paid common shares of a single series and of €1 par value each, all recorded by the book-entry system traded on the Spanish computerized trading system ("Continuous Market") (in the selective "Ibex 35" Index), on the four Spanish Stock Exchanges (Madrid, Barcelona, Valencia and Bilbao) and on the New York, London, Paris, Frankfurt, Tokyo, Buenos Aires, São Paulo and Lima Stock Exchanges.

Pursuant to Royal Decree 8/1997, the prior administrative authorization system applies to certain corporate resolutions that might be adopted by Telefónica, S.A., Telefónica Móviles, S.A. and Telefónica de España, S.A., and to certain others which may give entitlement to the direct or indirect acquisition, including third-party trusts or interposed third parties, of shares or certain assets of Telefónica, S.A., Telefónica Móviles, S.A. or Telefónica de España, S.A. The administrative authorization system will remain in force for ten years from February 18, 1997.

On June 15, 2001, the Stockholders' Meeting authorized the Board of Directors to increase the Company's capital, at one or several times within a maximum period of five years from that date, under the terms provided by Article 153.1 b) of the Spanish Corporations Law (authorized capital) up to a maximum of €2,274,677,655, by issuing for this purpose the related new common shares, be they redeemable or of any other type permitted by the Law, with a fixed or variable premium, with or without preemptive subscription right and, in all cases, with disbursements for the new shares issued in the form of monetary contributions. As of December 31, 2002, the Board of Directors had not made use of this authorization.

Also on June 15, 2001, the Stockholders' Meeting approved two successive capital increases with a charge to unrestricted reserves, each for an amount equal to 2% of the subscribed and paid-in capital stock, which were carried out in the first few months of 2002, as indicated below.

In addition, on June 15, 2001, the Stockholders' Meeting resolved to empower the Board of Directors to issue, within a maximum period of five years, at one or several times, fixed-income securities convertible into or exchangeable for Company shares, up to a maximum amount of g2,000 million or an equal amount in another currency, and to increase capital by the amount required to cater for such conversion requests as might be made. As of December 31, 2002, the Board of Directors had not made use of these powers.

Furthermore, on April 12, 2002, the Stockholders' Meeting resolved to approve two successive capital increases with a charge to unrestricted reserves, each for an amount equal to 2% of the subscribed and paid-in capital stock, through two successive issues of new shares that will be assigned totally free of charge to the Company's stockholders at a ratio of one new share for every 50 shares held by them, and empowered the Board of Directors accordingly to execute the resolution in question within one year from the date on which it was adopted. Before December 31, 2002, the Board of Directors resolved to carry out the first of the two aforementioned capital increases, for a par value of g97,213,225, in January and February 2003 (see Note 23).

Also on April 12, 2002, the Stockholders' Meeting resolved to issue fixed-income securities convertible into new Company shares and/or exchangeable for existing shares of the Company or of any of the Group companies, with disapplication of the preemptive subscription right, for a total maximum amount of g2,000 million or an equal amount in another currency, and to increase capital by the amount required to cater for such conversion requests as might be made. It also granted the Board of Directors the necessary powers to implement the resolution adopted by the Stockholders' Meeting and to determine the features of the issue and capital increase not specified by the latter, including the express power to refrain from implementing, or to only partially implement, this resolution. As of December 31, 2002, the Board of Directors had not made use of these powers to implement this resolution.

In addition, on April 12, 2002, the Stockholders' Meeting resolved to increase capital by g2,180,809 through the issuance of new common shares with additional paid-in capital of g11.61 per share to cater for the needs derived from the establishment of a stock option plan for the employees of the Endemol Group. It also granted the Board of Directors the necessary powers to implement the capital increase resolution, including the express power to refrain from implementing the resolution. In a resolution dated December 18, 2002, the Board of Directors expressly decided not to implement the aforementioned resolution to increase capital, and opted to cover the stock option plan referred to above by a means other than through a capital increase with the issuance of new shares (i.e., through the prior acquisition of Telefónica shares on the stock market).

Also on April 12, 2002, the Stockholders' Meeting authorized the Board of Directors to derivatively acquire treasury stock, for consideration, up to the limits and pursuant to the terms and conditions established by the Stockholders' Meeting, within a maximum period of 18 months from that date. However, it established that in no case could the par value of the shares acquired, added to that of the treasury stock already held by Telefónica, S.A. and any of its controlled subsidiaries, exceed 5% of the capital stock of Telefónica.

As of December 31, 2002 and 2001, the Telefónica Group companies held the following shares of the Parent Company, Telefónica, S.A.:

	Number of Shares	Cost per Share(*)	Market Value	%
Treasury stock at 12/31/02	91,631,076	8.53 g	781.61	1.88516
Treasury stock at 12/31/01	45,440,901	14.22 g	646.17	0.97264

(*) Lower of the market value of the treasury stock at year-end or the average market price in the last quarter. As indicated in Note 4-i, a drop in the market value of the shares would lead to the recording of additional provisions with a charge to consolidated income, but would not affect the total amount of consolidated equity.

In 2002 the Company acquired for consideration 55,169,765 shares of treasury stock and 1,819,821 shares were assigned to it in the capital increases at no charge to stockholders. Also, 799,411 shares were used to acquire holdings in certain Brazilian companies from Iberdrola, S.A. (see Note 2-c), and 10,000,000 shares were sold, giving rise to a loss of g1.79 million. The average acquisition cost of the shares of treasury stock as of December 31, 2002 and 2001, was g11.65 and g14.85 per share, respectively.

The consolidated balance sheets as of December 31, 2002 and 2001, include the acquisition cost of the shares of treasury stock (g1,067.94 million and g674.73 million, respectively) net of allowances of g733.38 million and g414.03 million, respectively, the provisions to which were recorded, in accordance with current accounting regulations (see Note 4-i), with a charge to the consolidated statement of operations in respect of the market value of these shares (g286.33 million and g26.29 million as of December 31, 2002 and 2001, respectively) and with a charge to unrestricted reserves in respect of the amount by which the market value exceeds the underlying book value (g447.05 million and g387.74 million in 2002 and 2001, respectively). The provision recorded with a charge to the 2002 consolidated statement of operations amounted to g288.09 million (see Note 20).

The Company has recorded the related restricted reserve for the amount of these shares of treasury stock. Also, in 2002 and 2001 it recorded provisions of g59.29 million and g387.74 million, respectively, with a charge to the "Unrestricted Reserves" caption on the asset side of the accompanying consolidated balance sheets to reflect the underlying book value of the treasury stock (see Note 4-i).

Variations in capital stock and additional paid-in capital in 2002

The variations in 2002 in the “Capital Stock” and “Additional Paid-in Capital” captions were as follows:

Millions of Euros

	Date of Share Issue	Number of Shares	Capital Stock	Additional Paid-in Capital
Balance at December 31, 2001		**4,671,915,885**	**4,671.92**	**11,670.02**
Capital increase at no cost to stockholders	02/13/02	93,438,317	93.44	–
Capital increase at no cost to stockholders	04/12/02	95,307,084	95.30	–
Balance at December 31, 2002		**4,860,661,286**	**4,860.66**	**11,670.02**

The capital increases carried out and formalized in 2002 were as follows:

– On February 13, 2002, the notarial deed of formalization and execution of a capital increase at Telefónica, S.A. was executed. This capital increase, for a par value of €93,438,317, was carried out with a charge to unrestricted reserves through the issuance of an equal number of new common shares of the Company, of €1 par value each, which were assigned to the Company’s stockholders free of charge at a ratio of one new share for every 50 shares held by them.

  Following registration of the aforementioned public deed at the Mercantile Registry, the new shares were admitted to listing on official markets from February 26, 2002.

– On April 12, 2002, the notarial deed of formalization and execution of a further capital increase at Telefónica, S.A. was executed. This capital increase, for a par value of €95,307,084, was carried out with a charge to unrestricted reserves through the issuance of an equal number of new common shares of the Company, of €1 par value each, which were assigned to the Company’s stockholders free of charge at a ratio of one new share for every 50 shares held by them.

  Following registration of the aforementioned public deed at the Mercantile Registry, the new shares were admitted to listing on official markets from April 30, 2002.

As a result of these two capital increases with a charge to unrestricted reserves, the capital stock of Telefónica, S.A. amounted to €4,860,661,286. This figure remained unchanged through December 31, 2002.

Variations in capital stock and additional paid-in capital in 2001

The variations in 2001 in the "Capital Stock" and "Additional Paid-in Capital" captions were as follows:

Millions of Euros

	Date of Share Issue	Number of Shares	Capital Stock	Additional Paid-in Capital
Balance at December 31, 2000		**4,340,710,735**	**4,340.71**	**10,987.99**
Capital increase at no cost to stockholders	01/25/01	86,814,214	86.82	–
TIES program	02/14/01	1,123,072	1.13	4.49
TIES program	02/20/01	31,504,244	31.51	126.02
Capital increase at no cost to stockholders	04/03/01	89,203,045	89.20	–
Acquisition of wireless business in Mexico from Motorola	06/19/01	122,560,575	122.55	551.52
Balance at December 31, 2001		**4,671,915,885**	**4,671.92**	**11,670.02**

The capital increases carried out and formalized in 2001 were as follows:

– In January 2001 the first of the two capital increases of Telefónica, S.A. approved by the Stockholders' Meeting on April 7, 2000, and which the Board of Directors agreed to implement on December 20, 2000, was carried out with a charge to unrestricted reserves. Under the capital increase, 86,814,214 common shares of the Company of €1 par value each were issued, thereby increasing the capital stock by €86,814,214. The new shares issued were assigned to the stockholders free of charge at a ratio of 1 new share for every 50 shares already held by them.

The capital increase was executed in a public deed and registered at the Mercantile Registry on January 25, 2001, and the new shares were admitted to listing on the official markets from February 2, 2001.

– A first capital increase at Telefónica, S.A., for a par value of €1,123,072, through the issuance of the same number of new common shares of the Company, of the same class and series and carrying the same rights as the outstanding shares, and with additional paid-in capital of €4 per share, was executed in a public deed on February 14, 2001. The new shares were fully subscribed and paid, through a monetary contribution, by the employees of several Telefónica Group companies who decided to participate in the stock option plan known as the TIES Program aimed at Group employees (see Note 20).

Following registration of the aforementioned capital increase deed at the Mercantile Registry, the new shares were admitted to listing on official markets from February 16, 2001.

– On February 20, 2001, the notarial deed of formalization and execution of a second capital increase at Telefónica, S.A. was executed. This capital increase, for a par value of €31,504,244, was carried out through the issuance of an equal number of common shares of the same class and series and carrying the same rights as the outstanding shares of the Company and with additional paid-in capital of €4 per share. The new shares were fully subscribed and paid, through a monetary contribution, by Banco Bilbao Vizcaya Argentaria, S.A. (50%) and Caja de Ahorros y Pensiones de Barcelona "La Caixa" (50%) as the agent banks of the aforementioned TIES program (see Note 20).

Following registration at the Mercantile Registry of the public deed for this second capital increase covering the TIES Program, the new shares thus issued were admitted to listing on official markets from March 1, 2001.

– In March 2001 the second of the capital increases at Telefónica, S.A. approved by the Stockholders' Meeting on April 7, 2000, and which the Board of Directors agreed to implement on January 24, 2001, was carried out with a charge to unrestricted reserves. Under the capital increase, 89,203,045 common shares of the Company of g1 par value each were issued, thereby increasing the capital stock by g89,203,045. The new shares issued were assigned to the stockholders free of charge at a ratio of 1 new share for every 50 shares already held by them.

The capital increase was executed in a public deed on March 30, 2001, and registered at the Mercantile Registry on April 3, 2001, and the new shares were admitted to listing on the official markets from April 9, 2001.

– On June 18, 2001, the notarial deed of formalization and execution of the capital increase at Telefónica, S.A. approved by the Company's Stockholders' Meeting on June 15, 2001, was executed. Capital was increased through the issuance of 122,560,575 common shares of the Company of g1 par value each, of the same series and carrying the same rights as the outstanding shares of the Company and with additional paid-in capital of g4.50 per share; these shares were subscribed and their par value and additional paid-in capital were paid in full through a nonmonetary contribution to Telefónica, S.A. of various Mexican companies owned by the Motorola Group, which entailed the direct or indirect acquisition by Telefónica, S.A. of all the shares of Telefónica Celular del Norte, S.A. de C.V., Celular de Telefonía, S.A. de C.V. and Baja Celular Mejicana, S.A. de C.V., and of holdings of 90% in Movitel del Noroeste, S.A. de C.V., Moviservicios, S.A. de C.V. and Movicelular, S.A. de C.V. (see Exhibit II).

The number of issued shares subscribed and paid by the persons or entities that transferred the aforementioned Mexican cellular companies was determined by applying the following variables defined by Telefónica, S.A.'s Stockholders' Meeting and Board of Directors' Meeting on June 15, 2001.

  – Value of the contributed assets for the purpose of their exchange for shares of Telefónica: g2,173,742,973.96. This amount is the result of applying the U.S. dollar/euro exchange rate of US$ 0.8492/g1 prevailing on June 14, 2001, to the amount of US$ 1,857,300,000 (initial valuation), less US$ 14,123,000 (debt adjustment), plus US$ 2,765,533.49 (interest accrued through the exchange transaction date).

  – Value of the Telefónica shares to be exchanged: g17.6355 each, i.e. an amount equal to the average market price of the Company's shares in the 20 trading sessions prior to the date on which the Stockholders' Meeting which approved the capital increase was held (June 15, 2001).

  – Cash disbursement: g12,325,950.35, equal to 10% of the result of dividing the value of the assets by the value of each Telefónica share.

The aforementioned public deed of capital increase stated that solely for the purpose of evidencing the full payment of the capi tal increase and the additional paid-in capital, pursuant to Articl 133.1 of the Mercantile Registry Regulations, regardless of the cri teria used to determine the exchange ratio, a total value o g674,083,162.50 was attributed to the nonmonetary contribu tion, which is lower than that established by the independen appraiser appointed by the Madrid Mercantile Registry, and i also lower than that used as a reference for setting the exchang ratio.

This capital increase was registered at the Madrid Mercantil Registry on June 19, 2001, and the new shares issued were admit ted to listing on official markets from June 25, 2001.

b) Legal reserve

Under the revised Corporations Law, 10% of income for each yea must be transferred to the legal reserve until the balance of thi reserve reaches at least 20% of capital stock. The legal reserve can b used to increase capital provided that the remaining reserve balanc does not fall below 10% of the increased capital stock amount. Oth erwise, until the legal reserve exceeds 20% of capital stock, it ca only be used to offset losses, provided that sufficient other reserve are not available for this purpose.

c) Revaluation reserves

The balance of the "Revaluation Reserves" caption arose as a result o revaluations made from 1946 to 1987 and of the revaluation mad pursuant to Royal Decree-Law 7/1996.

The detail as of December 31, 2002 and 2001, of the balances of th revaluation reserves, which amounted to g2,870.90 million an g3,059.64 million, respectively, and of the variations therein in 200 and 2001, is as follows:

Millions of Euros

Revaluations made from 1946 to 1987	4,478.76
Revaluation made pursuant to Royal Decree-Law 7/1996	1,357.40
Amounts used:	
Capital increases from 1977 to 1986	(447.68
Transfer to provisions in 1982	(113.16
Single tax on revaluation, Royal Decree-Law 7/1996	(40.72
Other variations from 1981 to 1986	(15.45
Amount used in 1998	(1,795.07
1999 capital increase	(188.42
Balance at 12/31/00	**3,235.66**
Capital increase on January 25, 2001	(86.82
Capital increase on April 3, 2001	(89.20
Balance at 12/31/01	**3,059.64**
Capital increase on February 13, 2002	(93.44
Capital increase on April 12, 2002	(95.30
Balance at 12/31/02	**2,870.90**

The balance of the "Revaluation Reserve Royal Decree-Law 7/1996 account can be used, free of tax, to offset recorded losses whic might arise in the future, and to increase capital stock. From Januar 1, 2007 (ten years from the date of the balance sheet reflecting th revaluations), the balance of this account can be taken to unrestricted reserves, provided that the monetary surplus has been realized. The surplus will be deemed to have been realized in respect of the portion on which depreciation has been taken for accounting purposes or when the revalued assets have been transferred or retired from the accounting records.

d) Consolidation reserves

The detail of the consolidation reserves as of December 31, 2002, and of the variations therein in 2002 is as follows:

Millions of Euros

	Balance at 12/31/01	Increase	Decrease	Balance at 12/31/02
Fully consolidated companies	3,773.35	3,217.16	(2,587.86)	4,402.65
Companies accounted for by the equity method	(440.48)	69.26	(161.29)	(532.51)
Total	**3,332.87**	**3,286.42**	**(2,749.15)**	**3,870.14**

The detail of the consolidation reserve as of December 31, 2001, and of the variations therein in 2001 is as follows:

Millions of Euros

	Balance at 12/31/00	Increase	Decrease	Balance at 12/31/01
Fully consolidated companies	1,045.78	4,727.86	(2,000.29)	3,773.35
Companies accounted for by the equity method	154.47	313.75	(908.70)	(440.48)
Total	**1,200.25**	**5,041.61**	**(2,908.99)**	**3,332.87**

The variations shown in the foregoing tables relate mainly to prior years' retained earnings (increases) and to dividends paid and losses incurred by the companies (decreases).

The detail of the contribution made by the Group companies to the consolidated reserves is shown in Exhibit I.

e) Translation differences in consolidation

The translation differences relate mainly to the effect of exchange rate fluctuations on the net assets of the companies located abroad after elimination of intercompany transactions and balances (see Note 4-b). This caption also includes the exchange differences resulting from specific-purpose foreign-currency financing transactions relating to investments in investees and which hedge the exchange risk on these investments.

The detail of the contribution made by the Group companies to the translation differences in consolidation is shown in Exhibit I.

(12) Minority interests

This caption relates to the share of minority stockholders in the equity and income/loss for the year of the fully consolidated Group companies. The variations in 2002 and 2001 in the balances of this caption in the consolidated balance sheets were as follows:

Millions of Euros

Balance at 12/31/00	**9,329.80**
Capital contribution and inclusion of companies	215.55
Loss for the year	(271.01)
Variation in translation differences	(215.49)
Other variations	(1,130.20)
Capital reduction and exclusion of companies	(373.23)
Dividend paid	(121.87)
Balance at 12/31/01	**7,433.55**
Capital contribution and inclusion of companies	3,325.65
Preferred share issue	2,000.00
Loss for the year	(5,795.61)
Variation in translation differences	(990.51)
Other variations	(142.70)
Capital reduction and exclusion of companies	(108.33)
Dividend paid	(109.12)
Balance at 12/31/02	**5,612.93**

The detail of the balances of this caption and of the variations relating to the main Group companies is shown in Exhibit IV.

The capital contributions and inclusions of companies in 2002 relate mainly to the conversion of debt to equity at Group 3G UMTS Holding GmbH, which gave rise to an increase of g3,051.36 million in the liability relating to minority interests (see Note 19).

The balance of the "Preferred Share Issue" account relates to the share issue launched by the Telefónica subsidiary Telefonica Finance USA, LLC for g2,000 million in December 2002.

The features of this share issue were as follows:

– Dividend: variable and non-cumulative:

  – Through December 30, 2012, the dividend will be 3-month Euribo with a maximum of 7% APR and a minimum of 4.25% APR; and

  – From that date on, 3-month Euribor plus a spread of 4% APR.

– Dividend payment:

  – dividends will be paid quarterly in arrears.

  – payment of dividends is conditional upon the Telefónica Grou having reported consolidated net income.

– Term: perpetual, with the option for the issuer of total or partia early redemption, from December 30, 2012, and at face value, o the shares issued.

– Remuneration: preferred, non-cumulative dividends, conditiona upon the obtainment of consolidated income or upon the pay ment of dividends on common shares.

– Guarantee: irrevocable joint and several Telefónica, S.A. guarantee

– Voting rights: none

The balance of the "Loss for the Year" account in 2002 includes mos notably the losses amounting to g874.38 million and g4,580.32 mil lion incurred in the year by the Terra Lycos Group and the Telefónica Móviles Group, respectively, and attributed to the minority stock holders of these groups (see Note 1).

(13) Deferred revenues

The detail of the balances of this caption in the accompanying consolidated balance sheets and of the variations therein in 2002 and 2001 is as follows:

Millions of Euros

	Capital Subsidies	Exchange Gains	Accrual of Investment Tax Credit (Note 18)	Other	Total
Balance at 12/31/00	**368.25**	**4.23**	**160.83**	**908.70**	**1,442.01**
Additions	12.88	60.85	0.05	231.15	304.93
Transfers and other variations	0.01	(0.51)	4.67	(3.19)	0.98
Allocation to income	(80.03)	(63.02)	(63.63)	(395.49)	(602.17)
Balance at 12/31/01	**301.11**	**1.55**	**101.92**	**741.17**	**1,145.75**
Additions	0.96	36.51	91.88	99.73	229.08
Transfers and other variations	(0.21)	4.71	(0.65)	(201.50)	(197.65)
Allocation to income	(63.79)	(39.31)	(36.09)	(157.53)	(296.72)
Balance at 12/31/02	**238.07**	**3.46**	**157.06**	**481.87**	**880.46**

The "Other" caption includes g143.80 million and g225.00 million as of December 31, 2002 and 2001, respectively, relating to the revenue to be collected in the five years following 1999 for the future deduction at Telesp of amortization of goodwill, which is tax deductible at that company.

The "Other" caption in the foregoing table also includes g186.41 million and g318.69 million as of December 31, 2002 and 2001, respectively, as a result of the negotiations between certain Brazilian subsidiaries and their employees, which disclosed the possibility of allocating to income over the remaining years of working life of the employees covered by the new pension plan the amounts provisioned in previous years under the terms and conditions then prevailing. The revaluation of the terms existing at 2002 and 2001 year-end in connection with these employees led to the allocation in 2001 of g172.16 million to the "Extraordinary Revenues" caption in the consolidated statement of operations (see Note 20).

This caption also includes g101.45 million as of December 31, 2002, relating to the amounts collected by Telefónica de España and Emergia from other operators for the use of underwater cable systems.

Capital subsidies

The detail of the capital subsidies not yet allocated to income is as follows:

Millions of Euros

Grantor	12/31/02	12/31/01
Official agencies, autonomous community governments, provincial and municipal governments and other	49.58	70.42
EU-		
STAR Programme	4.19	10.39
ERDF Programme	6.57	10.56
IRTA Programme	0.70	2.34
ERDF 94/95 Operating Programme	169.99	199.96
Other	7.04	7.44
Total	**238.07**	**301.11**

(14) Provisions for contingencies and expenses

The detail of the balances of the provisions for contingencies and expenses and of the variations therein in 2002 and 2001 is as follows:

Millions of Euros

	Balance at 12/31/00	Provisions	Amounts Used	Incl. of Companies	Other	Balance at 12/31/01	Provisions	Amounts Used	Incl. of Companies	Transfers and Other	Balance at 12/31/02
Provision for supplementary pension payments to retired employees (Note 9)	382.05	23.52	(108.03)	–	–	297.54	15.89	(0.43)	–	(313.00)	–
Group insurance	101.55	10.48	(0.95)	–	–	111.08	12.04	(1.40)	–	(112.68)	9.04
Provision for preretirement, social security expenses and voluntary severance	4,000.21	220.91	(731.80)	–	–	3,489.32	222.41	(428.76)	–	(2,148.95)	1,134.02
Technical reserves (Note 4-m)	892.12	61.55	–	–	–	953.67	17.24	(258.34)	–	2,574.68	3,287.25
Provision for pension funds of other companies	235.96	19.89	(4.03)	0.05	(70.00)	181.87	22.54	(28.33)	–	(53.98)	122.10
UMTS provision	–	–	–	–	–	–	2,371.46	(72.49)	–	–	2,298.97
Other provisions	1,275.91	174.63	(589.90)	(0.01)	(31.41)	829.22	348.93	(73.78)	60.46	(1.30)	1,163.53
Total	**6,887.80**	**510.98**	**(1,434.71)**	**0.04**	**(101.41)**	**5,862.70**	**3,010.51**	**(863.53)**	**60.46**	**(55.23)**	**8,014.91**

The main provisions and commitments to employees recorded under this caption in the accompanying consolidated balance sheets are as follows:

Supplementary pension payments to employees who retired before June 30, 1992

On July 8, 1992, Telefónica reached an agreement with its employees whereby it recognized supplementary pension payments for employees who had retired as of June 30, 1992, equal to the difference between the pension payable by the social security system and that which would be paid to them by ITP. Once the aforementioned supplementary pension payments have been quantified, they become fixed, lifelong and non-updateable. 60% of the payments are transferable to the surviving spouse recognized as such as of June 30, 1992, and to underage children.

In accordance with an actuarial study conducted by Telefónica, applying GRM-F8o tables and an assumed interest rate of 8%, as of June 30, 1992, the discounted present value of the commitments amounted to g793.49 million, and this amount was recorded under the “Provisions for Contingencies and Expenses” caption. Through that date, the Company had recorded provisions totaling g86.28 million in this connection. The resulting underprovision (g707.21 million) was recorded under the “Deferred Charges” caption and has been allocated to income since that date by the straight-line method over 15 years, the estimated average remaining life of the retired employees (1992-2007). Subsequently, in 1996 and 1997, the assumed interest rate was reduced to 6.3% and the necessary provision was recalculated accordingly. As of December 31, 2002, the amount yet to be charged to income was g277.14 million (g338.73 million in 2001) (see Note 9).

In accordance with Private Insurance Law 30/1995, on November 1, 1997, these commitments were externalized through an insurance policy (which was adapted before November 16, 2002, pursuant to Private Insurance Law 30/1995, Law 50/1998 on Tax, Administrative, Labor and Social Security measures and Royal Decree 1588/1999 enacting the regulations on the instrumentation of employers’ pension commitments to employees and beneficiaries) taken out with the Group company Seguros de Vida y Pensiones Antares, S.A.

Group life insurance (internal allowance for survivorship benefits)

Serving employees who did not join the pension plan continue to be entitled to receive survivorship benefits at the age of 65. Telefónica de España has recorded a provision to cover these commitments, based on the actuarial calculations made under the following assumptions: GRM/F-95 mortality table and an assumed interest rate of 4%. Most of these commitments were externalized in 2002. As of December 31, 2002 and 2001, this provision amounted to g9.04 million and g111.08 million, respectively.

Provisions for preretirements, early retirements, social security expenses and voluntary severances of Telefónica de España employees

In order to adapt to the competitive environment, in prior years Telefónica implemented preretirement, early retirement and technology renewal plans in order to adapt its cost structure to the new environment and took certain strategic decisions relating to its sizing and organization policy.

Against this backdrop, as a result of the agreements reached individually with the Telefónica de España employees, a total of 11,273 and 6,062 employees left the company in 1999 and 2000, respectively.

In 2001 provisions of g220.91 million for adjusting to present value were recorded, and payments totaling g731.80 million were made. Accordingly, the provision for preretirements and early retirements recorded as of December 31, 2001, covered all the obligations assumed in this connection.

In November 2002 the Company’s preretirement and early retirement commitments to employees under labor force reduction plans were externalized through a policy taken out with Antares. This caption continues to include the liabilities relating to severances of Telefónica de España employees and to the Special Social Security Agreement, the main features of which are explained in Note 4-l.

Technical reserves

This caption includes the reserves recorded by the Group’s insurance companies. As indicated in various sections of these notes to consolidated financial statements, in November 2002, pursuant to prevailing legislation, various of Telefónica de España’s commitments to its employees were externalized to the Group company Seguros de Vida y Pensiones Antares, S.A. The “Transfers” column in the “Provisions for Contingencies and Expenses” table shown above includes the effect of transferring these Telefónica de España commitments and obligations to the insurance company’s accounts. As of December 31, 2002, the main items and amounts included under the “Technical Reserves” caption were as follows:

Millions of Euros

Supplementary pension payments for retired personnel	579.05
Group life insurance	125.62
Preretirements and early retirements	2,407.67
Other technical reserves	174.91
Total	**3,287.25**

The companies that still have these commitments calculated the amounts to be provisioned at 2002 year-end using actuarial assumptions pursuant to current legislation, including most notably the ERM/F-2000 mortality tables and a floating interest rate of between 2.80% and 4% for the most significant figures, based on the related hire dates.

Provision for the pension funds of other companies

The subsidiary Telecomunicações de São Paulo, S.A. (Telesp) has had various pension plan and medical insurance commitments to its employees since 2000, the year in which these commitments were negotiated and converted into defined-contribution plans. Substantially all of this company’s serving employees availed themselves of these plans. As of December 31, 2002, the provision recorded in this connection amounted to g74.12 million.

As of December 31, 2002, this caption also included an amount of g36.83 million relating to Telefónica de Argentina, S.A.’s commitments to its employees.

The variations in the “Other” column in 2002 and 2001 relate mainly to translation differences.

UMTS provisions

As indicated in Note 1 in relation to the value adjustments performed on UMTS licenses, this caption includes most notably a provision of g2,371.46 million. As of December 31, 2002, the balance of this caption, net of the amounts used in the year, was g2,298.97 million.

Other provisions

The balance of this caption as of December 31, 2002, includes various provisions recorded by the Telefónica Group companies, including most notably g120.01 million from the Telefónica Internacional subgroup relating to provisions for severance costs for the employees' years of service at the respective companies, in accordance with the legislation applicable in each country or with the contractual agreements entered into (g272.00 million as of December 31, 2001), and g158.40 million from Telefónica de España relating to the accrued amount of long-service bonuses paid to personnel after 25 years of service (g141.54 million in 2001).

Also, certain Group companies, mainly those forming part of the Endemol Group, when investing in other companies make payment of part of the agreed price conditional upon compliance by the acquired company with some related future goal, in most case increased revenues, the obtainment of income, etc. Since a part o the acquisition price is therefore not fixed, each year the necessar estimates are made to evaluate the possible liabilities inherent t these transactions. As of December 31, 2002, the amounts provi sioned in this connection, g202.48 million and g38.59 million, wer recorded under the long-term "Provisions for Contingencies anc Expenses" and "Short-Term Provisions for Contingencies and Expens es" captions, respectively.

Lastly, the provisions and the amounts used recorded in 2002 anc 2001 under the "Other Provisions" caption include, inter alia, the pro visions recorded (or used) by the Group companies to cover the risk inherent to the realization of certain assets, the contingencies deriv ing from their respective business activities and the risks arising from commitments acquired in other transactions.

(15) Debentures, bonds and other marketable debt securities

The variations in the years ended December 31, 2002 and 2001, in the balances relating to debentures, bonds and other marketable debt securities were as follows:

	Issues			
	Non-Convertible Euro	Non-convertible Foreign Currency	Promissory Notes and Commercial Paper	Total
Balance at 12/31/00	**4,836.02**	**10,104.97**	**451.53**	**15,392.52**
New issues	2,189.52	1,600.51	3,754.31	7,544.34
Redemptions, conversions and exchanges	(1,131.86)	(1,995.04)	(2,486.20)	(5,613.10)
Inclusion of companies	–	16.25	–	16.25
Adjustments and other variations	119.21	(414.60)	(39.37)	(334.76)
Balance at 12/31/01	**6,012.89**	**9,312.09**	**1,680.27**	**17,005.25**
New issues	230.00	53.98	3,777.64	4,061.62
Redemptions, conversions and exchanges	(152.24)	(807.54)	(4,014.59)	(4,974.37)
Inclusion of companies	–	–	637.81	637.81
Adjustments and other variations	70.85	(1,312.30)	(182.96)	(1,424.41)
Balance at 12/31/02	**6,161.50**	**7,246.23**	**1,898.17**	**15,305.90**
Maturity:				
Long term	5,911.48	6,440.02	617.72	12,969.22
Short term	250.00	806.20	1,280.48	2,336.68
Unmatured accrued interest	288.95	–	–	288.95

The main issues in 2002 were as follows:

	Date	Face Value (Millions)	Currency	Maturity	Interest Rate
Note	04/11/02	100	Euros	2003	4.08% (discount)
Note	04/19/02	50	Euros	2005	(a)
FRN	06/18/02	80	Euros	2004	Floating Eonia + 0.30%

(a) Structured issue with a final interest rate of 3-month Euribor + 0.40%.

The main issues in 2001 were as follows:

	Date	Face Value (Millions)	Currency	Maturity	Interest Rate
Notes	07/09/01	30,000	Yen	2003	Floating Libor (0.22%)
Notes	07/12/01	22,000	Yen	2002	0.15%
Notes	09/12/01	50,000	Yen	2002	0.04%
Notes	10/30/01	2,000	Euros	Tranches (a)	–
Notes	08/20/01	150	Euros	2003	Floating Eonia (0.26%)
Notes	07/25/01	39.5	Euros	2004	4.91%

(a)	Amount	Maturity	Interest Rate
Tranche 1	g1,000 million	2004	Floating 3-month Euribor + (0.70%)
Tranche 2	g1,000 million	2006	5.13%

The debentures and bonds are shown in greater detail in Exhibit V.

Corporate promissory notes

The features of the main corporate promissory note issue program as of December 31, 2002, are as follows:

Millions of Euros Limit Outstanding	Addressed to:	Euros Face Value	Method of Sale
		1,000	Monthly auctions
2,000	Participating entities		
		1,000,000	Specific transactions

Commercial paper

The features of Telefónica Europe, BV's commercial paper issue program are as follows:

Millions of Euros Limit Outstanding	Addressed to:	Face Value	Method of Sale
		US$ 500,000	Specific transactions
2,000	Investors	g500,000	Specific transactions
		¥100,000,000	Specific transactions
		£100,000	Specific transactions

Also, as of December 31, 2002, Telefónica del Perú, S.A.A. had a commercial paper issue program with a maximum limit outstanding of US$ 180 million. The commercial paper relating to this issue was sold in specific transactions.

(16) Payable to credit institutions

The detail of the accounts payable to credit institutions is as follows:

Millions of Euros

	Balance at 12/31/02			Balance at 12/31/01		
	Short Term	Long Term	Total	Short Term	Long Term	Total
Corporate promissory notes	7.09	106.56	113.65	7.23	113.65	120.88
Loans and credits	2,198.44	3,569.39	5,767.83	4,254.85	3,307.05	7,561.90
Foreign currency loans	1,867.14	3,236.99	5,104.13	1,901.46	4,658.38	6,559.84
Total	**4,072.67**	**6,912.94**	**10,985.61**	**6,163.54**	**8,079.08**	**14,242.62**

As of December 31, 2002, the average interest rates on the corporate promissory notes, loans and credits and foreign currency loans were 13.52%, 3.46% and 2.12%, respectively. These percentages do not include the effect of the hedging transactions performed by the Group.

The most significant financial transactions in 2002 and 2001 were as follows:

	Amount (Millions)	Currency	Date	Maturity
BBK loan	100.00	Euro	03/26/02	03/26/04
Drawdown of syndicated loan (Tranche B)	1,500.00	Euro	08/27/02	08/27/03
Citibank loan	128.00	U.S. Dollar	03/20/01	12/21/01
BBVA loan	115.00	U.S. Dollar	12/21/01	07/02/06
BBVA loan	105.00	U.S. Dollar	03/20/01	11/21/02

The main repayments made in 2002 and 2001 were as follows:

	Amount (Millions)	Currency	Date
Drawdown of syndicated loan (Tranche A)	1,915.43	Euro	08/27/02
Qualcomm loan	433.96	U.S. Dollar	11/10/02
BBVA loan	103.44	U.S. Dollar	11/21/02
Citibank loan	127.40	U.S. Dollar	12/21/01
Citibank loan	100.00	U.S. Dollar	12/28/01

The claimability of certain financing arranged by various Telefónica Group companies may be subject to compliance with certain financial covenants. All the covenants were being complied with at the date of preparation of these consolidated financial statements.

The scheduled maturities for repayment of the debt as of December 31, 2002, were as follows:

Millions of Euros

	2003	2004	2005	2006	2007	Subsequent Years	Total
Corporate promissory notes	7.09	6.92	6.74	6.57	6.37	79.96	113.65
Loans and credits	2,198.44	1,159.41	917.05	1,029.90	195.22	267.81	5,767.83
Foreign currency loans	1,867.14	1,339.18	625.64	324.68	189.48	758.01	5,104.13
Total	**4,072.67**	**2,505.51**	**1,549.43**	**1,361.15**	**391.07**	**1,105.78**	**10,985.61**

As of December 31, 2002, the Telefónica Group had financing sources of various types exceeding g8,000 million and the possibility of negotiating the maturity dates of various of the existing financing commitments and, accordingly, any need of the Group arising from its short-term commitments is adequately covered.

Foreign currency loans

The detail of the foreign-currency loans as of December 31, 2002 and 2001, is as follows:

	Outstanding Balance (in Millions)			
	Foreign Currency		Euros	
Currency	12/31/02	12/31/01	12/31/02	12/31/01
U.S. dollars	4,657	4,860	4,441.36	5,454.30
Brazilian reais	512	–	138.15	–
Swiss francs	11	21	7.35	14.50
Argentine pesos	54	48	15.34	31.67
Bolivares	10,684	4,227	7.34	6.25
Yen	40,644	18,629	326.75	158.99
UF	206	129,144	27.35	221.36
New soles	315	583	85.45	189.75
Colones	–	3,077	–	1.52
Swaps	–	–	–	366.72
Pounds sterling	25	19	38.34	31.77
Mexican pesos	–	571	–	70.14
Other currencies	–	–	16.70	12.87
Total for the Group			**5,104.13**	**6,559.84**

(17) Derivatives

In 2002 the Group continued to use derivatives both to limit interest rate and exchange risks on unhedged positions and to adapt its debt structure to market conditions.

As of December 31, 2002, the total outstanding balance of hedging transactions arranged to eliminate balance sheet exposure to interest rate and exchange risks was g36,909.02 million (g39,430.49 million as of December 31, 2001), of which g18,431.37 million related to interest rate risk and g18,100.61 million to exchange risk (g18,444.25 million and g20,537.39 million as of December 31, 2001, respectively) (see Exhibit VI).

Most of the derivatives transactions are assigned directly to individual asset or liability positions on the consolidated balance sheet. Also, there is a transaction portfolio hedging other financial risks of the Group. The net financial expense incurred in 2002 in relation to these transactions amounted to g141.50 million.

(18) Tax matters

Pursuant to a Ministerial Order dated December 27, 1989, since 1990 Telefónica, S.A. has filed consolidated tax returns with certain Group companies. 67 companies formed the consolidated tax group in 2002.

Deferred tax assets and liabilities

The detail as of December 31, 2002 and 2001, of the Telefónica Group's deferred tax assets and liabilities, and of the variations there in 2002 and 2001, is as follows:

Millions of Euros

	Deferred and Other Tax Assets		Deferred Tax Liabilities		
	Short Term	Long Term	Short Term	Long Term	Intercompany Long Term
Balance at December 31, 2000	**152.68**	**2,666.11**	**3.36**	**1,334.57**	**54.85**
Reversal	(100.32)	(423.83)	(4.70)	(622.49)	(2.75)
Arising in the year	224.85	1,582.81	241.51	525.65	6.37
Net international variations	–	(98.43)	–	–	–
Inclusion/Exclusion of companies and other	(1.94)	31.12	–	244.72	0.16
Balance at December 31, 2001	**275.27**	**3,757.78**	**240.17**	**1,482.45**	**58.63**
Reversal	(213.86)	(995.88)	(189.00)	(150.80)	(1.67)
Arising in the year	238.43	6,576.84	90.87	367.55	8.05
Net international variations	15.03	(120.89)	–	(186.48)	–
Inclusion/Exclusion of companies and other	(4.77)	118.58	(10.48)	71.35	(19.62)
Balance at December 31, 2002	**310.10**	**9,336.43**	**131.56**	**1,584.07**	**45.39**

The balance of the “Long-Term Investments - Taxes Receivable” caption, which amounts to g9,679.42 million (see Note 8), includes, in addition to the deferred and other tax assets shown in the foregoing table, an amount of g342.99 million relating to tax credits recorded as indicated below.

The deferred intercompany taxes relate to the differences arising from the elimination of unrealized gains on intercompany transactions, plus the cumulative differences between the net tax payable reported in the Telefónica Group’s consolidated corporate income tax return and the sum of the net tax charges per the individual corporate income tax returns of the Telefónica Group companies.

In 2001 the income that qualified for tax deferral due to reinvestment in prior years was reversed, since the Group availed itself of a new tax credit for reinvestment of extraordinary income pursuant to Transitional Provision Three of Law 24/2001 on Tax, Administrative, Labor and Social Security Measures, which increased the Group’s taxable income by g1,359.72 million.

Taxes payable and taxes receivable

The detail of the “Other Nontrade Payables - Taxes Payable” and “Accounts Receivable - Taxes Receivable” captions as of December 31, 2002 and 2001, is as follows:

Millions of Euros

	Balance at 12/31/02	Balance at 12/31/01
Taxes payable:		
Personal income tax withholdings	106.77	96.00
VAT and Canary Islands general indirect tax	241.73	160.26
Corporate income tax	38.98	113.97
Accrued social security taxes	177.28	155.38
Deferred tax liabilities	131.56	240.17
Foreign taxes	331.71	825.34
Other	20.49	33.03
Total	**1,048.52**	**1,624.15**

Millions of Euros

	Balance at 12/31/02	Balance at 12/31/01
Taxes receivable:		
Withholdings at source from income from movable capital	11.13	3.49
Installment payments on individual income tax returns	6.04	25.23
Foreign withholding tax	296.63	155.75
Corporate income tax refundable	109.50	66.63
Taxes, surcharges and other payments recoverable	31.69	42.28
Deferred tax assets	310.10	275.27
VAT and Canary Islands general indirect tax	52.28	116.16
VAT deductible	107.97	70.66
Foreign taxes	130.03	1,322.01
Total	**1,055.37**	**2,077.48**

Reconciliation of the income/loss per books to the tax base for corporate income tax purposes and determination of the tax expense/revenue

The reconciliation of the income/loss per books to the tax base fo corporate income tax purposes as of December 31, 2002 and 2001 and the determination of the corporate income tax expense/revenue and the net tax payable/refundable for the two years are a follows:

Millions of Euros

	2002	2001
Income (Loss) per books	(14,601.06)	2,033.88
Permanent differences	(1,880.14)	(3,980.06
Timing differences	2,169.86	2,079.40
Tax base	**(14,311.34)**	**133.22**
Gross tax payable	(5,008.97)	46.63
Tax credits and tax relief	(409.41)	(278.79
Unrecorded tax assets	485.82	–
Corporate income tax payable (receivable)	**(4,932.56)**	**(232.16**
Tax effect of timing differences and deferred revenues	(705.70)	(719.66
Consolidation adjustments	2,299.66	139.68
Spanish corporate income tax expense	(3,338.60)	(812.14
Recognition of deferred tax liabilities in consolidation	(1.99)	(4.18
Accrued foreign taxes and other	111.94	1,014.40
Total income tax	**(3,228.65)**	**198.08**

The Spanish corporate income tax expense includes a revenue o g2,837.16 million relating to tax assets that arose as a result of th value adjustments made on the UMTS licenses (see Note 1).

The permanent differences arose mainly from the results obtained b the companies located abroad, the amortization of consolidation good will (see Note 5) and the results attributable to associated companies.

The main timing differences in 2002 arose from the investment val uation allowances recorded by the individual companies for th amounts yet to be allocated to income in connection with thei equity investments. Noteworthy in 2001 was the inclusion in the ta base of gains on fixed asset disposals which qualified for reinvest ment deferral in prior years, and the allowance for decline in value o tangible fixed assets.

The “Consolidation Adjustments” account includes the elimination made to adjust the consolidated income tax expense to the transac tions reflected in the consolidated statement of operations. Thes eliminations relate basically to the tax effect recognized in the indi vidual financial statements in connection with the provision to th investment valuation allowance eliminated in consolidation.

In 2001 the tax Group took tax credits totaling g371.99 million. I 2002, although no tax credits were taken since the tax Grou incurred a tax loss, an asset of g342.99 million was recorded pur suant to the resolution of the Spanish Accounting and Audit Insti tute (ICAC) dated March 15, 2002 (see Note 4-p). The amount of th tax credits taken by the other non-tax Group companies in 2002 wa not material.

As of December 31, 2002, the Telefónica tax group had €599.78 million (€567.95 million in 2001) of unused tax credits, relating mainly to 1999 (€131.33 million), 2000 (€144.47 million), 2001 (€246.45 million) and 2002 (€77.53 million). The aforementioned amount includes €342.99 million of tax credits recorded under the "Long-Term Investments - Taxes Receivable" caption. These tax credits, which were reflected for accounting purposes as indicated in the preceding paragraph, relate basically to tax credits for investments in fixed assets and R&D expenses. Of this amount, €254.89 million were recorded as a revenue under the "Corporate Income Tax" caption and the remaining €88.10 million are recorded under the "Deferred Revenues" caption (see Note 13).

The tax losses available for carryforward in Spain at the main Group companies total €16,911.80 million, of which €14,410.74 million and €1,212.80 million were incurred in 2002 and 2001, respectively, and the remainder relates mainly to 2000. These tax losses can be offset within 15 years. €14,537.63 million of these tax losses were capitalized, giving rise to a tax asset of €5,088.17 million, which was recorded under the "Long-Term Investments - Taxes Receivable" caption.

Also, Telefónica Móviles, S.A. is assessing the possibility of making a negative adjustment of €2,137.24 million in its corporate income tax settlement arising as a result of the transfer in 2002 of certain holdings acquired in prior years the market value of which differed from the book value at which they were recorded (underlying book value) because the Company availed itself of Article 159 of the Corporations Law. As of the date of preparation of these consolidated financial statements, no accounting effects in relation to these holdings had been considered.

As indicated in Note 1 and based on an analysis of its future earnings expectations, in 2002 the Terra Networks Group, in accordance with the accounting principle of prudence in valuation, did not record the tax assets relating to the 2002 losses, and partially wrote off the tax assets recorded for prior years. The effect on the accompanying consolidated statement of operations, an expense of €272.59 million, was recorded under the "Corporate Income Tax" caption. This amount was calculated taking into account the reversal of deferred tax liabilities recorded in prior years that was performed to avoid the duplication of tax assets. Noteworthy in this connection is the fact that once the effect of the losses attributed to minority interests is taken into account, this expense does not have a material effect on the Telefónica Group's consolidated net loss for 2002.

On September 25, 2002, tax audits commenced at several of the companies included in tax Group 24/90 of which Telefónica, S.A. is the parent company. The taxes subject to review are corporate income tax (for the years from 1998 to 2000) and VAT and tax withholdings and prepayments relating to personal income tax, tax on income from movable capital, property tax and nonresident income tax (1998 to 2001). No material liabilities are expected to arise as a result of the reviews currently being performed by the tax inspection authorities.

The years open for review by the tax inspection authorities for the main applicable taxes vary from one consolidated company to another, based on each country's tax legislation, taking into account their respective statute-of-limitations periods. In Spain, as a result of the tax review currently in progress, the tax Group has the following years open for review: the years since 2002 for tax withholdings and prepayments relating to personal income tax, tax on income from movable capital, property tax, nonresident income tax and VAT; and the years since 2001 for corporate income tax.

The variations in the accrual of the investment tax credits are shown in Note 13.

(19) Long-term debt - other payables and current liabilities - other nontrade payables

The "Long-Term Debt - Other Payables" caption, which is nonfinancial, included €2,983.53 million as of December 31, 2001, relating to accounts payable by certain Group companies to their other stockholders for the acquisition of UMTS licenses. These accounts payable and the interest accrued thereon were capitalized in 2002 (see Note 12).

The detail of the balances of the "Current Liabilities - Other Nontrade Payables" caption in the consolidated balance sheets as of December 31, 2002 and 2001, is as follows:

Millions of Euros

	Balance at 12/31/02	Balance at 12/31/01
Accrued expenses payable	101.75	767.08
Group company dividends payable	54.09	68.48
Exchange of telephone service with other operators	78.97	44.31
Guarantees and deposits	159.25	55.57
Compensation payable	322.79	294.57
Other nonfinancial nontrade payables	524.00	752.77
Total	**1,240.85**	**1,982.78**

(20) Revenues and expenses

Sales and services

The detail, by business line, of net sales and services is as follows:

Millions of Euros

	12/31/02	12/31/01
Wireline telephony business in Spain	10,272.11	10,220.37
Atento business	571.09	643.87
Telefónica Internacional business	6,954.14	10,137.37
Terra Networks business	599.95	689.96
Móviles business	9,449.34	8,729.95
Data business	1,731.41	1,849.69
Admira business	1,076.16	1,403.07
Directorios business	550.46	619.54
Instrumentality companies and other	650.40	826.33
Group revenues before intercompany sales	**31,855.06**	**35,120.15**
Intercompany sales	(3,443.76)	(4,067.55)
Total revenues from Group operations	**28,411.30**	**31,052.60**

Personnel expenses

The detail of the personnel expenses is as follows:

Millions of Euros

	12/31/02	12/31/01
Compensation	3,561.57	3,958.37
Provisions to the pension allowance and other commitments to employees	121.26	103.32
Accrual for the cost of the loyalty-building programs tied to share market price	16.97	14.29
Employee welfare expenses and other	1,093.97	1,314.28
Total	**4,793.77**	**5,390.26**

Inclusion in the general social security system
Since January 1, 1992, Telefónica de España and its employees, who were formerly covered by a company employee welfare system, have been contributing to the general social security system. As a result of the inclusion of serving employees in the social security system, Telefónica de España must make additional contributions to the social security system until the year 2016, based on the serving employees' effective contribution bases applicable at any time. These contributions consist of the payment of 2.2% of the base salary, and the related amount is recorded under the "Personnel Expenses – Employee Welfare Expenses and Other" caption. g27.23 million were recorded in this connection in 2002 (g26.09 million in 2001).

Supplementary pension plan for employees
Various Telefónica Group companies have arranged a defined-contribution pension plan pursuant to Pension Plans and Funds Law 8/1987. Under this plan, contributions of between 6.87% and 4.50% of the participating employees' regulatory base salary (based on each employee's respective hire date and the company in question) are made to the plan. The obligatory contribution of the participant is generally a minimum of 2.2% of the employee's regulatory base salary. The system used is an individual and financial capitalization system.

As of December 31, 2002, 65,817 Group employees were covered by the pension plans managed by the subsidiary Fonditel Entidad Gestora de Fondos de Pensiones, S.A. The contributions made by the various companies in 2002 amounted to g97.68 million.

Number of employees

	12/31/02		12/31/01	
	Average	Year-End	Average	Year-End
Telefónica, S.A.	769	799	680	727
Telefónica de España Group	42,356	42,162	42,627	42,425
Telefónica Móviles Group	14,153	13,694	13,857	14,677
Telefónica Internacional Group	28,715	25,673	32,983	30,425
Telefónica Data Group	4,609	4,331	4,674	4,952
Directorios Group	2,839	2,752	2,774	2,815
Telefónica de Contenidos Group	5,712	5,574	6,623	6,698
Atento Group	49,496	49,432	47,465	49,940
Terra Group	2,762	2,455	3,133	2,907
Katalyx Group	209	197	287	220
Emergia Group	147	136	134	156
Other	5,737	5,640	5,792	5,585
Total	**157,504**	**152,845**	**161,029**	**161,527**

The figures in the foregoing table relate to the consolidated companies

Also, the Group company Telefónica de España has filed various appeals for judicial review against the Government in connection with the monetary claim amounting to approximately g80 million relating healthcare services provided in 1999, 2000 and 2001. The claim for 2002 will be initiated once the accounts of the related entity cooperating with the Spanish National Social Security Institute have been closed.

Compensation systems tied to share market price

Telefónica, S.A. currently has in place two compensation systems tied to the market price of its shares. One of these systems (the TOP Plan) is aimed exclusively at executive personnel of Telefónica, S.A. and of several of its subsidiaries in Spain and abroad, including the executive directors of Telefónica, S.A., while the other (the TIES Program) is aimed at all the personnel of Telefónica, S.A. and its Spanish and foreign subsidiaries. Both systems were approved by the Stockholders' Meeting held on April 7, 2000.

The subsidiaries Telefónica Móviles S.A., Telefónica Publicidad e Información, S.A. and Terra Networks, S.A. have also established their own compensation systems tied to the market price of their respective shares.

Lastly, there is a program of options on Telefónica, S.A. shares targeted at the employees of Endemol (the EN-SOP Program).

Following is a detailed account of each of these two plans:

a) TOP Plan relating to options on Telefónica, S.A. shares targeted at executives of Telefónica Group companies

At its meeting on May 26, 1999, Telefónica, S.A.'s Board of Directors approved a compensation system tied to the market price of Tele fónica, S.A.'s shares (the "TOP Plan"), through the grant of options on the Company's shares. The term of this plan is four years and three months from the launch date (June 28, 1999).

The implementation of the Plan and the exercise and sale of the related stock option rights were approved by the aforementioned Stockholders' Meeting of Telefónica, S.A. on April 7, 2000.

The approval and implementation of this incentive Plan were notified to the Spanish National Securities Market Commission (CNMV) and published in the Complete Prospectus, which was verified and registered in the CNMV's Official Register on June 29, 1999; in the Continued Prospectus, which was verified and registered on June 23, 2000; and in the Specific Prospectus on the compensation systems tied to the market price of Telefónica, S.A. shares in force prior to January 1, 2000, which was verified and registered in the CNMV's Official Register on April 18, 2000. This prospectus included a clear description of the main features of the program and of the procedures for the assignment, exercise and settlement of the options.

Also, the CNMV was notified in due time and form of the assignment of options derived from this compensation system to executive directors, general managers and persons of a similar rank of Telefónica, S.A.

The TOP Plan, which is targeted at approximately 500 beneficiary executives of several Telefónica Group companies, consists of the grant to each beneficiary covered thereby of ten type-A options and ten type-B options on Telefónica, S.A. shares for every Telefónica, S.A. share assigned by each beneficiary to the Plan and which the beneficiaries must keep throughout the term of the Plan. The beneficiaries may exercise the stock option rights from the second year of the term of the Plan onwards at a rate of one-third of the total number of type-A options and one-third of the type-B options in arrears, i.e. in three equal portions in the second, third and fourth year of the Plan; the Company reserves the right to settle the Plan at each of the aforementioned maturity dates by paying the beneficiaries the result of the settlement in the form of shares or in cash. One share equals one option.

At the launch date, the exercise price of the options granted was as follows: for the type-A options, the exercise price was established on the basis of the market price of the shares when the compensation system was introduced (g46.18 per share); whereas the exercise price for the type-B options was set at the same price plus 50% (g69.27 per share). These figures related to the par value of the Telefónica, S.A. shares when the Plan was launched and, accordingly, prior to the three-way share split, consisting of three new shares for every old share, carried out in July 1999. Therefore, following this split and taking into account the antidilution clauses in the Plan, the type-A and type-B option exercise prices were g15.09 and g22.63 as of December 31, 2000, respectively; g14.50 and g21.75 as of December 31, 2001, respectively; and g13.94 and g20.91 as of December 31, 2002, respectively.

Originally 411 Telefónica Group executives were the beneficiaries of the TOP Plan (including four executive directors and nine general managers and persons of a similar rank). Consequently, although initially the TOP Plan was only partially awarded, it was established that if all the executives (approximately 500) targeted by the Plan had availed themselves of it, the total number of shares assigned to the Plan would have been 270,237 and, consequently, the total number of options granted would have been 5,404,740, prior to the aforementioned three-way share split carried out in July 1999.

Clearly, the TOP Plan provided for the possibility of assigning new options at dates subsequent to that on which it was introduced, particularly to cater for the needs which were disclosed as a result of the executive compensation policies and of new executive hirings. This possibility was expressly approved by the Stockholders' Meeting of Telefónica, S.A. in a resolution adopted on June 15, 2001.

In October 2000 and February and April 2001 new options were assigned under the TOP Plan to a further three executive directors and two executives who had joined the Group after the launch of the Plan, or who, as a result of promotion, held positions of responsibility which carry a higher level of option assignments than that at which they joined the Plan.

The new option assignments made in October 2000 and February and April 2001 (which were expressly ratified through a resolution adopted by the Stockholders' Meeting of Telefónica, S.A. on June 15, 2001) did not entail an extension of the TOP Plan, but rather in order to make these assignments, the remaining options that had been held by the Company throughout the term of the Plan were used. Accordingly, the terms and conditions of the options assigned on the aforementioned dates are the same as those of the TOP Plan, except for the exercise price thereof. In the case of the type-A options the exercise price was set at the Telefónica, S.A. share market price when the new assignments were approved by the competent corporate governing body.

Also, on June 15, 2001, the Stockholders' Meeting of Telefónica, S.A. empowered the Board of Directors to make, within the total volume of options under the TOP Plan, additional assignments of options to executive directors and general managers and persons of a similar rank, provided that the maximum number of options to be assigned to each director or senior executive did not exceed 175,000 type-A options or 175,000 type-B options. In no case could the exercise price for the type-A options be lower than the market price of the Company shares when the options were granted, and in no case could the exercise price of the type-B options be lower than that amount increased by a percentage of between 25% and 50%.

On December 31, 2001 (taking into account the fact that by that date the Board of Directors had not exercised the powers granted to it, as mentioned above, by the Stockholders' Meeting on June 15, 2001), there were 453 beneficiaries of the TOP Plan (including five executive directors of Telefónica, S.A. and ten general managers or persons of similar rank), who held a total of 14,966,640 purchase options on Telefónica, S.A. shares.

Subsequently, because, effective January 2, 2002, certain beneficiaries of the TOP Plan who work for subsidiaries of Telefónica Móviles, S.A. were included under the latter's stock option plan known as the MOS Program, which was set up after the TOP Plan, which led to their automatic exclusion from the latter Plan because of the total incompatibility of the two Plans, the number of beneficiaries of the

TOP Plan and the number of options assigned thereunder was significantly reduced. Therefore, as of that date (January 2, 2002) there were 335 beneficiaries of the TOP Plan (including four executive directors of Telefónica, S.A. and ten general managers or persons of similar rank), who held a total of 12,158,820 purchase options on Telefónica, S.A. shares.

In January 2002 the Board of Directors, exercising the powers granted to it by the aforementioned Stockholders' Meeting on June 15, 2001, resolved to assign options under the TOP Plan to several Telefónica Group executives, for which purpose unassigned options included within the total volume of options initially approved for the Plan were used. The beneficiaries of this assignment included three general managers or persons of similar rank.

At year-end 2002, there were 324 beneficiaries (participants) of the TOP Plan, who held a total of 13,066,516 purchase options on Telefónica, S.A. shares. These TOP Plan beneficiaries (participants) included 4 executive directors of Telefónica, S.A. and 13 general managers and persons of similar rank.

In order to cover the risks and economic obligations derived from the TOP Plan, the Group arranged hedging contracts with BBV and Argentaria, at a maximum total cost for the Telefónica Group of g72.12 million. g13.70 million of this cost have not yet been taken to income (see Note 9).

b) Telefónica, S.A. stock option plan targeted at all the employees of certain Telefónica Group companies ("TIES Program")

On February 23, 2000, the Board of Directors of Telefónica, S.A. approved the establishment of a new compensation system tied to the market price of the Company's shares, with the grant of options on Company shares, known as the TIES Program. This Program is aimed at all the employees of Telefónica, S.A. and its Spanish and foreign subsidiaries who meet the requirements established in the rules governing the Program and who are not participating in any other similar stock or stock option plan.

The aim of the TIES Program is identical to those achieved by other similar programs implemented in the past by Telefónica, S.A. or its subsidiaries and is broadly similar to programs which have been introduced in several European countries and in the U.S. Its main purpose is to introduce a system of global incentives and to reward the past and future services of all the employees of Telefónica, S.A. and its subsidiaries in the coming years. The TIES Program will basically motivate all its beneficiaries by giving them access to Telefónica, S.A. shares under highly favorable terms and conditions.

In order to achieve the purposes of the Program, on April 7, 2000, the Stockholders' meeting of Telefónica, S.A. approved two capital increases with disapplication of preemptive subscription rights, for a par value of g1,197,880 and g31,504,244, respectively, through the issuance of 1,197,880 and 31,504,244 new shares, respectively, of g1 par value each, with additional paid-in capital of 400% of the par value.

Telefónica, S.A. duly registered separate prospectuses for the aforementioned capital increases, which were verified by the Spanish National Securities Market Commission (CNMV) on November 16 2000 and February 16, 2001, respectively. It was clearly explained therein which options could be exercised in each tranche, and the procedures for exercising and settling these options.

The main features of the TIES Program are as follows:

1. Number of shares offered for initial acquisition by the beneficiaries: 1,197,880.

2. Issue price: g5.

3. Maximum no. of shares under option assigned to beneficiaries 31,504,244. This figure, which is the maximum amount necessary to cover the total rights carried by the shares initially assigned also includes a reserve for new beneficiaries of the Program equal to 4.5% of the initial beneficiaries.

4. Method of assignment of shares under option: depends on the appreciation of Telefónica, S.A. shares with respect to an initial reference value to be set by the Board of Directors and on the number of shares of Telefónica, S.A. initially acquired. The initial reference value was set at g20.5 per share.

5. Exercise price: g5.

At its meeting on June 28, 2000, the Board of Directors of Telefónica S.A. resolved to commence implementation of the TIES Program (the features and general terms of which had been established on February 23, 2000, by the Board of Directors' Meeting that approved the creation of the Program), and established the requirements to be met by the employees of the subsidiaries of Telefónica, S.A. in order to become beneficiaries of the TIES Program.

Subsequently, on November 29, 2000, the Board of Directors of Telefónica, S.A. adapted to the date on which the Program was ultimately launched the conditions and requirements to be met by the employees of the companies participating in the Program in order to become beneficiaries of the Program and the reference value initially set.

On February 14, 2001, the notarial deed of formalization and execution of the first capital increase at Telefónica indicated above was executed. The par value of the capital was increased by g1,123,072 through the issuance of an equal number of common shares with additional paid-in capital of g4 per share. The new shares were fully subscribed and paid, through a monetary contribution, by the beneficiaries of the TIES Program.

On February 20, 2001, the notarial deed of formalization and execution of the second capital increase to cater for the TIES Program was executed. The par value of the capital was increased by g31,504,244 through the issuance of an equal number of common shares with additional paid-in capital of g4 per share. The new shares were fully subscribed and paid, through a monetary contribution, by BBVA (50%) and La Caixa (50%).

On December 31, 2002, 75,842 persons were participating in the TIES program, who held a total of 29,956,042 purchase options on Telefónica, S.A. shares.

c) Telefónica Móviles, S.A. stock option plan ("MOS Program")

On October 26, 2000, the Special Stockholders' Meeting of Telefónica Móviles, S.A. authorized the establishment of a corporate stock option plan for the executives and employees of Telefónica Móviles, S.A. and its subsidiaries and, in order to facilitate coverage of the Company's obligations to the beneficiaries of the plan, resolved to increase the capital stock of Telefónica Móviles, S.A. by g11,400,000 through the issuance of 22,800,000 shares of g0.50 par value each.

Subsequently, on June 1, 2001, the Stockholders' Meeting of Telefónica Móviles, S.A. approved the introduction of certain modifications and clarifications of the stock option plan with a view to making it more attractive and a more efficient mechanism for the motivation and loyalty-building of its beneficiaries.

Lastly, on September 21, 2001, the Board of Directors of Telefónica Móviles S.A. resolved to develop and establish, in conformity with the aforementioned resolutions of the Stockholders' Meetings on October 26, 2000 and June 1, 2001, the terms and conditions of the stock option plan. The main features of this plan are as follows:

1. The plan is open to all the executive directors, executives (including general managers or similar) and employees who on December 1, 2001, were working for companies in which Telefónica Móviles directly or indirectly, during the term of the plan (i) has a holding with voting rights of over 50%, or (ii) has the right to appoint over 50% of the members of the Board of Directors.

   Without prejudice to the above, the MOS Program envisages the possibility of awarding new options at dates subsequent to its initial implementation.

2. There are three types of option:

   – Type-A options, with an exercise price of g11.

   – Type-B options, with an exercise price of g16.5.

   – Type-C options, with an exercise price of g7.235.

   Each beneficiary of the Program will receive an equal number of type-A and type-B options and a number of type-C options equal to the sum of the type-A and type-B options received.

3. The executive directors and executives who are beneficiaries of the MOS Program must place a deposit on one share of Telefónica Móviles for every 20 options assigned to them.

4. Each option, regardless of type, will entitle its holder to receive one share of Telefónica Móviles, S.A.

5. The options may be exercised at a rate of one-third each year from the day after the day on which two, three and four years have elapsed since the date on which the options were granted (January 2, 2002).

6. At the exercise date, the options may be settled, at the beneficiary's request, either (i) through delivery of shares of Telefónica Móviles, S.A., once the beneficiary has paid the option exercise price, or (ii) through cash differences.

The first phase of the plan commenced on January 2, 2002. On June 1, 2002, the second phase of the plan commenced and included the Telefónica Móviles Group companies and new employees who fulfilled the requirements envisaged in the plan. The total number of beneficiaries of the MOS Program is currently 12,379. Of these beneficiaries, one is an executive director of Telefónica Móviles, S.A. and eight are general managers or similar executives.

In order to provide coverage for the MOS Program, on September 21, 2001, the Board of Directors resolved to carry out the capital increase approved by the Stockholders' Meeting on October 26, 2000, through the issuance of 21,445,962 shares of g0.50 par value each, which were subsequently subscribed and paid by BBVA (50%) and La Caixa (50%).

On September 27, 2001, Telefónica Móviles, S.A., on the one hand, and BBVA and La Caixa, on the other, entered into the related share subscription and purchase option contracts under which the two aforementioned financial institutions granted Telefónica Móviles, S.A. a purchase option on each of the shares subscribed in order to enable Telefónica Móviles, S.A. to meet its commitments to the beneficiaries of the MOS Program, as described earlier.

The implementation of this Telefónica Móviles, S.A. stock option plan (the MOS Program) and the capital increase at Telefónica Móviles, S.A. to provide coverage for the Program were notified to the CNMV and published in the Abridged Prospectus, which was verified and registered in the CNMV's Official Register on November 2, 2001

d) Telefónica Publicidad e Información, S.A. stock option plan (TPI)

Telefónica Publicidad e Información, S.A. (TPI) has set up a stock option plan on TPI shares targeted at TPI executives and employees who, provided they meet the preestablished requirements, wish to participate in and be beneficiaries of the plan. A given number of TPI shares must be bought by the executives and employees for their own account on the market and must be held for the whole term of the plan.

The TPI stock option plan consists of granting to each beneficiary thereof 15 options to purchase shares of Telefónica Publicidad e Información, S.A. for every share assigned to the plan. The stock option plan had been partially assigned as of December 31, 2002.

Of the total number of TPI stock options issued, and taking into account that split of TPI's shares on June 19, 2000 (7,212,147 shares representing approximately 2% of the total capital stock), as of December 31, 2002, 4,697,400 options had been assigned.

The beneficiaries may exercise the rights under the plan from the first half of November 2001 at a rate of one-third each year in arrears from the following year (2001, 2002 and 2003), except in the case of one executive hired in April 2001, for whom the exercise periods, like those of the plan currently in force, will be counted from the related option contract date and, accordingly, the first third can be exercised in September 2003.

As is customary in compensation systems of this nature, the stock option plan was made subject to the generally applicable antidilution and other contractual clauses. Accordingly, as indicated above, the plan was modified as a result of the three-way split of the company's shares authorized by the Stockholders' Meeting on April 17, 2000, and carried out in June 2000.

On April 28, 1999, the Stockholders' Meeting of TPI approved a capital increase of €120,202.454, through the issuance of new shares, exclusively to create and provide coverage for a stock option plan for company executives.

All the new shares were subscribed and paid in full through a monetary contribution by Caja de Ahorros y Pensiones de Barcelona (La Caixa), the Agent Bank for the plan, which for this purpose had entered into a contract with TPI under which the former granted the latter an irrevocable purchase option right on the new shares issued (2,404,049 new shares, which were converted into 7,212,147 shares following the aforementioned share split subsequently carried out).

At its meeting on June 22, 1999, the Appointments and Compensation Committee made the first proposal for the assignment of options to executives, which was approved by the Board of Directors at its meeting on July 8, 1999. Subsequently, the Board of Directors, at its meeting on December 22, 1999, assigned or offered new options to executives. From that date, with the same expiration date, the exercise price was set at the market price on the date on which the related resolution was adopted.

On April 17, 2000, the Stockholders' Meeting, in accordance with current legislation, approved the execution, the exercise in the envisaged periods and the sale of the stock option rights under this compensation system, and empowered the Company's Board of Directors to assign, at the proposal of the Appointments and Compensation Committee, the options on shares not yet assigned to the employees and executives who formed or were going to form part of TPI. It empowered the Board of Directors to establish the terms and conditions it deemed fit relating to the exercise of the options and, specifically, to extend the exercise period and increase the purchase price of the shares.

Exercising the powers granted by the aforementioned Stockholders' Meeting, on April 17, June 9 and 29, August 30 and November 13, 2000 and April 26 and June 2, 2001, the Board of Directors assigned new stock options to executives and employees.

Worthy of special mention is the fact that subsequently, on April 26, 2001, the Board of Directors, exercising the powers granted by the Stockholders' Meeting on April 17, 2000, decided to extend the stock option plan to all TPI employees who met the preestablished requirements. The plan was extended in accordance with the periods, terms and conditions of the plan in force, and the exercise price was set at €5.

On June 2, 2001, the Stockholders' Meeting ratified, in the terms in which it was performed, the assignment of options carried out to implement the plan after the Stockholders' Meeting on April 17, 2000, and, specifically, with respect to the persons who have the status of executive director and senior executive, as provided for in Additional Provision Fifteen of the Securities Market Law.

Also, on June 2, 2001, the Stockholders' Meeting resolved to empower Board of Directors to assign, in order to implement and develop the stock option plan in force, at the proposal of the Appointments and Compensation Committee, up to the limit of the total number of options under the plan, additional options to executive directors and senior executives, under the following terms and conditions:

– Number of options to be delivered: a maximum of 450,000 options will be delivered to each executive director or senior executive.

– Option exercise price: the option exercise price will be the lower of the closing market price of the Telefónica Publicidad e Información, S.A. shares on the day on which the options are granted or the weighted average market value of the Telefónica Publicidad e Información, S.A. shares on the 20 calendar days immediately preceding the day on which the options are granted.

– Term: the options will have a term of four years from the date on which they are granted and can be exercised partially at the same rate as that envisaged in the stock option plan in force.

As of December 31, 2002, 828 persons were participating in the plan, one of whom is a director of the company (the Executive Chairman) and six are general managers or similar.

e) Terra Networks, S.A. stock option plan

The Terra Networks, S.A. stock option plan was approved by the Stockholders' Meeting on October 1, 1999, and implemented by Board of Directors' resolutions adopted on October 18, 1999, and December 1, 1999.

The Plan provides, through the exercise of the stock options by their holders, for the ownership by the employees and executives of the Terra Group companies of a portion of the capital of Terra Networks, S.A. up to a maximum of 14,000,000 shares.

On October 5, 1999, Banco Zaragozano, S.A., Caja de Ahorros y Pensiones de Barcelona and Terra Networks, S.A. entered into a contract under which these entities granted to Terra Networks, S.A. an irrevocable purchase option on 14,000,000 issued shares, which may be exercised at any time prior to April 30, 2004, to cover the stock option plan approved.

The approval and implementation of this compensation system were notified to the CNMV and were made public through the complete information memorandum verified and registered in the CNMV Official Register on October 29, 1999, and in the Prospectus presented to the Securities and Exchange Commission (SEC) in the U.S.

On December 1, 1999 and June 8, 2000, the Board of Directors, pursuant to the powers granted to it by the Stockholders' Meeting, implemented the first phase of the plan by granting options to employees of the Terra Group. The main features of these options are as follows:

1. Each of the stock options under the plan entitles the holder to acquire one share of Terra Networks, S.A. at an exercise price of €11.81 per share.

2. Duration of four years and three months, and the options may be exercised at a rate of one-third of those granted each year from the second year onwards.

3. The exercise of the options is conditional upon the beneficiary remaining a Terra Group employee.

In 2001 the Board of Directors implemented the second phase of the Terra Networks, S.A. stock option plan, which was approved by the Stockholders' Meeting on June 8, 2000, and launched pursuant to a resolution adopted by the Board of Directors on December 22, 2000, through the assignment of options to executives and employees who were already beneficiaries of the stock option plan, in addition to the assignment of options to new employees who had joined the Group.

The main features established by the Board of Directors for this assignment were as follows:

1. Each of the stock options under the Plan entitles the holder to acquire one share of Terra Networks, S.A. at an exercise price of €19.78 per share.

2. The duration of the Plan was modified by a resolution adopted by the Stockholders' Meeting on June 8, 2000, and was set at six years with a two-year grace period. The options can be exercised at a rate of one-quarter of those granted each year from the third year through the sixth year.

3. The exercise of the options is conditional upon the beneficiary remaining a Terra Group employee.

4. Options were granted to one executive director and four general managers and persons of a similar category, and this was duly notified to the CNMV on December 29, 2000.

On February 21, 2001, the Board of Directors resolved to modify the resolution adopted on December 22, 2000, in respect of the duration and method of accrual of the stock options. Accordingly, the period for the exercise of the options assigned was set at five years, and the options may be exercised at a rate of one-quarter each year from the end of the first year.

In 2001, at the recommendation of the Appointments and Compensation Committee, the Board of Directors approved, each quarter (specifically at its meetings on May 10, July 25 and November 6) the assignment of options to new company employees, and set the exercise price at the market price of the shares during the related quarter and with the same terms and conditions as regards exercise period and duration as those envisaged for the second phase of the plan.

On June 7, 2001, the Stockholders' Meeting of Terra Networks, S.A. resolved to partially modify the resolution relating to the stock option plan which was ratified and approved by the Stockholders' Meeting on June 8, 2000, as regards the extension of the stock option plan to executives and directors, and extended the option exercise period to ten years from that in which they were granted, stipulating that a portion of the options could be exercised each year during this period. As of December 31, 2001, the Board of Directors had not yet extended the option exercise period.

In 2002, at the recommendation of the Appointments and Compensation Committee, the Board of Directors approved, each quarter (specifically at its meetings on January 30, July 25 and September 26), the assignment of options to new Company employees, and set the exercise price at the market price of the shares during the related quarter and with the same terms and conditions as regards exercise period and duration as those envisaged for the second phase of the plan. In addition, on February 25, 2002, the assignment of further options was approved by the Board of Directors.

In June 2002 it was decided to confine assignments of options to new hires, and that options could be assigned from that date onwards to professional categories 1 and 2.

As of December 31, 2002, options on 8,900,502 shares had been assigned to Group employees, executives and directors, of which 1,870,221 relate to the first phase of the plan and the remainder to the second phase. The average stock option exercise price is €13.82.

As of December 31, 2002, the Company's executives and directors held 1,365,215 stock options under the Terra Networks, S.A. stock option plan, the average exercise price of which is €16.77.

f) Terra Networks, S.A. stock option plan resulting from the acquisition of the stock option plans of Lycos, Inc.

Under the agreements entered into for the acquisition of Lycos, it was agreed to exchange options on the shares of Lycos, Inc. for options on the shares of Terra Networks, S.A.

On June 8, 2000, the Stockholders' Meeting of Terra Networks, S.A. resolved to acquire the stock option plans of Lycos, Inc., provided that the two companies merged.

On October 25, 2000, the Board of Directors of Terra Networks, S.A. approved (i) the exchange of options on Lycos, Inc. shares existing prior to the conclusion of the transaction for options on Terra Networks, S.A. shares; (ii) the transfer to Citibank NA (Agent Bank) of all the options on Lycos, Inc. shares for their early exercise; and (iii) the entering into of a contract between Terra Networks, S.A. and the Agent Bank in connection with the new Terra Networks, S.A. stock option plan.

As a result of the exercise of the options on Lycos, Inc. shares by the Agent Bank, the latter subscribed to 29,088,488 shares of Lycos, Inc. which, pursuant to the resolutions adopted by the Stockholders' Meeting of Lycos Inc. on October 27, 2000, were converted into 29,088,488 shares of Lycos Virginia, Inc. and contributed in the exchange, together with the other shares of Lycos Virginia, Inc. As a result of the exchange of Lycos, Inc. stock options for Terra Networks, S.A. stock options, the employees, executives and directors of Lycos Virginia, Inc. received purchase options on 62,540,249 shares of Terra Networks, S.A. owned by the Agent Bank.

On June 7, 2001, the Stockholders' Meeting of Terra Networks, S.A. resolved to partially modify the resolution relating to the stock option plan, which was ratified and approved by the Stockholders' Meeting on June 8, 2000, as regards the obligations arising from the assumption of the Lycos Virginia, Inc. stock options by Terra Networks, S.A., following the exchange of shares between the latter and Lycos Virginia, Inc., which may be covered with Terra Networks, S.A. shares held by Citibank, NA, as a result of the exchange of Lycos Virginia, Inc. shares, held by Citibank, NA to cover the stock options of the employees and executives of Lycos Virginia, Inc.

As of December 31, 2002, the employees, executives and directors of Lycos had exercised 14,823,990 options, and 27,918,329 options had been committed at an average exercise price of US$ 19.15.

As of December 31, 2002, the directors and executives of Lycos held stock option rights on 9,090,776 options, derived from the Lycos stock option plans set up prior to the acquisition of Lycos by Terra. The average exercise price of the stock options granted to executives and directors derived from the Lycos plan is US$ 17.91.

The directors hold 8,267,026 options on Terra Networks, S.A. shares derived from the Lycos, Inc. plans, the average exercise price of which is US$ 19.49, with the price fluctuating between a minimum of US$ 6.28 and a maximum of US$ 30.41.

g) Telefónica, S.A. stock option plan aimed at executives of Endemol ("EN-SOP Program")

In order to fulfill the commitments assumed by Telefónica, S.A. in the acquisition of the Dutch company Endemol (in mid-2000), and in order to establish a competitive compensation system similar to that in place at other companies in the industry in which Endemol operates, on April 25, 2001, the Standing Committee of the Board of Directors of Telefónica, S.A. approved the establishment of a Telefónica, S.A. stock option plan targeted at the employees of Endemol Entertainment N.V. (Endemol) and its subsidiaries (Endemol Group), known as the EN-SOP Program.

This Program consists of the grant to the beneficiaries (all the Endemol Group's permanent employees on January 1, 2001, who are not participating in another similar stock or stock option plan), effective January 1, 2001, 2002, 2003 and 2004, of a variable number (based on the various wage and functional categories) of purchase options on Telefónica, S.A. shares. The duration of the options will be four years from the grant date, and the options may be exercised at a rate of one-half each year three and four years after the related grant date.

The total number of options to be delivered each year will be determined by dividing g27,500,000 by the annual reference value of the Telefónica, S.A. shares, which will be taken to be the arithmetic mean of the closing prices of the Telefónica, S.A. shares on the Spanish Continuous Market for the last five trading days prior to that on which the Board of Directors of Telefónica, S.A. hold the Meeting calling the Annual Stockholders' Meeting.

The option exercise price will be the related annual reference value, and the exercise terms will be the customary terms in programs of this nature. The beneficiaries must remain uninterruptedly permanent employees of Endemol until the options are exercised, without prejudice to the regulation of cases of early settlement of the options in certain cases in which the employment relationship i interrupted prior to the exercise of the options.

The options may be settled through the acquisition by the benefici ary of the underlying shares or, alternatively, in the form of shares o cash.

In order to cover each annual grant of options, it was provided tha Telefónica: (i) would increase capital by the amount necessary t cater for the delivery of the shares derived from the exercise of th options by the beneficiaries or, alternatively, (ii) would acquire on th market the related purchase options on Telefónica, S.A. shares.

Accordingly, in order to cover the annual grant of options in 2001, o June 15, 2001, the Stockholders' Meeting of Telefónica, S.A. approve a capital increase at Telefónica, S.A. of g1,425,624, through th issuance of an equal number of common shares with additiona paid-in capital of g18.2898 per share, and granted the necessar powers to the Board of Directors to carry out the capital increase with express powers, where appropriate, to not carry it out.

As a result of the significant change in stock market conditions i the second half of 2001, on September 26, 2001, the Board of Direc tors decided not to implement the aforementioned capital increas approved by the Stockholders' Meeting, and decided that, instead o the capital increase, the annual grant of options for 2001 under th EN-SOP Program would be covered through the acquisition on th market of purchase options on Telefónica, S.A. shares.

Under the EN-SOP Program, in 2001 1,281,040 purchase options o Telefónica, S.A. shares were delivered to the employees of the Ende mol Group (with the distribution agreed on by the Appointment and Compensation Committee of the Board of Directors of Telefóni ca, S.A., the governing body responsible for this as established whe the resolution to set up this Program was adopted), at an exercis price of g19.2898 per share (annual reference value). As of Decembe 31, 2001, 976 persons were participating in the Program.

With respect to the application of the EN-SOP Program in 2002, i order to cover the annual grant of options in 2002, on April 12, 200 the Stockholders' Meeting of Telefónica, S.A. approved a capita increase at Telefónica, S.A. of g2,180,809 euros, through the issuanc of an equal number of common shares with additional paid-in capi tal of g11.61 per share, and granted the necessary powers to th Board of Directors to carry out the capital increase, with expres powers, where appropriate, to not carry it out.

As in 2001, on December 18, 2002, the Board of Directors decide not to implement the aforementioned capital increase approved b the Stockholders' Meeting, and decided that, instead of the capita increase, the annual grant of options for 2002 under the EN-SOP Pro gram would be covered, where necessary, with Telefónica, S.A. share previously acquired in the securities market.

Under the EN-SOP Program, in 2002 1,933,504 purchase options o Telefónica, S.A. shares were delivered to the employees of the Ende mol Group at an exercise price of g12.61 per share (annual referenc value). 977 persons are participating in the Program.

Other interest on accounts payable and similar expenses and revenues from other equity investments and loans

The detail of the “Other Interest on Accounts Payable and Similar Expenses” and “Revenues from Other Equity Investments and Loans” captions is as follows:

Millions of Euros

	12/31/02	12/31/01
Debentures, bonds and other marketable debt securities	1,060.64	933.50
Loans and credits	659.66	692.44
Other	63.84	362.08
Total other financial expenses	**1,784.14**	**1,988.02**
Associated companies	31.07	15.38
Other companies	289.30	419.81
Total other financial revenues	**320.37**	**435.19**

Exchange differences

The detail of the exchange gains/losses allocated to the consolidated statements of operations is as follows:

Millions of Euros

	12/31/02	12/31/01
Exchange losses	(2,245.17)	(2,026.88)
Exchange gains	1,612.85	1,244.20
Exchange differences	**(632.32)**	**(782.68)**

Of these total exchange differences, the most significant amount relates to the variation in the debt denominated in foreign currency at the Argentine companies, as a result of the currency devaluation which took place in Argentina. Accordingly, exchange differences were recorded which led to a net negative impact of g528.87 million in 2002 and of g528.76 million in 2001 (see Note 1).

Extraordinary revenues

The detail of the extraordinary revenues is as follows:

Millions of Euros

	12/31/02	12/31/01
Prior years’ revenues	15.66	65.74
Indemnity payments for breach of contract	31.76	63.07
Insurance settlement consortium	0.87	14.04
Corporate restructuring of the wireless business in Brazil	49.10	–
Allocation of deferred revenues to income (Note 13)	–	172.16
Provisions for treasury stock (Note 11)	–	106.87
Other extraordinary revenues earned in the year	158.57	349.12
	255.96	**771.00**

The “Other Extraordinary Revenues” caption includes the extraordinary revenues earned by all the Group companies, the amounts of which taken individually were not material.

Extraordinary expenses and losses

Millions of Euros

	12/31/02	12/31/01
Provision for contingencies	31.29	50.67
Extraordinary provisions for preretirements (Note 14)	395.01	460.97
Write-off of goodwill (Note 5)	2,259.81	249.00
Provisions for treasury stock (Note 11)	288.09	–
Fraud suffered and court claims	4.51	98.56
Fines, penalties and litigation	107.01	27.33
Write-off of start-up expenses (Note 4-c)	56.62	–
UMTS license value adjustments (Note 1)	2,753.90	–
Other extraordinary expenses	838.80	430.48
	6,735.04	**1,317.01**

The “Other Extraordinary Expenses” caption includes extraordinary expenses of a very diverse nature incurred by numerous Telefónica Group companies.

Losses on fixed assets

This caption includes most notably the losses recorded relating to UMTS license value adjustments, amounting to g9,526.19 million (see Note 1).

This caption also includes net amounts of g15.49 million and g62.24 million as of December 31, 2002 and 2001, respectively, recorded as a result of the dismantling of Telefónica de España’s plant for network digitalization (see Note 7).

(21) Directors' compensation and other benefits

The compensation of the directors of Telefónica, S.A. consists of a fixed monthly payment and of attendance fees for attending the Board of Directors advisory committee meetings. Also, the executive directors receive compensation for the executive duties discharged by them.

In 2002 the members of the Board of Directors of Telefónica, S.A. earned g11,907,088.40 (g3,312,042.31 fixed monthly payment; g76,416.29 of attendance fees for attending the Board of Directors advisory committee meetings; g8,405,975.34 of salaries and variable compensation of the executive directors; g69,537.84 of compensation in kind paid to the executive directors, which include life insurance premiums; and g43,116.62 of contributions paid by the Company, as promoter and for executive directors, to pension plans).

The breakdown of the compensation and benefits received by the directors in 2002 is as follows:

a. Board of Directors*:* annual amount of the fixed payment received by each director (in euros):

Position	2002
Chairman	90,151.82
Deputy Chairmen	150,253.03
Directors (1):	
Executive directors	90,151.82
Nominee directors	90,151.82
Independent directors	90,151.82

(1) Two independent executive directors, one of whom left the Board in December 2002, receive an additional annual payment of g60,101.21 each, because their experience and work in relation to Latin America is of special interest to the Company.

b. Standing Committee*:* annual amount of the fixed payment received by each director (in euros):

Position	2002
Chairman	60,101.21
Deputy Chairman	60,101.21
Directors	60,101.21

The directors do not receive any attendance fees for attending meetings of the Board of Directors or of the Standing Committee.

c. Other committees of the Board of Directors*:* total annual amounts for attending meetings of the advisory committees of the Board of Directors, received by all the directors.

Committee	200
Audit and Control 4 directors	Attendance fee per meeting: g858.61 Number of meetings: 8 Total received: g24,041.08
Appointments and Compensation and Best Practice Corporate Governance 4 directors	Attendance fee per meeting: g858.61 Number of meetings: 8 Total received: g26,616.91
Human Resources and Corporate Reputation 4 directors	Attendance fee per meeting: g858.61 Number of meetings: 3 Total received: g10,303.32
Regulation 4 directors	Attendance fee per meeting: g858.61 Number of meetings: 4 Total received: g11,161.93
Service Quality and Commercial Service 4 directors	Attendance fee per meeting: g858.61 Number of meetings: 2 Total received: g4,293.05

d. Executive directors*:* total amounts (in euros) received by the exec-utive directors taken as a whole for the items indicated below:

	200
Salaries	4,096,718.5
Variable compensation	4,309,256.7
Compensation in kind	69,537.8
Contributions to pension plans	43,116.6

The executive directors César Alierta Izuel, Fernando Abril-Martorel Hernández, Antonio J. Alonso Ureba and Antonio Viana-Baptista, in their capacity as directors of the Telefónica Group, are beneficiarie of the compensation plan linked to the share market price of th shares of Telefónica, S.A. targeted at the Telefónica Group's execu-tives (the "TOP Plan") discussed in Note 20; the cost for Telefónica o the aforementioned compensation plan, with respect to the execu-tive directors participating in the plan, amounted to g1.2 million i 2002 and g1.26 million in 2001.

Additional notes:

a) The nonexecutive directors do not receive any compensation i the form of pensions or life insurance, and they do not participat in the compensation plans linked to share market price.

b) In 2002 the Company did not grant any advances, loans or credit to the directors.

(22) Other information

a) Litigation

Telefónica, S.A. and its Group companies are party to numerous lawsuits which are currently in progress in the law courts and the arbitration courts of the various countries in which the Telefónica Group is present. These lawsuits cover substantially all areas of law.

However, Telefónica, S.A. considers it reasonably certain that any adverse outcome of these lawsuits will not materially affect the Group's economic and financial position or solvency. These lawsuits include most notably the following:

1. A court proceeding contesting the resolutions adopted by the Special Stockholders' Meeting of Telefónica, S.A. on February 4, 2000.

   The stockholder Javier Sotos García, who owns 300 shares of the Company, has filed a complaint contesting the resolutions adopted by the Special Stockholders' Meeting on February 4, 2000, based on the purported contravention of the rules regulating the holding of the Meeting and on the purported contravention of the rules for disapplication of preemptive rights of subscription in capital increases.

   The Company is convinced that the outcome of the aforementioned court proceeding will be wholly satisfactory for the Company and, since there has been no court decision in this connection, the complaint filed does not in any way signify holding in abeyance the implementation of the corporate resolutions approved by the Stockholders' Meeting and contested in that court proceeding.

2. A court proceeding contesting certain resolutions adopted by the Annual Stockholders' Meeting of Telefónica, S.A. on June 15, 2001.

   The aforementioned stockholder, Javier Sotos García, has also filed a complaint contesting some of the resolutions adopted by the Company's Annual Stockholders' Meeting on June 15, 2001.

   By filing this new complaint contesting the corporate resolutions, the objective of Javier Sotos García is to have the resolutions adopted by the Stockholders' Meeting in relation to the following items on the Agenda set aside by the Court: item I (approval of the 2000 financial statements and of the conduct of business by the Board of Directors in that year); item X (capital increase for the acquisition of the shares of various Mexican cellphone companies owned by Motorola); and item XII (capital increase to cover the Company's stock option plan for Endemol employees).

   The aforementioned proceeding is based on the purported contravention of the contesting stockholder's right to information and on the purported contravention of the legal rules for disapplication of preemptive rights of subscription in capital increases.

   The Company is convinced that the outcome of the aforementioned court proceeding will also be wholly satisfactory for the Company.

   Also, it should be noted that the complaint filed against the aforementioned resolutions adopted by the Stockholders' Meeting on June 15, 2001, does not in any way signify holding in abeyance the possible implementation of those resolutions.

3. Complaint filed by IDT against Telefónica, S.A., Terra Networks, S.A. and Lycos, Inc.

   International Discount Telecommunications Corporation (IDT) filed a complaint with the State Courts of New Jersey (U.S.) against Telefónica, S.A., Terra Networks, S.A., Terra Networks U.S.A., Inc., and Lycos, Inc., seeking the payment of damages amounting to approximately US$ 6,600 million.

   This complaint is based on the purported breach of the joint venture agreement entered into between IDT and Terra in October 1999, on purported nonperformance of the obligations deriving from the agreement to terminate the aforementioned agreement, on purported fraud and contravention of the legislation regulating the issuance of securities (Federal Securities Exchange Act), and on purported fraudulent concealment of information.

   After the complaint had been filed, IDT modified its complaint by eliminating all express references to a claim for damages of a specific amount, since this contravenes the U.S. legislation applicable to the claim. Accordingly, the lawsuit is for an unspecified amount, without prejudice to the possibility of the damages being specified and quantified in the course of the proceeding.

   In May 2002 the State Courts of New Jersey decided to dismiss counts X and XI of the complaint, relating to the purported breach of the joint venture agreement.

   Recently IDT added a new claim to the "second modified complaint" alleging the liability of Telefónica, as a control person, for the alleged fraud against Terra in its negotiations with IDT, which culminated in the termination agreement. Telefónica has filed objections to this claim, which are being considered by the Court.

   Legal counsel for the defendants consider that the defendants have a sound defense with respect to the complaint filed against them and, accordingly, Telefónica is convinced that the outcome of the aforementioned lawsuit resulting from the complaint filed by IDT will not be unsatisfactory for Telefónica or for Terra and that, if it were, the economic and financial impact on the Telefónica Group should not be material.

4. Notice of arbitration filed by IDT against Telefónica Internacional, S.A.

   International Discount Telecommunications Corporation (IDT) filed a notice of arbitration against Telefónica Internacional, S.A. (Sole-Stockholder Company) at the American Arbitration Association (AAA).

   The notice of arbitration is based on the purported breach of a memorandum of understanding entered into by IDT and Telefónica Internacional on August 11, 1999. IDT is seeking in its statement of claim damages by reason of the breach of not less than

US$ 2,000 million, as well as the performance of the aforementioned memorandum of understanding.

In turn, Telefónica Internacional, S.A. (Sole-Stockholder Company) filed a counterclaim against IDT for damages amounting to US$ 3,500 million.

Telefónica, S.A. is convinced that the outcome of the arbitral proceeding resulting from the notice of arbitration filed will not be unsatisfactory for Telefónica Internacional and that, if it were, the economic and financial impact on the Telefónica Group should not be material.

5. Preliminary proceedings conducted by Central Examining Court nº. 1 of the Audiencia Nacional (National Appellate Court).

Central Examining Court nº. 1 of the National Appellate Court is conducting preliminary proceedings in relation to charges pressed in October 2000 by Juan Francisco Franco Otegui against certain ex-directors of Telefónica, S.A., and against the partner of the Company's audit firm, in relation to certain conduct and corporate resolutions alleged by Mr. Otegui to be acts constituting corporate offenses. To these preliminary proceedings was joined an investigation by the Special Public Prosecutor's Office for Combatting Corruption-Related Financial Crime in relation to the acquisition by Telefónica of the Dutch company Endemol.

6. Sistemas e Instalaciones de Telecomunicación, S.A.U. (Sintel).

As a result of the voluntary bankruptcy proceeding being conducted at Madrid Court of First Instance nº. 42, case number 417/2001, which is the continuation of the petition for Chapter 11-type insolvency filed by the director of Sintel on June 8, 2000, two criminal proceedings have commenced which affect Telefónica, S.A.

Under the bankruptcy order, inter alia, the effects of the bankruptcy were backdated to June 8, 1998. As a result of the backdated effects of the bankruptcy pursuant to the order, the related bodies sent Telefónica a payment demand for g22.87 million, which represents the total amount paid for Sintel, since they consider null and void as a matter of law the involvement of Sintel in the contract dated December 30, 1998, in which a debt of g21.35 million was recognized due to the sale of the shares of Sintel to Mastec Internacional, S.A. and the amounts paid by Sintel, which in the aforementioned contract appeared as a joint and several guarantor of the fulfillment of these payment obligations.

Telefónica filed an ancillary complaint in which it proposes that the effects of the bankruptcy be backdated to a date closer to that of the bankruptcy order, so that the contract dated December 30, 1998, is not affected. The representatives of the employees filed a counterclaim proposing that the effects of the bankruptcy be backdated to the date of the sale of the Sintel shares (April 1996).

The two criminal proceedings which commenced recently are as follows:

Expedited proceeding 273/2001, in relation to which, on September 24, 2002, Telefónica, S.A. and Telefónica de España, S.A. appeared before Central Examining Court nº. 1 filing a civil suit a parties suffering loss, against the directors of Sintel and of Mastec Internacional, S.A. Leave was given for them to appear as parties to the proceeding.

Preliminary proceeding 362/2002, which was commenced or October 23, 2002, by the Central Examining Court for a possible offense of extortion. This proceeding arises from the preceding one, concerns the possible commission of an offense of extortion in the assumption by Sintel of joint and several liability with Mastec for the obligation to pay the related sale price.

b) Commitments

Agreements with Portugal Telecom (Brazil)

On January 23, 2001, Telefónica, S.A. and its subsidiary Telefónica Móviles, S.A., on the one hand, and Portugal Telecom SGPS, S.A. and its subsidiary PT Moveis, SGPS, S.A., on the other, entered into an agreement in order to group together all the wireless telephony businesses in Brazil and, accordingly, they undertook to contribute all their wireless telephony assets in Brazil to a joint venture, which subject to the obtainment of the necessary regulatory authorizations, would be a subsidiary of the two groups, and in which they would each have a 50% ownership interest. Also, under the terms of this agreement, the two parties expressed their interest in increasing their reciprocal ownership interests, subject to compliance with the applicable regulatory and bylaw conditions.

On October 17, 2002, Telefónica Móviles, S.A., on the one hand, and Portugal Telecom SGPS, S.A. and its subsidiary PT Móveis SGPS, S.A. on the other, entered into the definitive agreements (Stockholders Agreement and Subscription Agreement) that implement the aforementioned agreement signed in January 2001. On December 27 2002 (after having obtained the necessary authorizations), the two groups' holdings in their respective Brazilian wireless telephony operators were contributed to a Dutch joint venture, Brasilcel N.V., in accordance with the provisions of the aforementioned Subscription Agreement.

In accordance with the aforementioned definitive agreements Telefónica Móviles, S.A. and the Portugal Telecom Group will have the same voting rights at Brasilcel, N.V. This equality in voting rights will cease to exist if, as a result of capital increases at Brasilcel, N.V., the percentage of ownership of either of the parties fall below 40% during an uninterrupted period of six months. In this event, if the group with the reduced interest were the Portugal Telecom Group, it would be entitled to sell to Telefónica Móviles S.A., which would be obliged to buy (directly or through another company), all of Portugal Telecom's ownership interest in Brasilcel N.V. This right expires on December 31, 2007. The price for the acquisition of the Portugal Telecom Group's holding in Brasilcel N.V. would be calculated on the basis of an independent appraisal (in the terms provided for in the definitive agreements) performed by investment banks, selected using the procedure established in these agreements. Subject to certain conditions, the payment could be made, at Telefónica Móviles' choice, in (i) cash, (ii) Telefónica Móviles S.A. shares and/or Telefónica, S.A. shares, or (iii) a combination of the two. This sale option would be exercisable in the 12 months subsequent to the end of the aforementioned six month period, provided that the Portugal Telecom Group had no increased its ownership interest to 50% of the total capital stock of Brasilcel N.V.

Also, in accordance with the definitive agreements, the Portugal Telecom Group will be entitled to sell to Telefónica Móviles, S.A., which will be obliged to buy, its holding in Brasilcel, N.V. should there be a change in control at Telefónica, S.A., Telefónica Móviles, S.A. or any other subsidiary of the latter that held a direct or indirect ownership interest in Brasilcel N.V. Similarly, Telefónica Móviles, S.A. will be entitled to sell to the Portugal Telecom Group, which will be obliged to buy, its holding in Brasicel, N.V. if there is a change of control at Portugal Telecom SGPS, S.A., PT Móveis SGPS, S.A or any other subsidiary of either company that held a direct or indirect ownership interest in Brasilcel N.V. The price will be determined on the basis of an independent appraisal (in the terms provided for in the definitive agreements) performed by investment banks, selected using the procedure established in these agreements. The related payment could be made, at the choice of the group exercising the sale option, in cash or in shares of the wireless telephony operators contributed by the related party, making up the difference, if any, in cash.

Agreements for the acquisition of Pegaso (Mexico)

In accordance with the agreements entered into by Telefónica Móviles, S.A. on April 26, 2002, with Sprint, Leap Wireless, Qualcomm and other financial investors, the acquisition by Telefónica Móviles, S.A. of 65% of the capital stock of the Mexican company Pegaso Telecomunicaciones, S.A. de C.V. (Pegaso) was definitively concluded on September 10, 2002.

Also, in compliance with the agreements adopted on that date Telefónica Móviles, S.A. and the Burillo Group, which owns 35% of the remaining capital stock of Pegaso, all the shares of Pegaso were contributed to a company formed for this purpose called Telefónica Móviles México, S.A. de C.V. Telefónica Móviles, S.A. also contributed to this new company the companies which it owned in the northern Mexico. After these contributions, Telefónica Móviles, S.A. had a 92% holding in the new company.

Under the agreements entered into, the Burillo Group has certain mechanisms with which it can cease to be a stockholder, instrumented through an option to sell its holding in Telefónica Móviles México, S.A. de C.V. The Burillo Group can exercise its sale option in 2007 or 2008, or, if its holding in the company falls below 50% of its original ownership interest, on the date on which such decrease occurs. If the Burillo Group did not exercise its sale option, Telefónica Móviles could exercise its purchase option on the shares of the company owned by the Burillo Group. In this case, the purchase price for the shares will be determined on the basis of a valuation of the company on the date on which the rights were exercised. The agreements entered into envisage that a portion of the purchase price will be paid in cash, the amount of which will depend upon the Burillo Group's original investment in the company, to which interest will be added and from which any cash distribution received by the Burillo Group will be deducted. The remaining portion of the purchase price, if any, will be paid, at Telefónica Móviles' choice, in cash, in shares of Telefónica Móviles or a combination of the two.

Also, under the shareholders agreement entered into the Burillo Group has certain rights to veto agreements on the conversion of shares from one class to another, declarations of bankruptcy or Chapter 11-type insolvency proceedings, dissolution or liquidation, bylaw amendments which adversely affect the rights of the Burillo Group and mergers or corporate reorganizations which do not afford the Burillo Group the opportunity to maintain a given percentage of ownership.

Guarantees provided for Ipse 2000 (Italy)

The Telefónica Group has provided for the Italian company Ipse 2000 S.p.A. (the awardee of an UMTS license in Italy), in which it owns a holding indirectly through Telefónica Móviles, S.A. and Telefónica DataCorp, S.A., Sole-Stockholder Company, guarantees securing financial transactions, mainly to secure its financing commitments relating to the accounts payable to the Italian State due to the acquisition of the license amounting to g636.36 million.

Telefónica DataCorp. Guarantee provided for Atlanet (Italy)

Telefónica DataCorp, S.A., Sole-Stockholder Company, a subsidiary of Telefónica, S.A., owns 34% of the shares of the Italian company Atlanet S.p.A. The assets of Atlanet S.p.A. include most notably its 12% holding in the capital stock of Ipse 2000, a consortium which holds an UMTS license in Italy.

Atlanet S.p.A. has arranged various credit transactions with Banco di Roma consisting of credit lines amounting to g191.56 million, which are secured by the stockholders of Atlanet S.p.A. in proportion to their ownership interest in this company. Telefónica DataCorp, S.A., Sole-Stockholder Company has guaranteed 34% of this amount (i.e. g65.133 million).

Telefónica Internacional (Puerto Rico)

1. On December 22, 1992, Telefónica International Holding B.V., which owns 14.9% of the shares of the Puerto Rican company Telecomunicaciones Ultramarinas de Puerto Rico (TUPR), entered into a stockholders agreement with the Puerto Rico Telephone Authority (PRTA) to acquire, through a reciprocal purchase-sale option, the shares representing the remaining 85.1% of the capital stock of TUPR.

   On May 21, 1999, Telefónica International Holding B.V. announced its intention to exercise this purchase option; however, the purchase transaction was never carried out.

   On April 4, 2002, PRTA exercised its sale option, and notified Telefónica Internacional Holding B.V. of its decision to sell 85.1% of TUPR for a price, subject to a due diligence review, of US$ 24.9 million.

2. On February 4, 2000, Telefónica Larga Distancia de Puerto Rico (TLD) and ClearCom, L.P. entered into a joint venture agreement to carry on the cellular telephony business in Puerto Rico through a new company (Newcomm). Under this agreement, which was subsequently modified, TLD was granted an option to acquire a 50.1% holding in Newcomm, by converting promissory notes into shares representing 49.9% of Newcomm's capital stock and entering into a share purchase agreement for shares representing the remaining 0.2%.

   In line with the process of reorganization by line of business carried out by the Telefónica Group, TLD and Telefónica Móviles, S.A.

have agreed that the rights which the aforementioned agreement confers on the Telefónica Group will be transferred to Telefónica Móviles, S.A., and the related documents have already been prepared for presentation to the Federal Communications Commission (FCC), so that FCC can approve the transfer of licenses and the acquisition of a controlling interest in the company by Telefónica Móviles, S.A.

Telefónica CTC Chile-Sonda
On September 26, 2002, Telefónica CTC Chile, S.A. granted a shareholder of Sonda S.A., Inversiones Santa Isabel Limitada, a purchase option to be exercised between July 26 and August 5, 2005, on 35% of the capital of the aforementioned company, currently owned by Telefónica CTC Chile; the exercise of this option can be brought forward to between July 26 and July 31, 2003 and 2004. The price will be determined in accordance with the process stipulated in the related contract, and will be paid in cash.

Atento
Within the framework of the strategic agreement entered into on February 11, 2000, by BBVA and Telefónica, on December 4, 2001, the two entities signed an agreement establishing the procedure and conditions for the integration in Atento, a Telefónica Group subsidiary, of the BBVA Group's Spanish and international call center business.

The transaction agreed on consists of: (i) the initial contribution by Telefónica S.A. of all its call center business (now carried on by Atento Holding Inc.) to a newly-formed subsidiary (Atento N.V.); and (ii) the subsequent inclusion of the BBVA Group in the stockholder structure of Atento N.V. through various monetary and nonmonetary contributions of all the shares of the Spanish companies Procesos Operativos, S.A. and Leader Line, S.A. These contributions will entail the transfer to Atento of all the BBVA Group's Spanish and international call center business and the subscription by BBVA of up to 9% of the capital stock of Atento N.V.

The transaction also envisages the signing of various specific agreements for the provision to the BBVA Group by Atento of call center services in Spain and Portugal and in ten Latin American countries, for most of which contracts have already been signed. BBVA's ownership interest in Atento N.V. may be adjusted on the basis of whether these agreements are actually entered into and the volume of business actually contributed by the BBVA Group to Atento.

Atento N.V. was incorporated on May 13, 2002. All Telefónica, S.A.'s call center business was contributed to it on that date. The contributions by the BBVA Group under the terms of the agreement discussed in this section had not yet been made as of that date, although this will foreseeably take place in the first quarter of 2003.

Commitments relating to Vía Digital
1. Telefónica has provided to third parties, including other stockholders of DTS Distribuidora de Televisión Digital, S.A. (Vía Digital), guarantees of the liquidity of the investments made which grant the beneficiaries a sale option and Telefónica a purchase option, which can be exercised if certain conditions are met, including that relating to the statutory limitations of percentage of ownership of the capital stock. The total price of this purchase option would amount to approximately g143 million.

2. The agreements entered into by Sogecable, S.A., Telefónica, S.A and Telefónica de Contenidos, S.A. Sole-Stockholder company fo the merger of Vía Digital into Sogecable are described in Note 23

3. The agreement referred to in the previous point establishes the commitment of Telefónica de Contenidos, S.A., Sole-Stockholde Company to Sogecable, S.A. to offer it or another Telefónica Grou company the possibility of acquiring the rights which DTS Distribuidora de Televisión Digital, S.A. (Vía Digital) currently holds o the Soccer World Cup in Germany in 2006. In this regard, management of Vía Digital plans to start offering the aforementione rights to other operators in the market with a view to obtainin an optimum price for them. In accordance with the accountin principle of prudence in valuation a provision of g19.6 millio was recorded in this connection with a charge to the accompanying consolidated statement of operations.

Commitment of Telefónica de Contenidos with respect to Euroleague Marketing, S.L.
Under a framework contract dated August 24, 2000 (amended o November 17, 2001), regulating the exploitation of economic right (including mainly audiovisual, sponsorship and Internet rights licenses, etc.) on the European basketball competition, th "Euroleague", Telefónica de Contenidos, S.A. (Sole-Stockholder Company), a subsidiary of Telefónica, S.A., has a commitment to pa Euroleague Marketing, S.L., a company in which Telefónica de Contenidos, S.A. (Sole-Stockholder Company) owns a 70% holding, th difference between the revenues obtained by Euroleague Marketing, S.L. from the exploitation of the aforementioned rights and maximum of US$ 25 million for the 2002/2003 season (a maximu of US$ 20 million for the remaining two seasons).

Commitments of Telefónica de Contenidos in relation to Audiovisual Sport
Telefónica de Contenidos, S.A. (Sole-Stockholder Company), a subsidiary of Telefónica, S.A., has provided a guarantee, to secure payment of g74.5 million relating to 40% of the outstanding balance o the syndicated loan, originally amounting to g300.51 million, granted by several financial institutions to Audiovisual Sport, S.L., a 40% owned investee of Gestora de Medios Audiovisuales Fútbol, S.L., tha is a subsidiary of Telefónica de Contenidos, S.A.

Also, it should be noted that the agreements relating to the merge of Vía Digital and Sogecable provide for a commitment to acquir the 40% holding that Telefónica de Contenidos, S.A. Sole-Stockholde company owns in Audiovisual Sport, S.L.

Purchase and sale commitments relating to the shares of Uno e-Bank owned by Terra
Note 23 ("Subsequent Events") details various purchase and sal commitments relating to the shares of Uno e-Bank, S.A. owned b Terra Networks, S.A. included in a contract between the latter an Banco Bilbao Vizcaya Argentaria, S.A. (BBVA) dated January 10, 2003

Other commitments in the form of performance bonds for concessions or licenses
1. Telefónica de España, S.A. (Sole-Stockholder Company), a subsidiary of Telefónica, S.A., has provided counter-guarantees for 4 guarantees provided by Banco Santander Central Hispano and b the insurance company Zurich totaling approximately g100.

million, relating to definitive guarantees provided by Telefónica Cable, S.A. (Sole-Stockholder Company), a subsidiary of Telefónica de España, S.A. (Sole-Stockholder Company), in relation to 43 concession contracts with the Spanish State for the provision of cable telecommunications services in 43 franchise areas.

These guarantees ensure performance by the concession-holder company of the obligations assumed under the concession contracts, in particular in relation to coverage of the services and the timetable for their implementation. The aforementioned guarantees were maintained after the concession deeds were converted into 19 individual B1-type licenses.

Through a Telecommunications Market Commission Resolution dated January 7, 2003, it was decided to propose to the Ministry of Science and Technology that 90% of the amount of the final guarantees provided by Telefónica Cable, S.A. (Sole-Stockholder Company) for the formalization of the aforementioned 43 contracts be reimbursed. The Ministry of Science and Technology has given notification of the commencement of the related cancellation proceeding, which must be completed within three months.

2. Telefónica Móviles, S.A., a subsidiary of Telefónica, S.A., has provided certain financial guarantees to the Spanish State amounting to g1,100 million, in relation to the grant to Telefónica Móviles España, S.A. (Sole-Stockholder Company) of a UMTS services license in Spain. These guarantees ensure fulfillment of the commitments assumed by the company awarded the license in relation to network deployment, job creation, investments, etc.

   As of January 20, 2003, the guarantees amounted to g721 million, since g379 million were released as a result of fulfillment of certain of the objectives set. The release of a further g90 million has been requested, for which the Ministry of Science and Technology has yet to verify that the related commitments have been met.

   Also, Telefónica Móviles España began conversations with the aforementioned Ministry, which have given rise to the commencement of an administrative proceeding, with a view to changing the current systems of guarantees, replacing all the guarantees in force by one or several guarantees, the overall amount of which, per the proposed resolution prepared by the Ministry, would not exceed g203 million. These new guarantees would also secure all the commitments assumed in relation to the UMTS license and, accordingly, the guarantees would have to be provided again should they be totally or partially executed due to failure to fulfill any of the commitments that they are securing. A Ministerial Order to regulate this administrative proceeding is pending approval.

3. In 1999 Telefónica de Argentina, S.A. provided guarantees to the Government of the Republic of Argentina for the fulfillment of obligations assumed by Telefónica Comunicaciones Personales, S.A. arising from the obtainment of its PCS licenses, amounting to US$ 22.5 million individually and to US$ 45 million on a joint and several basis with the other operator, Telecom. These guarantees are still in force, pending verification by the Argentine National Communications Commission of the fulfillment of the obligations secured by these guarantees.

The contingencies arising from the commitments described above were evaluated when the consolidated financial statements as of December 31, 2002, were prepared, and the provisions recorded with respect to the commitments taken as a whole are not representative.

c) Environmental matters

The Telefónica Group, through its investees, and in line with its environmental policy, has been undertaking various activities and projects relating to environmental matters. In 2002 it incurred expenses and made investments for scantly material amounts which were recorded in the consolidated statement of operations and the consolidated balance sheet, respectively.

As regards the current systems implemented by the Group to reduce the environmental impact of its plant, systems were brought into service for, inter alia, reducing emissions into the atmosphere, treating and recycling water, measuring effluents, reducing noise and vibrations, etc. The cost of these items was included in the cost of the plant in which they are located.

As regards possible environmental contingencies, there are sufficient internal control mechanisms which are periodically supervised, either in-house or by prestigious outside firms. No significant contingencies have been disclosed in this connection.

d) Fees paid to auditors

The fees paid in 2002 to the various member firms of the Deloitte & Touche international organization, to which Deloitte & Touche España, S.L., the auditors of the Telefónica Group in 2002, belongs, amounted to g15.92 million.

The detail of the foregoing amount is as follows:

Millions of Euros	
Audit of financial statements	6.94
Other audit services	2.90
Work additional to or other than audit services	6.08
Total	**15.92**

The fees paid to other auditors in 2002 amounted to g12.51 million, the detail being as follows:

Millions of Euros	
Audit of financial statements	1.95
Other audit services	0.42
Work additional to or other than audit services	10.14
Total	**12.51**

These fees include the amounts paid in connection with the fully consolidated Spanish and foreign Telefónica Group companies.

(23) Subsequent events

Capital increase in progress with a charge to reserves

February 2003 saw the first of the Company's two capital increases with a charge to unrestricted reserves, approved by the Stockholders' Meeting on April 12, 2002, and which the Board of Directors resolved to carry out at its Meeting on December 18, 2002.

The capital increase was carried out through the issuance of 97,213,225 new common shares of the Company of g1 par value each, thereby increasing the capital stock by g97,213,225 to g4,957,874.511. These new shares were assigned free of charge to the stockholders in the proportion of one new share for every 50 shares already owned.

The deed of capital increase was executed on February 12, 2003, and registered at the Mercantile Registry on February 18, 2002.

Also, on February 12, 2003, the Standing Committee of the Board of Directors of Telefónica, S.A., making use of the powers granted to it by the Board of Directors on January 29, 2003, resolved to carry out the second capital increase with a charge to unrestricted reserves approved by the Stockholders' Meeting on April 12, 2002, through the issuance of 99,157,490 new common shares of the Company, of the same series and carrying the same rights as the outstanding shares, of g1 par value each, which will be assigned free of charge to the stockholders in the proportion of one new share for every 50 shares already owned.

The period for the assignment free of charge of the shares relating to the second capital increase is scheduled to commence in the second half of March 2003, and the new shares will foreseeably be admitted to official listing in mid-April 2003.

Merger of Vía Digital with Sogecable

On May 8, 2002, Sogecable S.A. and Telefónica S.A. (the latter through its subsidiary Telefónica de Contenidos S.A. –Sole-Stockholder Company)– entered into an agreement relating to the merger of DTS Distribuidora de Televisión Digital, S.A. (Vía Digital) with Sogecable.

The transaction was ratified by the Board of Directors of Telefónica de Contenidos S.A. (Sole-Stockholder Company) and Sogecable S.A. in May 2002, subject to the authorization of the relevant public authorities, which was granted on November 29, 2002, through the adoption by the Council of Ministers of certain resolutions authorizing the merger provided that certain conditions were met.

On January 29, 2003, Sogecable S.A., Telefónica, S.A. and Telefónica de Contenidos S.A. (Sole-Stockholder Company) entered into an agreement whereby they deemed the contract terms established for the merger of Sogecable and Vía Digital to have been fully met. Also, Telefónica de Contenidos S.A. (Sole-Stockholder Company) and Sogecable S.A. agreed on the related detailed action plans and deadlines for the instrumentation of the conditions imposed by the Government in the aforementioned Council of Ministers resolutions. Through these plans, Telefónica de Contenidos S.A. (Sole-Stockholder Company) and Sogecable S.A. accepted the conditions established by the Government; however, they filed appeals for judicial review against certain of the conditions (obligation to distribute channels joint marketing of commercial packages, price caps and prohibitior of strategic alliances).

The terms under which the transaction will be carried out in accor dance with the agreements dated May 8, 2002 and January 29, 2003 are as follows:

- The transaction will be carried out through a capital increase a Sogecable, S.A. targeted at the stockholders of Vía Digital, who will be able to contribute their Vía Digital shares.
- If all the shareholders of Vía Digital subscribe to the capita increase, the percentages of ownership of Sogecable, S.A. afte the capital increase will be 77% in the case of the present stock holders of Sogecable and 23% in the case of the present stock holders of Vía Digital.
- After the exchange has been carried out, the Telefónica Group wil have an ownership interest in the capital stock of Sogecable, S.A equal to that of its two stockholders Prisa and Groupe Canal after the dilution arising from the share exchange, which, if al the capital stock of Vía Digital is exchanged, would represen 16.38% of the capital stock of Sogecable, S.A. With this ownershi interest, Telefónica would not exercise such voting rights carried by the shares received in the exchange as might exceed the afore mentioned percentage.
- Telefónica has stated that its present strategic plans envisage that the aforementioned ownership interest will not be disposed of for at least three years from the date of the exchange.
- The representation of Telefónica, Prisa and Groupe Canal + on the Board of Directors of Sogecable, S.A. will be consistent with thei respective ownership interests, and each of the aforementioned three entities will appoint five directors. The Chairman of the Board of Directors will be chosen from among the five director appointed by Telefónica.
- Prisa and Groupe Canal + will maintain their present sharehold ers' agreement, to which Telefónica will not be a party.
- Each of the three major stockholders will grant a ten-year partic ipating loan of g50 million earning interest at 11%.
- Sogecable, S.A. will offer its shareholders the possibility of partic ipating in a nine-year subordinated debt security issue of g17 million, the subscription of which will be underwritten by Tele fónica, bearing interest at 10.28%. The remuneration for the sub scribers will include the issuance of warrants equal, overall, to 1% of the capital stock of Sogecable, S.A.
- The debt of Vía Digital and of Sogecable, S.A. as of April 30, 2003 must not exceed g425 million and g705 million, respectively.

Strategic alliance between Telefónica, Terra and Bertelsmann

On February 12, 2003, Telefónica and Terra Networks, S.A. entered into a Framework Strategic Alliance Agreement to replace the Strategic Agreement dated May 16, 2000, to which Bertelsmann wa also a party (whereby, in the framework of the acquisition of Lycos by Terra, Telefónica, S.A. undertook to commission from Terra, the portion of the advertising services committed by Bertelsmann that the latter did not commission from Terra, up to a maximum amount of US$ 675 million).

Additionally, on February 12, 2003, Telefónica, Terra, Lycos and Bertelsmann, entered into a preferential interest agreement which will enable them to continue to explore opportunities for the mutual provision of communications, development and content services in the on-line market.

The term of the Framework Strategic Alliance Agreement is six years, ending on December 31, 2008. The agreement is automatically renewable for one-year periods unless it is expressly terminated by the parties.

The main features of this Framework Strategic Alliance Agreement are summarized as follows:

1. Strengthening of the Terra Lycos Group as:

   – The exclusive provider of essential portal elements, including brand image, and aggregator of the broad and narrow band Internet content and services targeted at the residential, SOHO and, when so agreed, SME market segments, for the Telefónica Group Companies' connectivity and ISP services.

   – Preferential provider of audit, consulting, management and maintenance services for the country portals of the Telefónica Group companies.

   – Exclusive provider of Telefónica Group employee on-line training services.

   – Preferential provider of on-line integral marketing services with the Telefónica Group companies.

2. Guaranteed minimum volume of acquisitions of Terra Lycos Group on-line advertising space by Telefónica Group companies.

3. Exclusive acquisition of connectivity and wholesale Internet access services by Terra Lycos Group companies from Telefónica Group companies under the legally permitted most-favored-customer conditions.

4. Outsourcing by Terra Lycos Group companies to Telefónica Group companies of all or part of the services and/or operation of the Internet access elements for the provision of ISP services to its residential, SOHO and, when so agreed, SME customers under the legally permitted most-favored-customer conditions.

5. Exclusive acquisition by Terra Lycos Group companies from Telefónica Group companies of the advanced broad and narrow band network and platform services required to construct the range of services to be offered to residential, SOHO and, when so agreed, SME customers under the legally permitted most-favored-customer conditions.

The Framework Strategic Alliance Agreement guarantees the generation for the Terra Lycos Group of a minimum annual value throughout the term of the Agreement of g78.5 million. This amount is the difference between the revenues arising from the services provided under the aforementioned Framework Strategic Alliance Agreement and the costs and investments directly associated therewith.

Terra Networks, S.A.-BBVA (Uno-e Bank, S.A.)

On May 15, 2002, Terra Networks, S.A. (Terra) and Banco Bilbao Vizcaya Argentaria, S.A. (BBVA) entered into a memorandum of understanding to integrate the consumer finance lines of business of Finanzia Banco de Crédito, S.A. (a subsidiary of BBVA) and Uno-e Bank, S.A. The agreement relating to this integration was subject to a legal, financial and business review, and to the obtainment of the relevant internal and administrative authorizations. When the integration takes place, Terra's ownership interest in Uno-e Bank, S.A. will be 33% and that of the BBVA Group will be 67%.

On that same date (May 15, 2002), BBVA and Terra entered into an agreement in which they established the following liquidity mechanisms (purchase and sale options) relating to the Uno-e Bank, S.A. shares owned by Terra:

– Terra has the right to sell to BBVA, and BBVA is obliged to acquire, Terra's holding in Uno-e Bank, S.A. between May 15, 2004 and May 15, 2006, at the higher of the following prices: (i) the market value as determined by an investment bank; and (ii) the price paid by Terra to acquire its ownership interest (g189.4 million).

– BBVA has the right to acquire from Terra, and Terra is obliged to sell, Terra's holding in Uno-e Bank, S.A. between May 15, 2004 and May 15, 2006, at the higher of the following prices: (i) the market value as determined by an investment bank; and (ii) the price paid by Terra to acquire its ownership interest (g189.4 million), plus annual interest at a rate of 4.70%.

– If a definitive agreement were reached regarding the aforementioned integration of the consumer finance lines of business of Finanzia Banco de Crédito, S.A. and Uno-e Bank, S.A., the liquidity mechanisms would be modified. BBVA would lose its right of purchase and Terra would retain its right of sale, but only at the market value as determined by an investment bank.

On January 10, 2003, Terra and BBVA entered into an agreement to integrate the consumer finance lines of business of Finanzia Banco de Crédito, S.A. and Uno-e Bank, S.A. in terms that were more in keeping with their respective interests and those of Uno-e Bank, S.A. than those provided for in the memorandum of understanding dated May 15, 2002. Accordingly, the memorandum of understanding was rendered null and void, and the definitive agreement was made conditional upon obtainment of the relevant internal and administrative authorizations, which must be secured prior to June 30, 2003, as a condition for the formalization and performance of the integration. After the integration takes place, Terra's ownership interest in Uno-e Bank, S.A. will be 33% and that of the BBVA Group will be 67%.

On that same date (January 10, 2003), BBVA and Terra entered into a liquidity agreement that will replace that dated May 15, 2002, once the aforementioned integration has taken place. This agreement establishes the following liquidity mechanism (sale option) relating to the Uno-e Bank, S.A. shares owned by Terra: Terra has the right to sell to BBVA, and BBVA is obliged to acquire, Terra's holding in Uno-e Bank, S.A. between April 1, 2005 and September 30, 2007, at market value, established as the higher of the two following values: (i) that determined by an investment bank; and (ii) that obtained by multiplying the income after taxes of Uno-e Bank, S.A. by the PER of BBVA, multiplied by the percentage of the ownership interest held by Terra that it is intended to sell as of that date.

Also, the exercise price of the aforementioned option may not be lower than g148.5 million if Uno-e Bank, S.A. does not achieve the net ordinary revenue and pre-tax income targets set for 2005 and 2006.

Acquisition of shares of Antena 3 de Televisión, S.A.

In 1997 and 2000 Telefónica provided guarantees to the entity that is now Banco Santander Central Hispano, S.A. to ensure the liquidity and value of the investments made by it in Antena 3 de Televisión, S.A. To execute these agreements, in 1999 Telefónica Media, S.A. (Sole-Stockholder Company) (now Telefónica de Contenidos, S.A. - Sole-Stockholder Company), a subsidiary of Telefónica, S.A., acquired shares representing 7.1395% of the capital stock of Antena 3 de Televisión, S.A. Additional acquisitions have yet to be formalized and the guarantee on certain of the shares has yet to be executed.

On January 7, 2003, as a result of a change in the legal conditions applicable to the ownership of shares of television concession-holder companies, Telefónica, S.A. and its subsidiary Telefónica de Contenidos, S.A. (Sole-Stockholder Company) exercised vis à vis Banco Santander Central Hispano, S.A. purchase options on 17,365,125 and 2,167,500 shares of Antena 3 de Televisión, S.A., which, taken as a whole, represent 11.719% of the capital stock of Antena 3 de Televisión, S.A. The shares were to be acquired by the Telefónica, S.A. subsidiary Corporación Admira Media, S.A. (Sole-Stockholder Company).

After the related procedural formalities had been carried out, on February 5, 2003, the transfer of the aforementioned shares was formalized, and, accordingly, as of that date, the guarantees provided to Banco Santander Central Hispano, S.A. were fully executed and fulfilled. The resulting percentage of ownership was 59.24%.

Acquisition of Tele Centro Oeste Celular Participaçoes (TCO)

In January 2003 Brasilcel N.V., owned 50% by Telefónica Móviles, S.A and 50% by Portugal Telecom Moveis, S.A., the joint venture createc by these companies to manage and develop their cellular telephony business in Brazil, entered into an agreement to acquire, through the subsidiary Telesp Celular Participaçoes, S.A., from the Brazilian company Fixcel 61.10% of the common shares with voting rights of Tele Centro Oeste Celular Participações, S.A. (TCO) representing 20.37% o the latter's total capital stock. The formalization of this acquisition i subject to the satisfactory conclusion of the due diligence review in progress at present and to the obtainment of the pertinent administrative authorizations.

If this acquisition is concluded, pursuant to current stock marke legislation in Brazil, a tender offer will be launched for the TCO' common shares held by the other stockholders. Subsequently, TCO' shares will be exchanged for preferred shares of Telesp Celular Participações, S.A., which will give the latter company the opportunity to own all the shares of TCO.

Restructuring of the debt of Telefónica Comunicaciones Personales (Argentina)

In January 2003 Telefónica Comunicaciones Personales, S.A., a subsidiary of Telefónica Móviles, S.A. in Argentina, entered into agreements with various Ericsson Group Companies to refinance its deb of US$ 130 million to the Ercisson Group.

Also, Telefónica Comunicaciones Personales refinanced its intercompany debt of US$ 630 million to Telefónica Móviles, S.A.

Telefónica Europe, B.V. bond issue

On February 6, 2003, Telefónica Europe B.V. launched two long-term bond issues underwritten by Telefónica S.A. The first issue, which matures on February 14, 2013, has a face value of g1,500 million anc an annual coupon of 5.125%. The second issue, with a face value o g500 million, matures on February 14, 2033, and has an annua coupon of 5.875%.

(24) Consolidated statements of changes in financial position

APPLICATION OF FUNDS	12/31/02	12/31/01	SOURCE OF FUNDS	12/31/02	12/31/01
Funds applied in operations	–	–	**Funds obtained from operations**	8,719.49	11,615.74
Start-up and debt arrangement expenses	468.96	783.10			
Fixed asset additions			**Stockholder contributions**		
a) Intangible assets	1,106.58	1,650.09	a) Capital increase	–	32.64
b) Property, plant and equipment	2,819.65	6,770.80	b) Additional paid-in capital	–	130.51
c) Long-term investments	2,176.26	2,923.82	c) Minority interests	5,294.95	158.18
Deferred tax assets	92.04	1,582.81			
Deferred tax liabilities	–	655.03	**Deferred revenues**	229.09	–
Dividends	108.63	121.87			
Deferred revenues	–	21.73	**Long-term deferred tax liabilities**	436.61	–
			Long-term debt	1,762.92	8,781.66
Repayment or transfer of long-term debt	6,746.65	6,153.88	**Fixed asset disposals**		
			a) Intangible assets	39.21	90.13
Allowances	863.53	888.73	b) Property, plant and equipment	296.34	401.17
			c) Long-term investments	784.16	1,080.11
			Transfer to short term of long-term loans	403.05	–
Decrease in working capital due to disposal of equity investments	1,060.54	–	**Increase in working capital due to disposal of equity investments**	–	158.90
Decrease in working capital due to inclusion of subsidiaries	–	216.21	**Increase in working capital due to inclusion of subsidiaries**	495.50	–
Variation in working capital due to translation differences	714.95	–	**Variation in working capital due to translation differences**	–	493.70
TOTAL FUNDS APPLIED	**16,158.01**	**21,768.07**	**TOTAL FUNDS OBTAINED**	**18,461.32**	**22,942.74**
FUNDS OBTAINED IN EXCESS OF FUNDS APPLIED (INCREASE IN WORKING CAPITAL)	**2,303.31**	**1,174.67**	**FUNDS APPLIED IN EXCESS OF FUNDS OBTAINED (DECREASE IN WORKING CAPITAL)**		**–**
	18,461.32	**22,942.74**		**18,461.32**	**22,942.74**

Variations in working capital

INCREASE IN WORKING CAPITAL	12/31/02	12/31/01	DECREASE IN WORKING CAPITAL	12/31/02	12/31/01
Due from stockholders for capital calls	–	2.25	Due from stockholders for capital calls	2.25	–
Inventories	–	–	Inventories	304.26	37.41
Accounts receivable	–	–	Accounts receivable	1,974.86	934.35
Accounts payable	3,663.88	5,576.42	Accounts payable	–	–
Short-term investments	1,146.39	–	Short-term investments	–	3,311.28
Cash	–	–	Cash	77.97	143.74
Accrual accounts	–	22.78	Accrual accounts	147.62	–
TOTAL	**4,810.27**	**5,601.45**	**TOTAL**	**2,506.96**	**4,426.78**
VARIATION IN WORKING CAPITAL		**–**	**VARIATION IN WORKING CAPITAL**	**2,303.31**	**1,174.67**
	4,810.27	**5,601.45**		**4,810.27**	**5,601.45**

The reconciliation of the balances of the consolidated statements of operations to the funds obtained from operations is as follows:

Millions of Euros	12/31/02	12/31/01
Income (Loss)	(5,576.80)	2,106.81
Loss attributable to minority interests	(5,795.61)	(271.01
Income of associated companies	527.88	376.49
	(10,844.53)	2,212.29
Add:		
Dividends of companies accounted for by the equity method	58.16	8.52
Depreciation and amortization expense	6,692.42	7,373.98
Provisions for property, plant and equipment	37.88	24.95
Amortization of debt arrangement expenses	43.23	55.43
Amortization of consolidation goodwill	665.43	841.62
Amortization of other deferred charges	240.98	55.42
Write-down of consolidation goodwill	2,259.81	249.00
Investment valuation provisions	117.63	68.85
Exchange differences	(316.72)	313.60
Undepreciated plant dismantled	33.85	62.24
Provisions for inventory adjustment	23.32	9.24
Period provisions	3,281.40	428.36
Provisions to technical reserves of insurance companies	17.24	61.55
Deferred interest	5.10	291.77
Deferred tax liabilities and other	–	1,479.55
Property, plant and equipment and intangible assets	9,597.77	164.91
Financial provision and supplementary pension payments to retired employees	61.62	61.59
Losses on disposal of consolidated companies	209.25	–
Less:		
Gain on disposal of property, plant and equipment and intangible assets	16.28	29.29
Capital subsidies	63.79	80.03
Nonrefundable third-party contributions	–	53.15
Long-term deferred tax assets and liabilities	3,228.65	–
Gain on disposal of consolidated companies	101.78	302.09
Fixed asset allowances used	36.83	668.41
Other allowances used	17.02	1,026.91
Other	–	(12.75
Funds obtained from operations	**8,719.49**	**11,615.74**

(25) Explanation added for translation to English

These consolidated financial statements are presented on the basis of accounting principles generally accepted in Spain. Certain accounting practices applied by the Group that conform with generally accepted accounting principles in Spain may not conform with generally accepted accounting principles in other countries.