



[*the markets*]

7.1 Shareholders and investors

Several articles in the Telefónica's Board of Directors regulations deal with the channels through which the relationships between the Board of Directors and the Company's shareholders (both private shareholders and shareholders who are institutional investors) are organised, in order to ensure the greatest possible degree of transparency of such relations.

Moreover, it is expressly established that the Board of Directors commits to guarantee impartiality in its relations with shareholders.

The Company's actions in this area, based on the maximum standard of transparency, are aimed at distributing all public information produced by the Company and making it accessible to all its shareholders simultaneously and in a non-discriminatory basis, fulfilling their information needs and guaranteeing that the published information complies with the criteria of quality, clarity and veracity. The information is disseminated using a variety of media (official communications to markets, press releases, publications on the Company's Web Page, attendance at forums, staff and group meetings, ordinary and electronic mail, conference calls, Internet webcast, etc...).

Shareholders' Office

In order to foster permanent contact with the Company's shareholders, in 1997 Telefónica created the

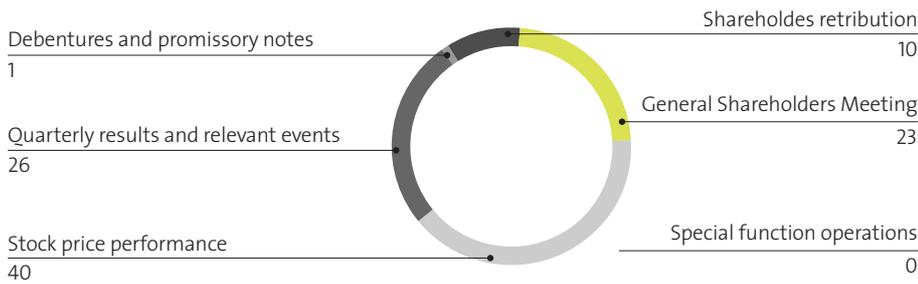
so-called «Servicio de Atención al Accionista» (Shareholder Service Area) with the aim of establishing a transparent and fluid communication with its private shareholders and allowing them to have access to the same information at the same time and in the same way as institutional investors.

The communication channels that Telefónica has established with these private shareholders have gradually evolved and strengthened with time. At present, it is worth highlighting the following aspects relating to the functioning of this Office:

- A Shareholder Freephone Service - 900 111 004 - operative from Monday to Friday from 9 to 19 hours. A total of 123,285 calls were made to this number in 2002, requesting different types of information.
- A Shareholders' Web Page, providing information on economic events and relevant incidents relating to the Company.
- Distribution of a quarterly publication which contains information on quarterly results and economic-financial events which may be relevant for shareholders. Today it is sent to more than 170,000 resident shareholder households.
- Personalised sending of documentation or information whenever requested (international mailing list, documentation relating to the General

Distribution of total consultation made to the «Shareholder Service Area»

(data shown as percentages)



Shareholders’ Meeting, etc.). In 2002, 2,360 personalised information mailings were sent, and 2,389 enquiries were received and handled through the Shareholder Service Website.

Telefónica also participates in specialised Forums in stock exchanges and other markets (Madrid, Barcelona and Valencia) addressed to private investors, where presentations are made on the management and prospects of Telefónica and its Group.

Lastly, and in order to improve the quality of information supplied by the Shareholders’ Office, all the enquiries handled through the call centre, Web page and by ordinary post are processed by computer means. This enables the Company to perform a qualitative and quantitative analysis of the efficiency of these services and, thus, to improve the communication channels and to correct any existing deficiencies. Consequently, in 2002 the distribution of enquiries by Telefónica’s shareholders per area of interest were as follows:

Investor Relations Area

The Investor Relations Department, created at the same time that the Shareholders’ Office, in order to provide support to shareholders and investors, began to operate in 1987, when the Company was admitted to listing on the New York Stock Exchange. The Investor Relations Area reports directly to General Manager of Corporate Finance of Telefónica, what shows the Company’s commitment to offer its investors all the updated relevant information necessary for them to make their investment decisions.

This area’s main task is the design and implementation of the Company’s disclosure programme with respect to national and international financial markets, in order to present and explain the Company’s main strategic, operative, organisational and business actions, thus, actively contributing to the proper pricing of the Company’s securities.

In this way, the Company organises through this area regular informative meetings about the development of the Company and the Group’s these meetings are attended by all Spanish and foreign shareholders and institutional investors, as well as by any executive officer that by reason of the nature of the matters to be presented should attend. In March 2002 Telefónica announced the celebration of the 2nd Investors Conference, which was attended by 275 investors and analysts. The presentations made at this Conference were sent to the different securities markets regulatory bodies and disclosed on the Investor Relations Web Page. There have been a total of 139,499 downloads from these files since then.

In 2002, more than 275 meetings were held with investors and analysts, including direct contacts and roadshows in Europe and in the United States.

Finally, the Investor Relations area performs a periodic analysis of the company’s shareholders and analysts information needs, as well as the analysis of the shareholder and bondholder structure, with the aim of increasing the usefulness of the information that it has been distributed and making Telefónica the leader in the sector in terms of transparency.

Disclosure Policy

The Regulations of the Board of Directors establish that the latter shall perform the following specific functions in relation to the securities markets:

- a. Supervising the periodic public financial information.
- b. Taking the necessary actions and steps in order to ensure the Company's transparency before the financial markets, specifically, the Board must inform these markets of any events, decisions or circumstances which may be relevant for the Company's shares listing.
- c. Taking the necessary actions and steps in order to foster the correct pricing of the Company's shares and, where appropriate, of those of its subsidiaries, avoiding, in particular, insider trading practices.

The Board of Directors expressly commits in its Regulations to adopt the necessary steps to ensure that any biannual, quarterly and any other information to be disclosed to the markets is prepared in accordance with the same principles, standards and professional practices with which the Financial Statements were prepared, and that it is as reliable as the latter. For this purpose, the Audit and Control Committee review such information in its capacity as a specialised Board of Directors sub-Committee.

Moreover, in compliance with the provisions contained in the applicable legislation, the Company provides all the regulatory market bodies where its shares are traded, by issuing the necessary statements, with timely information on any material event

in relation to the Company and its Group. As a result, in 2002 the Company notified 33 Relevant Events and 27 press releases, as well as other less important information that was not classified as relevant.

In addition to this information supplied in real time, and beyond the scope of regulatory requirements, Telefónica is aware of the importance of periodic financial information on results. In this connection, the Investor Relations Area makes a special communication effort by organising quarterly audioconferences to present and analyse results, and which may be followed by telephone or over the Internet (webcast), guaranteeing universal and real-time access to information. Similarly, and with the same structure, specific audioconferences are organised to provide financial markets with information on relevant strategic decisions and operations, after notifying the corresponding regulatory bodies accordingly.

The Company also provides investors and shareholders with information contained in different Informative Prospectuses released either annually or more frequently and registered with the different regulatory bodies of the securities markets.

Moreover, all this information is available to the public on the Web Page of the Company. Special mention must be made of the design and implementation of a specific Web Page for the Investor Relations Area, which has developed into one of the most important tools for the achievement of the transparency objective in the distribution of updated information to the market, guaranteeing simultaneous and non-discriminatory access. At present, the Investor Relations Web Page has 10 main sections which provide access

to all official, financial, operative and strategic information released by the Company to the different regulatory bodies and to the markets in general. (www.telefonica.es / www.telefonica.com / www.telefonica.com/ir).

Lastly, it is important to mention that the Telefónica Group's policy of transparency and information has been granted with international recognition:

- 2nd best European company in terms of transparency (evaluated in early 2002 in a Reuters study and the «Institutional Investor» magazine) in which clarity, depth and speed of response to its investors were assessed.
- Best Investor Relations performance at European telecommunications level (July 2002, Thomson Extel Survey).
- 2nd position for the Telefónica Investor Relations wWeb site among all European companies and 3rd best European company in terms of use of virtual multiconferencing. («Investor Relations Magazine»).
- Best on-line annual report for Spain and Portugal, as well as 2nd best Investor Relations website (MZ Consult, Brazil).
- Telefónica CTC Chile was awarded a prize as one of the best investor relations websites in Latin America («Latin Finance» magazine).

Disclosure Controls and Procedures Regulation

Telefónica, as a Company whose securities are listed not just on the four Spanish Securities Mar-

kets but also on the stock markets in London, Paris, Frankfurt, Tokyo, New York, Buenos Aires, Lima and Sao Paulo and included on the Stock Exchange Automated Quotation System (SEAQ International), always bears in mind its commitment to each of these markets regarding compliance with their respective rules governing securities markets; one of its main duties is to comply with their disclosure obligations. And, despite the priority given to the regulatory body in its market of origin - the CNMV - and to Spanish legislation, the Company's internal regulation require compliance with the standards of those markets in which it trades.

However, in addition to its legal obligations, Telefónica has assumed a commitment to transparency with its shareholders, investors and with the market in general, and aims to place the Company at the forefront in terms of market transparency. Accordingly, the new legal requirements affecting Telefónica pursuant to both, current Spanish legislation and certain foreign regulations, as well as the recent developments in corporate governance issues, recommend the adoption of internal rules relating to disclosure to markets; as of the date of this Report, these rules have been granted with the favourable report of the Audit and Control Committee, and the Nominating, Compensation and Corporate Governance Committee, and they will be subject to the approval of the Board of Directors.

These rules govern the basic principles of the functioning of the processes and control systems for communicating information, through which the Company aims to guarantee that the relevant

corporate information is known by its senior executives and management and to establish the necessary mechanisms for performing regular assessments of the efficiency of these processes and systems.

7.2 Organisation of the General Shareholders' Meeting

In accordance with the provisions established in its Regulations, the Board of Directors must promote the informed participation of shareholders at the General Shareholders' Meetings and adopt any measures it deems appropriate to ensure that General Shareholders' Meeting effectively exercises the functions within the scope of its jurisdiction, pursuant to the provisions established in the Law and Articles of Association.

In order to provide the greatest transparency, the Company immediately informs all markets of any decision of the Board of Directors to call the General Shareholders' Meeting, including any information relating to points to be included on the Meeting agenda.

Appart from complying with the Spanish legal provisions governing the announcement of the call, and provided that Telefónica has shareholders in other jurisdictions, the notice of this call is published, in accordance with applicable provisions, in each of the following countries: Brazil, Peru, Argentina or Japan. As required by Spanish legislation, the official call notice must be published in one high circulation newspaper in the province. It must also be published in various national newspapers and normally also in a num-

ber of high circulation newspapers in Europe, in order to guarantee greater diffusion.

According to the provisions established in the Spanish mercantile legislation, all documentation relating to the points on the agenda must be made available to the shareholders at the Company's headquarters as from the moment of official publication of the call notice; shareholders must also be able to request that this information be sent to them free of charge. The Shareholders' Office collaborates in this task by providing information to shareholders through its call centre, Internet and mailing of documentation by ordinary post. For this purpose, the Company provides on call notices and help cards, the Shareholders' Office freephone number where shareholders can call to request information or documentation.

The Company also provides its shareholders with all documentation in the relevant language, either Spanish, English or Portuguese, where necessary in each one of the countries, in order to enable shareholders to reach a founded opinion on the proposals before participating in the Shareholders' Meeting or delegating their vote.

Hence, in terms of the General Shareholders' Meeting held in 2002, the Shareholders' Office handled:

- 20.000 calls on the Shareholder Telephone Help Line.
- 130 mailings of information on the General Shareholders' Meeting.

- 54.904 authorisations to delegate votes for representation at the General Shareholders' Meeting.

7.3 Internal Code of Conduct for Securities Markets Issues

Regarding the adoption of codes of conduct to avoid insider trading and similar irregularities, as mentioned before, the Company's Board of Directors' meeting of October 30th, 2002 approved a new Code of Conduct for Securities Markets Issues.

This regulation is meant to be addressed to all persons in contact with privileged information, including senior directors and members of the Board of Directors, as well as employees who, by virtue of their position, might have regular access to this type of information.

These Regulation do not only contain a general provision prohibiting operations with the Company's securities when in possession of privileged information. It goes further by establishing broad time restrictions. At times when there is objectively privileged information within the Company, such as in the month prior to the presentations of results or the month prior to the preparation of the financial statements by the Company's Board of Directors. Moreover, the Regulations impose the obligation to maintain acquired securities for a minimum period of six months in order to prevent speculation with the Company's securities.

The Regulation also establishes in detail the principles to be followed in conflict-of-interest situa-

tions, establishing the obligation to disclose such situations and any modifications which might arise from such circumstances.

Lastly, and in accordance with the provisions contained in the new Spanish Financial Law, the Internal Code of Conduct regulates the treatment of confidential information, and determines a series of obligations for individuals involved in these types of operations.

In addition to all these measures, the Company has launched a regulatory «Compliance Programme», by means of which it structures the technical and human means required to strengthen compliance with these new Regulation. With this purpose in mind, a Regulatory Compliance Committee has been set up. This Committee is formed by five of the Company's General Managers and is responsible for safeguarding the proper development of the programme. In addition to this Committee, a Regulatory Compliance Unit has also been established, and is responsible for ensuring the effective execution of the obligations contained in this Regulation.

7.4 The Company External Auditors

The basic responsibilities of the Audit and Control Committee include proposing the appointment of the Accounts Auditor, the terms and conditions of his/her contract, the scope of his/her professional mandate and, where appropriate, the rescission or extension of the appointment. In turn, it must act as a communication channel between the Board of Directors and the Accounts Auditor, evaluate the results of each audit and the responses to the

management team to its recommendations, and mediate and arbitrate in the event of discrepancies between management and the auditor in connection with principles and criteria applicable in preparing the financial statements.

According to the foregoing, the Board of Directors has established, through the Audit and Control Committee, a sound and professional relationship with the Company's Account Auditor, strictly respecting his/her independence, in order to comply with the recommendations made in the Olivencia Report.

The Board of Directors must also try to ensure that the financial statements are prepared without reservations on the part of the Auditor. However, if the Board considers that it must maintain its opinion, it shall offer a public explanation of its content and the scope of the discrepancies in question.

Lastly, the Company must disclose in detail the fees paid to the audit firm in both its Notes to the Financial Statements and Information Prospectus verified by the CNMV, specifying the fees received for professional audit services and for other non-audit services.

As regards the information corresponding to the year 2002, the Company will include detailed information on both Telefónica and the Spanish and foreign companies belonging to the Telefónica Group and consolidating by the global integration method.

Telefónica S.A.

Corporate Governance Annual Report 2002

This Report is also available at
Telefonica's Internet websites:
www.telefonica.es (Spanish),
www.telefonica.com (English) and
www.telefonica.com.br (Portuguese)

Shareholders may request copies of this Report
from Telefónica's **Shareholders Services Office**
by calling freephone **900 111 004** (in Spain),
or by electronic mail to: accion.telefonica@telefonica.es
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The information required by law
is also available to shareholders
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