

AUDIT REPORT ON THE ANNUAL ACCOUNTS

"Translation of a report and financial statements originally issued in Spanish. In the event of a discrepancy the Spanish-language version prevails" (See Note 21).

To the Shareholders of
Telefónica, S.A.

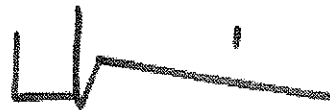
1. We have audited the annual accounts of Telefónica, S.A., which consist of the balance sheet as of December 31, 2005, the profit and loss account and the notes thereto for the year then ended, the preparation of which is the responsibility of the Company's Directors. Our responsibility is to express an opinion on the aforementioned annual accounts taken as a whole, based upon work performed in accordance with generally accepted auditing standards in Spain, which require the examination, through the performance of selective tests, of the evidence supporting the annual accounts and the evaluation of their presentation, of the accounting principles applied and of the estimates made.

2. In compliance with Spanish mercantile law, for comparative purposes, the Company's Directors have included for each of the captions presented in the balance sheet, the profit and loss account and the statement of source and application of funds, in addition to the figures of 2005, those of 2004. Our opinion refers only to the annual accounts for 2005. On March 4, 2005 other auditors issued their audit report on the 2004 annual accounts, in which they expressed an unqualified opinion.

3. In our opinion, the accompanying 2005 annual accounts give a true and fair view, in all material respects, of the net equity and financial position of Telefónica, S.A. at December 31, 2005 and of the results of its operations and of the source and application of funds for the year then ended, and contain the required information necessary for their adequate interpretation and understanding, in conformity with generally accepted accounting principles and criteria in Spain, applied on a basis consistent with those of the preceding year.

4. The accompanying management report for the year ended December 31, 2005 contains such explanations as the Directors consider appropriate concerning the situation of Telefónica, S.A., the evolution of its business and other matters, and is not an integral part of the annual accounts. We have checked that the accounting information included in the report mentioned above agrees with the annual accounts for the year ended December 31, 2005. Our work as auditors is limited to verifying the management report in accordance with the scope mentioned in this paragraph, and does not include the review of information other than that obtained from the Company's accounting records.

ERNST & YOUNG, S.L.



José Miguel Andrés Torrecillas

March 1, 2006

Telefonica

TELEFÓNICA, S.A.
BALANCE SHEET AT DECEMBER 31

ASSETS (millions of euros)	2005	2004
A) FIXED AND OTHER NON CURRENT ASSETS	40,392.56	43,715.40
I. Start-up expenses	0.51	12.19
II. Intangible assets (Note 5)	84.99	40.08
Computer software	153.51	95.90
Intellectual Property	20.38	8.88
Other intangible assets	61.63	1.65
Accumulated amortization	(150.53)	(66.35)
III. Property, plant and equipment (Note 6)	529.63	261.59
Land and buildings	213.61	220.21
Furniture, tools and other items	39.43	23.73
Property, plant and equipment under construction	356.31	79.88
Accumulated depreciation and provisions	(79.72)	(62.23)
IV. Long-term investments (Note 7)	39,777.43	43,401.54
Investments in Group companies	23,127.69	22,415.48
Investments in associated companies	1,098.16	1,479.16
Other investments	1,847.70	14.42
Loans to Group and associated companies	14,004.66	20,531.41
Other loans	0.59	55.17
Long-term deposits and guarantees given	6.41	35.05
Tax receivables (Note 14.2)	3,255.69	4,343.19
Provisions	(3,563.47)	(5,472.34)
B) DEFERRED CHARGES (Note 8)	265.04	266.22
C) CURRENT ASSETS	10,277.34	7,515.63
I. Accounts receivable	219.53	109.93
Trade receivables	15.85	7.86
Receivable from Group companies	143.09	71.04
Receivable from associated companies	0.43	0.15
Sundry accounts receivable	7.98	6.73
Employee receivables	0.75	0.78
Tax receivables (Note 14.2)	61.60	27.89
Provision for bad debts	(10.17)	(4.52)
II. Short-term investments	9,651.57	6,447.97
Loans to Group companies and associated companies (Note 7.6)	9,614.15	6,184.36
Short-term investment securities (Note 7.7)	37.42	263.61
III. Short-term treasury stock (Note 9)	348.48	690.18
IV. Cash	22.29	255.72
V. Prepayments and accrued income	35.47	11.83
TOTAL ASSETS	50,934.94	51,497.25

The accompanying Notes 1 to 20 and Appendix I are an integral part of the balance sheet.

Telefonica

TELEFÓNICA, S.A.
BALANCE SHEET AT DECEMBER 31

LIABILITIES (millions of euros)	2005	2004
A) SHAREHOLDERS' EQUITY (Note 9)	10,989.20	14,399.38
I. Capital stock	4,921.13	4,955.89
II. Share premium	1,670.83	5,287.68
III. Revaluation reserves	1,368.89	1,368.89
IV. Reserves	1,273.96	1,485.52
Legal reserve	920.08	789.94
Reserve for treasury stock	348.48	690.18
Other reserves	5.40	5.40
V. Income for the year	1,754.39	1,301.40
B) PROVISIONS FOR LIABILITIES AND CHARGES (Note 16.6)	444.41	139.30
C) LONG-TERM LIABILITIES	23,601.51	20,770.55
I. Debentures, bonds and other marketable debt securities (Note 10)	1,914.65	1,917.52
Non-convertible debentures and bonds	1,828.32	1,824.62
Other marketable debt securities	86.33	92.90
II. Payable to credit institutions (Note 11)	9,864.60	2,950.56
III. Payable to Group and associated companies (Note 12)	11,622.28	15,697.40
IV. Other payables	11.83	13.02
V. Taxes payable (Note 14.2)	43.02	46.92
VI. Unpaid portion of investments in Group and associated companies	145.13	145.13
Group companies	145.13	145.13
D) CURRENT LIABILITIES	15,899.82	16,188.02
I. Debentures, bonds and other marketable debt securities (Note 10)	1,297.21	1,814.65
Non-convertible debentures and bonds	-	799.06
Other marketable debt securities	1,246.87	963.84
Interest on debentures and other securities	50.34	51.75
II. Payable to credit institutions	3,236.71	2,619.35
Loans and other accounts payable (Note 11)	3,130.91	2,607.85
Accrued interest payable	105.80	11.50
III. Payable to Group and associated companies (Note 12)	10,977.97	11,551.42
IV. Trade accounts payable	61.72	53.87
V. Other non-trade payables	326.21	148.73
Taxes payable (Note 14.2)	26.23	17.31
Other non-trade payables (Note 15)	299.98	131.42
TOTAL SHAREHOLDERS' EQUITY AND LIABILITIES	50,934.94	51,497.25

The accompanying Notes 1 to 20 and Appendix I are an integral part of the balance sheet.