



REPORT OF THE BOARD OF DIRECTORS OF TELEFONICA, S.A. RELATING TO THE PROPOSAL FOR A RESOLUTION TO BE SUBMITTED FOR THE APPROVAL OF THE GENERAL SHAREHOLDERS' MEETING ON ISSUING FIXED-INCOME SECURITIES WHICH ARE CONVERTIBLE AND/OR EXCHANGEABLE, WITHOUT EXCLUDING THE PREEMPTIVE RIGHT (POINT VIII ON THE AGENDA OF MEETING)

1. PURPOSE OF THE REPORT

The Agenda of meeting for the Annual General Shareholders' Meeting of "Telefónica, S.A.", called for June 14 and 15, 2001, includes, in Point VIII thereof, a proposal for delegating to the Board of Directors the power to issue fixed-income securities convertible into newly- issued shares of the said Company and/or exchangeable for shares thereof already pre-existing, for the amount of 2 billion Euros or the equivalent value thereof in another currency. For such purpose the present report is made in accordance with that established in Article 292 of Corporation Law.

2. JUSTIFICATION OF THE PROPOSALS

As we know, one of the means of financing for companies is raising outside funds by issuing obligations of various types, such as secured or unsecured obligations or subordinate, convertible, exchangeable, etc. The modality of being convertible and/or exchangeable presents a dual advantage. On the one hand it offers the investor more of an attraction by making it possible for him to join the Company as a shareholder by converting and/or exchangeable his securities against the Company into shares or for shares and, as well, to the extent allowing capitalization for the company given that its own funds do not have to be used to cover such securities. For these reasons companies are accustomed to select and use this type of obligation.

Given that, upon submitting this request for approval, it is unknown at what time the market conditions will be suitable, it is also proposed that the Board of Directors be delegated so that, within a maximum term of five years commencing from the adoption of the resolution by the General Shareholders' Meeting, it may, in the event that the situation of the markets may so make advisable, resolve upon the issuance and the other conditions thereof not set by the General Shareholders' Meeting, and to develop the bases and modalities of the conversion, setting and finalizing the terms not provided for therein, as well as to partially or fully refrain from carrying out the issue. Commencing from the mentioned deadline, by expiration, such delegation shall be deemed to be null and void, and deeming that the Board of Directors is empowered to refrain from executing the resolution in full or in part.



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The present resolution for issuance is to be carried out with the general guarantees of the law with respect to the determination of the conditions, within such bases and modalities as the General Shareholders' Meeting may approve, with the conversion carried out by means of capital increases up to such maximum as the General Shareholders' Meeting may set. In addition, a syndicate or protection association of the holders of securities will proceed to be created, as well as the appointing of an Auditor, all of this in accordance with Article 282, et seq., of the Revised Text of the Corporation Law and the parallel provisions of the Regulations of the Mercantile Register. Finally, the maximum amount of the issuance or issuances will, at all time, be in accordance the limits set in article 282 of the Corporation Law on, that states that "the Company may issue numbered series of bonds or other securities that recognize or create a debt, provided that the total amount of the issuance is not greater than the capital stock paid in plus the reserves that appear in the last approved profit and loss accounts and the adjusted balance sheets, once these have been accepted by the Fiscal Ministry.

A report issued by the Auditor of Accounts in compliance with that provided for in Article 292.2 of the Corporation Law is to be attached as an exhibit.

In addition, and in accordance with Article 292 of the Corporation Law the bases and modalities of the conversion of the present issue as well as the increase in the capital stock in the amount necessary for attending thereto, which are to be submitted for the approval of the Shareholders' Meeting, are being transcribed.

Finally, the Board of Directors will also submit for the approval of the General Shareholders' Meeting a delegation of this power to the Standing Committee and/or in any of the Directors with delegated powers under the terms permitted by the law and in accordance with that established in Article 141 of the Law on Stock Companies.

3. **PROPOSALS FOR RESOLUTIONS SUBMITTED FOR THE APPROVAL OF THE REGULAR GENERAL SHAREHOLDERS' MEETING**

A) To delegate to the Board of Directors, upon previously obtaining such authorizations as may be required and in accordance with the applicable rules, the power to issue, during a maximum period of five years commencing from the adoption of the present resolution, in one or more issues and up to a total maximum amount of 2 billion Euros (2,000,000,000.00 Euros), or the equivalent value thereof in any other currency, a numbered series of obligations which may be exchanged for shares in "Telefónica, S.A." already pre-existing and/or convertible into shares of a new issue of "Telefónica, S.A." , with or without incorporated rights (warrants), whether or not subordinate, in accordance with the bases and modalities and other conditions indicated in the following:

Face Value and Issue Price for the Securities



The securities to be issued shall have a face value not lower than one hundred Euros for each one of them and they shall be issued at the face value, at least, that is, at one hundred percent of the face value thereof, free of expenses for the subscriber, and the disbursement thereof shall take place on the closing date of the public offering period.

Redemption Value

The redemption rate shall be set by the Board of Directors in the exercise of the delegation of powers to which the present resolution refers.

Interest Rate

The Board of Directors shall determine the nominal interest on the securities, the interest accrual periods and the payment of coupons depending on the market conditions.

Conversion and/or Exchange

Such securities as may be issued under the delegation of powers referred to in the present resolution shall be convertible into new shares of "Telefónica, S.A." and/or may be exchanged for outstanding shares thereof, with the Board of Directors to have the power to determine whether they are convertible and/or exchangeable, as well as to determine whether they are necessarily or voluntarily convertible and/or exchangeable and, in the event that they are voluntarily so, at the option of the holder of the securities of the issuer, with such frequency and during such period as may be established in the resolution on the issue.

In the event that the issue is convertible and exchangeable the Board of Directors may establish that the issuer reserves the right to opt, at any time, between the conversion into new shares or the exchange thereof for outstanding shares, establishing the nature of the shares to be delivered at the time of carrying out the conversion or exchange, including the ability to opt for the delivery of a combination of shares of a new issue with shares already pre-existing. In any event the issuer must adhere to equality of treatment as among all of the holders of the fixed-income securities which are converted and/or exchanged on a single date.

Price of Conversion and/or Exchange

The price of conversion and/or exchange shall be determined at the time of each issue. The conversion and/or exchange may be established at a fixed price or at a variable price, as well as with a premium, discount or at the same price quoted at the time of the issue. In the event that the issue is carried out at a fixed conversion and/or exchange price it shall not be able to be lower than the quoted price of the shares at the time of launching the issue. In the event that they issue is carried out at a variable conversion and/or exchange rate it shall be referred to the quote at the time of the conversion and/or exchange. In no case shall the value of the share be able to be lower than its par value. In addition, the valuation of each obligation



or bond may or may not include the interest accrued and not paid at the time of the conversion and/or exchange thereof.

Conversion at the Time of the Redemption of the Securities

At the time of the final redemption of the securities the issuing company may offer the holders thereof the possibility of converting them into new "Telefónica, S.A." shares or of exchanging them for outstanding shares thereof, provided that they are the owners of such securities on the date indicated for the exercise of the option and provided that early redemption has not taken place, as the case may be.

Preemptive Rights in Increases in Capital and in Issues of Convertible Securities

In the event that, prior to the conversion and/or exchange of the securities into shares, capital increases are carried out with the issue of new common or preferred shares, or issues of securities which are convertible and/or exchangeable, the holders of the securities which are convertible and/or exchangeable of the issue or issues in force shall have a preemptive right in the proportion of the par value of the shares which would pertain thereto in the event of carrying out the conversion and/or exchange of the securities at that time at the rate of exchange provided therefor, all of this in accordance with that provided for in Articles 158 and 293 of the Revised Text of the Corporation Law.

Anti-dilution Clause:

If, prior to the conversion and/or exchange of the stock to shares, a capital increase takes place charged against reserves or a capital reduction against losses, the exchange rate for the stock to shares shall be modified in proportion to the amount of the increase or decrease, in such a way that the shareholders and the holders of the convertible and/or exchangeable stock are affected equally.

Preemptive Right for the Securities of the Issue or Issues

Such shareholders as are shareholders, by the date when the issue or issues are resolved and the holders of convertible bonds pertaining to previous issues shall have such rights as, in each case, may be determined by the law in force. The shareholders and holders of convertible bonds may subscribe securities of each issue in the proportion resolved upon by the Board of Directors with respect to such shares and convertible bonds as they may hold on the date of the opening of the subscription period. Upon the end of the open subscription period, if all of the securities of the issue have not been requested, their subscription may proceed during such period as the Board of Directors may set, finally determining the securities issued, and the Board of Directors may resolve as to the closing of the issue and reduce the amount thereof to that finally subscribed, which shall be set forth in a public document recorded in the Mercantile Register setting forth the exact number and numbering, as the case may be, of those issued and not subscribed, for the purposes of the voiding thereof. In the event that applications exist in



excess of the face value issued the Company shall proceed to pro-rate them in accordance with that established in the law in force.

Redemption

The duration of the issue or issues shall not be greater than fifteen years. The issuing company reserves the right to redeem the securities which are the subject matter of each one of the issues in advance at any time, under such terms as may be resolved upon by the Board of Directors thereof in each case. Such redemption shall be carried out with repayment of the securities at the face value plus the interest accrued up to the date of the early redemption.

Syndicate of Holders of the Securities

For each issue, in accordance with the Corporation Law in force and with the Regulations on the Mercantile Register, a Syndicate shall be formed of the holders of the securities, with the appointment by the Board of Directors of the issuer of a Provisional Auditor, both senior and junior, until the holding of the first Meeting of the Syndicate.

Guarantees of the Issue

The issue or issues shall be guaranteed with the universal proprietary liability of the issuer in accordance with the law.

Representation of the Securities

The securities to be issued under this resolution shall be represented by certificates or book entries in accordance with the law in force at each time and, in particular, pursuant to the rules applicable on the secondary market on which they are traded.

Listing and Quoting

By resolution of the Board of Directors of the issuing company may request the listing and quoting of the securities of each issue or issues on the organized securities markets.

B) Pursuant to that provided for in Article 292 of the Revised Text of the Corporation Law, it is resolved to increase the capital stock of the Company up to a maximum of two billion Euros in order to cover, as the case may be, the eventualities of the conversion of securities into shares in the Company by means of the issuance of the number of common shares, of the same class and par value as those which may be outstanding at such time, in such quantity as may be required in order to attend to the applications for conversion. Pursuant to that established in Article 159.4 of the Revised Text of the Corporation Law, no preemptive right shall arise in the capital increase or increases resulting from the conversion of securities into shares in each one of the corresponding issues.



C) The Board of Directors shall have the power, in the fullest possible terms, in the exercise of the present delegation, to carry out the issue or issues of fixed-income securities convertible into shares of a new issue of "Telefónica, S.A." and/or exchangeable for shares of "Telefónica, S.A." already pre-existing for a maximum amount resolved upon, setting, as the case may be, within the present bases and modalities of conversion, those which may remain to be determined, with no limitation whatsoever. In particular, and without the following listing to have an exhaustive character, the Board of Directors shall have the power:

- a) To establish or not to establish the subordination of the issue and the determination of the ranking of the credit in relation to the entirety of the obligations of the Company; to incorporate rights into the securities (warrants), as the case may be; to determine the maximum amount per subscriber, as the case may be, during the open subscription period, if any exists; to set the place for the subscription; and to request the discounting or redemption of the securities.
- b) To determine the issue rate of the securities which, in any event, shall be at the face value, at least, that is, at one hundred percent of the face value thereof.
- c) To redeem the issue or issues in advance.
- d) During such time as may be resolved upon, to extend the term of open subscription for third parties or to reduce the amount of the issue to the amount subscribed by the close of such period.
- e) To issue, up to the maximum resolved, such new shares as may be necessary in order to attend to the conversion of the securities, attributing the corresponding numbering to the new shares issued and adapting, as a result thereof, Article 5 of the Bylaws relating to the capital stock.
- f) To adjust, to clarify, to interpret, to specify and to supplement the resolutions adopted by the General Shareholders' Meeting in such recorded or other documents as may be made in the execution thereof and, in particular, to cure or correct such defects, omissions or errors, whether of substance or of form, as may impede the access of the resolutions and of the results thereof to the Mercantile Register, the official registers of the National Securities Market Commission or any others.
- g) To redraft and to publish, as it may see fit, the offering documents pertaining to the issue.
- h) For the purposes of the applicable rules, to designate such person or persons as, in the name of the Company, are to assume responsibility for the content of the informative offering documents in each one of the issues.



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- i) To modify the exchange rate of the securities for shares in the event that, prior to the conversion or exchange, a capital increase arises with a charge to reserves or a reduction in capital due to losses.

Pursuant to that established in Article 141 of the Corporation Law and in Article 31.1 of the Bylaws, the Board of Directors may delegate the powers referred to in the present resolution to the Standing Committee and/or in any of the Directors with delegated powers thereof in full or in part.

Madrid, April 25, 2001