

REPORT PREPARED BY THE BOARD OF DIRECTORS OF TELEFÓNICA, S.A. IN CONNECTION WITH THE PROPOSED DELEGATION TO THE BOARD OF DIRECTORS OF THE POWER TO ISSUE DEBENTURES, BONDS, NOTES AND OTHER FIXED-INCOME SECURITIES AND HYBRID INSTRUMENTS, INCLUDING PREFERRED SHARES, IN ALL CASES BE THEY SIMPLE, EXCHANGEABLE AND/OR CONVERTIBLE AND/OR GRANTING THE HOLDERS THEREOF A SHARE IN THE EARNINGS OF THE COMPANY, AS WELL AS WARRANTS, WITH THE POWER TO EXCLUDE THE PRE-EMPTIVE RIGHTS OF SHAREHOLDERS, AND ALSO THE AUTHORIZATION TO GUARANTEE ISSUANCES BY COMPANIES OF THE GROUP, TO BE SUBMITTED FOR APPROVAL OF THE SHAREHOLDERS AT THE ORDINARY GENERAL SHAREHOLDERS' MEETING (ITEM VI ON THE AGENDA).

1. PURPOSE OF THE REPORT

The Agenda for the Ordinary General Shareholders' Meeting of Telefónica, S.A., called to be held on June 8 and 9, 2017, includes in item VI thereof a proposal regarding the granting of powers to the Board of Directors, with the express power of substitution in favor of the Executive Commission, to issue debentures, bonds, notes and other similar fixed-income securities or debt instruments (including warrants) or hybrid instruments (including, among others, preferred shares), which may be convertible into and/or exchangeable for shares of the Company, of any of the companies within its Group or of any other company, and/or giving the holders thereof a share in the earnings of the Company including the authorization for the Company to guarantee issuances of such securities by companies within the Group.

2. RATIONALE FOR THE PROPOSAL

Given the current situation of the major securities markets, the Board of Directors of the Company regards it as necessary to have the delegated powers allowed by current legal provisions in order to be able to acquire on the market the funds that may be necessary for appropriate management of the corporate interests. For that reason, the purpose of this delegation is to provide the Company's board with the required instruments and responsiveness required by the current competitive environment, in which

the success of an initiative or a financial transaction frequently depends on the ability to carry out it out quickly, without incurring the delays and costs that inevitably ensue from the call to and holding of a General Shareholders' Meeting.

For such purpose, in accordance with the general rules governing the issuance of debentures and pursuant to the provisions of Sections 285, 297 and 511 of the Companies Act (*Ley de Sociedades de Capital*) and 319 of the Regulations of the Commercial Registry (*Reglamento del Registro Mercantil*), and of article 15^o of the By-Laws which authorize the shareholders at a General Shareholders' Meeting to delegate to the Board of Directors the power to issue fixed-income securities and other similar instruments, on one or more occasions, with a term of five years , the proposed resolution set forth under item VI of the Agenda is submitted to the shareholders at the General Shareholders' Meeting, which proposal also includes the power to deprive of effect, to the extent of the unused amount, the resolution providing for the delegation of powers to issue securities approved by the shareholders at the Meeting held on May 30, 2014.

The proposal provides that the aggregate maximum amount of the issuances to be carried out under the delegation of powers will be 25,000 million euros or the equivalent thereof in another currency. In addition, the proposal contemplates authorizing the Board of Directors so that, in the event that the Board decides to issue debentures, bonds or hybrid instruments, it may issue them as convertible and/or exchangeable, whether obligatory or voluntary or even contingent, and in the event that they are convertible approve the capital increase required to accommodate the conversion. The power to increase the share capital may only be exercised to the extent that the Board, adding the capital increase effected to accommodate the issuance of convertible securities and any other capital increases it may have resolved to effect pursuant to authorizations granted by the shareholders at a General Shareholders' Meeting does not exceed the limit of one-half of the amount of share capital, as prescribed established in Section 297.1.b) of the Companies Act, or 20% of such total amount of share capital if the issuance of the convertible securities excludes the pre-emptive rights of the shareholders, all in accordance with

the authorization granted by the shareholders at a General Shareholders' Meeting that is in effect on the date of the resolution to increase share capital.

The proposal also includes the standards for determining the terms and conditions for conversion into shares and/or exchange of securities into shares, in the event that the Board resolves to use the authorization granted by the shareholders to issue convertible and/or exchangeable securities, but it delegates to the Board of Directors itself the power to specify such terms and conditions for conversion and/or exchange for each particular issuance within the limits and in accordance with the standards set out by the shareholders at the Meeting. Thus, the Board of Directors will decide whether the securities issued are convertible and/or exchangeable; whether mandatory or voluntary, even contingent; and if voluntary, whether the conversion and/or exchange is at the option of the holder or the issuer; and will also determine the rate of conversion and/or exchange of the shares to be issued for the conversion or of those to be used to exchange the securities, which rate may be fixed or variable, with the shares being valued in accordance with any of the procedures set forth in the following paragraphs, at the election of the Board and as the Board deems to be more appropriate. In any event, if the Board decides to issue convertible and/or exchangeable securities in exercise of the authorization requested of the shareholders at the General Shareholders' Meeting, the Board will, upon approving the issuance, issue a report describing the specific terms and conditions of the conversion and/or exchange applicable to such issuance, which will be the subject-matter of the related report prepared by an Independent expert other than the Company's auditor, appointed for such purpose by the Commercial Registry, mentioned in Section 414.2 of the Companies Act.

Specifically, the resolution submitted by the Board for approval of the shareholders at the General Shareholders' Meeting provides that in the event that the convertible and/or exchangeable securities are issued at a fixed conversion and/or exchange rate, the price of the shares to be set by the Board of Directors for purposes of the conversion and/or exchange, subject to the relevant anti-dilution adjustments, may not be less than the arithmetic mean of the closing prices, the weighted average price or

another benchmark price of the shares of the Company on the Spanish Continuous Market during the period to be determined by the Board of Directors, which may not be more than three months or less than one day, prior to (i) the date of the holding of the Board of Directors' meeting at which the Board approves the issuance of the securities in the exercise of the powers delegated hereby, or (ii) specific dates between the announcement of the issue and the date the securities are paid up by subscribers (both inclusive). A premium or discount on such price per share may also be established, but if there is a discount on the price per share, it may not be greater than 25% of the value of the shares used as the benchmark in accordance with the provisions above. In the event of an exchange for shares of another company (whether or not belonging to the Group), the same rules above will apply, to the extent that they are appropriate and with such adjustments, if any, as may be necessary, provided, however, that such rules will refer to the listing price of the shares of such company on the respective market. In this way, the Board believes that it is granted an adequate degree of flexibility to set the value of the shares for purposes of the conversion and/or exchange based on market conditions and other relevant factors to take into account, but always with reference to the market value thereof at the time that the Board approves the issuance of the securities.

On the other hand, in the event that the issuance is carried out at a variable conversion and/or exchange rate, the price of the shares to be set by the Board of Directors for purposes of the conversion and/or exchange will be the arithmetic mean of the closing prices, the weighted average price, or other benchmark price of the shares of the Company on the Spanish Continuous Market during a period to be determined by the Board, which will not be more than three months or less than one day prior to the date of conversion or exchange, with the Board being authorized to set a premium or, if appropriate, a discount on such price per share, which may be different for each conversion or exchange date under each issuance. However, if the Board sets a discount on such price per share, such discount may not be greater than 30% of the listing price of the share during the period prior to the date of conversion and/or exchange of the securities into shares established by the Board itself. Notwithstanding the foregoing, limits on the minimum and/or maximum benchmark price of the

shares for purposes of the conversion and/or exchange thereof may be established upon terms decided by the Board. In the event of an exchange for shares of another company (whether or not belonging to the Group), the same rules above will apply, to the extent that they are appropriate and with such adjustments, if any, as may be necessary, provided, however, that such rules will refer to the listing price of the shares of such company on the respective market. Again, the Board believes that the foregoing grants it adequate maneuverability to set the variable conversion and/or exchange rate based on market circumstances and any other factors that the Board should take into account, and allows it to apply various measures regarding the price of the shares in order to ensure that the issue price of the new shares at the time of conversion does not differ from the market value by more than a reasonable amount.

In both cases, it is provided that, pursuant to Section 415 of the Companies Act, debentures may not be converted into shares if the nominal value of such debentures is less than the value of such shares, and it is also provided that in no event may the value of the shares for purposes of the conversion rate be less than the nominal value thereof. Moreover, it is provided that the Board of Directors is authorized to determine whether or not the valuation of each security for purposes of determining whether or not the conversion and/or exchange rate for shares will include the interest accrued and unpaid at the time of the conversion and/or exchange.

In addition, it is provided that the authorization to issue fixed-income securities includes, in the event that the issuance covers convertible securities, granting the Board of Directors the power to completely or partially exclude the pre-emptive rights of shareholders when necessary to raise funds on the markets or as otherwise required by the corporate interest. The Board of Directors believes that this additional capacity, which is recognized by current legal provisions, will provide it with increased maneuverability and responsiveness. As already stated, the ability to act flexibly and quickly is necessary in the current market environment in order to be able to take advantage of the times when market conditions are most favorable. Therefore, this measure may be necessary if one desires to obtain financial resources on the domestic or international markets or through the use of bookbuilding. Finally, the exclusion of pre-emptive rights

makes it possible to relatively reduce the financial cost of the borrowing and the costs associated with the transaction (including, in particular, the fees of the financial institutions participating in the issuance) as compared to an issuance made with pre-emptive rights, and at the same time reduces the effect of distortion in the trading of the Company's shares during the issuance period.

In any event, it should be noted that the exclusion of pre-emptive rights is a power that the shareholders at the General Shareholders' Meeting delegate to the Board of Directors and that it falls upon the Board, considering the particular circumstances and observing legal requirements, to decide in each case whether or not it is appropriate to exclude such rights. In this regard, if the Board decides to exclude pre-emptive rights in connection with a specific issuance of convertible securities which it may decide to make pursuant to the authorization requested of the shareholders at the General Shareholders' Meeting, it will, upon approving the issuance, issue a report describing the specific reasons of corporate interest that warrant such measure, on which the related independent expert report required under Section 417 of the Companies Act will be issued. Both reports will be made available to the shareholders and reported to the shareholders at the first General Shareholders' Meeting held following adoption of the resolution approving the issuance and will also be immediately posted on the Company's website.

Likewise, in view of the fact that in certain circumstances it may be advisable for fund-raising activities to be carried out by a company within the Group, and given that, in such cases, it is an essential condition for the success of the transaction that the issuance, if any, made by any such Group company be fully supported and guaranteed by the Company, the Board of Directors also requests express authorization of the shareholders at the General Shareholders' Meeting in order for the Company to be allowed to guarantee the obligations of any kind that may arise for the Group companies from the issuances made thereby in order to raise funds for the Telefónica Group, for a period equal to the period of delegation of the power to issue the securities covered by this report.

It is also proposed that the resolutions required by applicable legal provisions be adopted in order for the securities to be issued pursuant to this delegation of powers to be admitted to listing on any Spanish or foreign, official or unofficial, organized or other secondary market.

Finally, the proposal expressly contemplates that the powers of any kind granted to the Board of Directors may be delegated, in turn, by the Board to the Executive Commission.

3. PROPOSED RESOLUTION SUBMITTED FOR APPROVAL OF THE SHAREHOLDERS AT THE ORDINARY GENERAL SHAREHOLDERS' MEETING

The full text of the proposal with respect to this item that is submitted for the approval of the shareholders at the General Shareholders' Meeting is as follows:

To delegate to the Board of Directors, in accordance with the general rules governing the issuance of debentures and pursuant to the provisions of sections 285, 297 and 511 of the Companies Act (Ley de Sociedades de Capital) and 319 of the Regulations of the Commercial Registry, (Reglamento del Registro Mercantil), and article 15 of the By-Laws, the power to issue, on one or more occasions, debentures, bonds, notes and other similar fixed-income securities or debt instruments (including warrants) or hybrid instruments (including, among others, preferred shares), that may be convertible into and/or exchangeable for shares, and/or giving the holders thereof a share in the earnings of the company, and to guarantee the issuance thereof, all in accordance with the following conditions:

- 1. The aforementioned securities may be issued on one or more occasions, at any time, within a maximum term of five years as from the date of approval of this resolution.*
- 2. The securities issued may be debentures, bonds, notes and other fixed-income securities or similar debt instruments, or hybrid instruments in any of the forms permitted by law (including, among others, preferred*

shares), both simple and, in the case of debentures, bonds and hybrid instruments, convertible into shares of the Company and/or exchangeable for shares of the Company, of any of the companies within its Group or of any other company and/or giving the holders thereof a share in the earnings of the Company. This delegation also includes warrants or other similar securities that might give the right to directly or indirectly subscribe or acquire shares, whether newly issued or already outstanding, and which may be paid for by physical delivery or by set-off.

3. *The maximum total amount of the issuance(s) of securities approved under this delegation of powers may not exceed, at any given time, the sum of 25,000 million euros or the equivalent thereof in another currency. In the case of notes, the outstanding balance of any notes issued under such delegation of powers shall be computed for purposes of the aforementioned limit. Also for purposes of the foregoing limit, in the case of warrants, the sum of the premiums and exercise prices of the warrants for each issuance that is approved under this delegation shall be taken into account.*

4. *The delegation shall include the power to establish the different aspects and terms and conditions of each issuance. It shall fall upon the Board of Directors to determine, without limitation and for each issuance: (i) the amount thereof (observing the applicable quantitative limit); (ii) the number of securities and their nominal value; (iii) the law governing the issuance; (iv) place of issue -whether in Spain or abroad-; (v) currency, and if in foreign currency, the equivalent thereof in euros; (vi) the class of securities, whether notes, bonds, debentures or any other security permitted by Law, including subordinated securities; (vii) the issue date or dates; (viii) interest rate; (ix) procedures and dates of coupon payment; (x) whether they are repayable or not (including, if applicable, the possibility of repayment by the issuer) and, if appropriate, the periods and events of repayment) (in whole or in part), whether the*

securities are perpetual or maturing on a specific date and, in the latter case, the due date; (xi) whether the securities are mandatorily or voluntarily convertible and/or exchangeable, including on a contingent basis, and if voluntarily convertible, at the option of the holder of the securities or of the issuer, and if they are exchangeable and not convertible, whether mandatorily or voluntarily and at the option of the holder or of the issuer; (xii) guarantees, type of reimbursement and lots and premiums; (xiii) representation, whether by certificates (registered or bearer) or book entries; (xiv) pre-emptive right, if applicable, and subscription system; (xv) if appropriate, make application for listing on Spanish or foreign, official or unofficial, organized or not, or other secondary markets of the securities issued, complying with the requirements of applicable law in each case; (xvi) if appropriate, anti-dilution mechanisms and conversion price adjustments; (xvii) in general, any other condition of the issuance; (xviii) where applicable, appoint the security-holders' syndicate representative (comisario) or the person or entity that is to represent the holders of the securities and approve the basic rules that are to govern the legal relations between the Company and the syndicate or collective organization mechanism of the holders of the securities issued that may be in place, if appropriate.

The Board of Directors is further empowered, subject to receipt of the required authorizations and consents, to amend the repayment conditions of the securities, their term, interest rate and, in general, any of the conditions of the issuances made in reliance on this authorization.

5. *In the event that convertible and/or exchangeable securities are issued, it is resolved to establish the following criteria for the determination of the basis and terms of the conversion and/or exchange:*
 - a) *securities issued under this resolution may be convertible into new shares of the Company and/or exchangeable for outstanding shares of the Company, of any of the companies of its Group or of any other*

company in accordance with the conversion and/or fixed or variable exchange ratio (whether determined or determinable), with the Board of Directors having the power to decide whether they are convertible and/or exchangeable, as well as to determine whether they are subject to mandatory or voluntary conversion and/or exchange, even on a contingent basis, and if voluntary, at the option of the holder thereof or the issuer, with the frequency and for the maximum period established in the resolution approving the issuance.

b) The conversion and/or exchange ratio shall normally be fixed and, for such purposes, fixed-income securities shall be valued at their nominal value and shares shall be valued at the fixed exchange ratio determined in the Board of Directors' resolution, or at such exchange ratio as is determinable on the date or dates specified in the resolution of the Board, and on the basis of the listing price of the shares of the Company on the date or dates, or period or periods, used as a reference in such resolution. In any case, the price of the shares for purposes of the conversion and/or exchange, subject to the anti-dilution adjustments, may not be less than the arithmetic mean of the closing prices, the weighted average price or another benchmark price of the shares of the Company on the Spanish Continuous Market during the period to be determined by the Board of Directors, which may not be more than three months or less than one day prior to (i) the date of the holding of the Board of Directors' meeting at which the Board approves the issuance of the securities in the exercise of the powers delegated hereby, or (ii) specific dates between the announcement of the issuance and the disbursement of the securities by subscribers (both inclusive). A premium or discount on such price per share may also be established, but if there is a discount on the price per share, it may not be greater than 25% of the value of the shares used as the benchmark in accordance with the provisions above. In the event of an exchange for shares of another company (whether or not belonging to the Group) the same rules will

apply, to the extent that they are appropriate and with such adjustments, if any, as may be necessary, provided, however, that such rules will refer to the listing price of the shares of such company on the respective market.

- c) Notwithstanding the provisions of paragraph b) above, the issuance of securities may be approved with a variable conversion and/or exchange ratio. In this case, the price of the shares for purposes of the conversion and/or exchange will be the arithmetic mean of the closing prices, the weighted average price, or other benchmark price of the shares of the Company on the Spanish Continuous Market during a period to be determined by the Board of Directors, which shall not be more than three months nor less than one day prior to the date of conversion and/or exchange, with a premium or, if appropriate, a discount on such price per share. The premium or discount may be different for each conversion and/or exchange date under each issuance (or under each tranche of an issuance, if any), provided, however, that if a discount on the price per share is set, such discount may not be greater than 30%.*

Notwithstanding the foregoing, limits on the minimum and/or maximum benchmark price of the shares may be established for purposes of the conversion and/or exchange thereof upon terms decided by the Board. In the event of an exchange for shares of another company (whether or not belonging to the Group), the same rules will apply, to the extent that they are appropriate and with such adjustments, if any, as may be necessary, provided, however, that such rules will refer to the listing price of the shares of such company on the respective market.

- d) Pursuant to the provisions of Section 415 of the Companies Act, debentures may not be converted into shares if the nominal value of such debentures is less than the value of such shares. In addition,*

convertible debentures may not be issued in an amount that is less than the nominal value.

- e) *Whenever a conversion and/or exchange is admissible, any fractional shares to be delivered to the holders of securities being converted and/or exchanged shall be rounded downward by default to the immediately lower integer, and each holder shall receive, in cash, the difference that may arise in such instance.*
 - f) *When approving an issuance of convertible and/or exchangeable securities in reliance on the authorization set forth in this resolution, the Board of Directors shall issue a Directors' report elaborating on and specifying, on the basis of the standards described above, the terms and conditions of the conversion that are specifically applicable to the above-mentioned issuance. Such report shall be accompanied by the corresponding report of the independent expert mentioned in Section 414 of the Companies Act.*
6. *In any event, this delegation of powers to issue convertible and/or exchangeable securities shall include:*
- a) *The power to increase share capital by the amount required to accommodate the requests for conversion. Such power may only be exercised to the extent that the Board, adding the capital increase effected to accommodate the issuance of convertible securities and any other capital increases it may have resolved to effect pursuant to authorizations granted by the shareholders at General Shareholders' Meetings, does not exceed the limit of one-half of the amount of the share capital established in Section 297.1 b) of the Companies Act, or 20% of such total amount of share capital if the issuance of the convertible securities excludes the pre-emptive rights of the shareholders, all in accordance with the authorization granted by the shareholders at a General Shareholders' Meeting that is in effect on the date of the resolution to increase share capital and without such*

provisions in any way affecting the application of any anti-dilution adjustments, when such adjustments are appropriate. This authorization to increase capital includes the power to issue and float, on one or more occasions, the shares required to carry out the conversion, as well as the power to amend the article of the By-Laws relating to the amount of share capital.

b) The power to completely or partially exclude the pre-emptive rights of shareholders whenever required to raise funds on domestic and international markets, to use bookbuilding techniques, to facilitate the acquisition by the Company of assets that are appropriate to further the achievement of the object of the company or whenever otherwise warranted for reasons of corporate interest. In the event that the Board decides to exclude the pre-emptive right of the shareholders in connection with a specific issuance of convertible securities that it may decide to effect in reliance on this authorization, it will, upon approving the issuance, formalize a report describing the specific reasons of corporate interest that warrant such measure, which will be the subject of a corresponding report by an independent expert appointed for such purpose by the Commercial Registry, all in accordance with section 417.2 a) and b) of the Companies Act. Both reports shall be made available to the shareholders and reported to the shareholders at the first General Shareholders' Meeting held following adoption of the resolution approving the issuance, and shall also be immediately posted on the Company's website.

c) The power to elaborate on the terms and conditions of the conversion and/or exchange established in section 5 above and, in particular, the power to determine the time of conversion and/or exchange, which may be limited to a pre-established period, the circumstance of whether the securities are subject to mandatory or voluntary conversion and/or exchange, even on a contingent basis, and, if voluntary, at the option of the holder of the securities or the issuer,

the manner in which holders of the securities are to be paid (by means of conversion, exchange, or even a combination of both methods, which may be selected by the issuer at the time of execution) and, in general, all terms and conditions that may be necessary or appropriate for the issuance.

7. *As long as the conversion into and/or exchange for shares of the convertible and/or exchangeable securities issued in exercise of the powers delegated hereby is possible, the holders thereof shall have all the rights afforded them by applicable legal provisions.*
8. *Convertible warrants: The rules set forth in the preceding paragraphs shall apply, mutatis mutandis, in the case of issuance of warrants or other similar securities that may give the right to directly or indirectly subscribe newly-issued or existing shares, with the delegation including the broadest powers and with the same scope as those included in the numbers above, to decide all matters that it deems appropriate with respect to such class of securities.*
9. *Whenever appropriate, the Company shall make application for listing on Spanish or foreign, official or unofficial, organized or not, or other secondary markets of the debentures, bonds and other securities issued pursuant to this delegation of powers, and the Board is authorized to conduct all formalities and take all actions that may be necessary for admission to listing before the appropriate authorities of the various Spanish or foreign securities markets.*

It is expressly stated for the record that if application is subsequently made for delisting the securities issued pursuant to this delegation of powers, such delisting shall be effected in compliance with the same formalities as for the application for listing to the extent applicable, and in such case, the interests of the shareholders or debenture-holders opposing or not voting on the resolution shall be safeguarded in compliance with the requirements set out in the Companies Act and

related provisions, all of the foregoing pursuant to the provisions of the Securities Market Act (Ley del Mercado de Valores) and the provisions in implementation thereof. It is also expressly stated that the Company submits to the rules now existing or that may hereafter be issued regarding the Stock Exchanges, especially regarding trading, maintenance of the listing and de-listing.

10. *The Board of Directors is authorized to guarantee, on behalf of the Company, the issuance of the securities mentioned in section 2 above issued by the Companies belonging to its Group of Companies. This authorization will remain in effect for a period of five years as from the date of this resolution.*
11. *At the successive General Shareholders' Meetings held by the Company, reports shall be made to the shareholders on the use, if any, made to that date of the delegation of powers to which this resolution refers.*
12. *The Board of Directors is hereby authorized to, in turn, delegate to the Executive Commission (pursuant to the provisions of Section 249 bis I) of the Companies Act) the powers delegated in this resolution.*
13. *The delegation of powers to issue securities granted by the shareholders at the General Shareholders' Meeting held by the Company on May 30, 2014 is hereby deprived of effect to the extent of the unused amount*

Madrid, 4 May 2017