

TELEFONICA S A
Form 6-K
March 14, 2008

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FORM 6-K
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
Report of Foreign Private Issuer
Pursuant to Rule 13a-16 or 15d-16
of the Securities Exchange Act of 1934
For the month of March, 2008
Commission File Number: 001-09531
Telefónica, S.A.
(Translation of registrant's name into English)
Gran Vía, 28
28013 Madrid, Spain
3491-459-3050
(Address of principal executive offices)

Indicate by check mark whether the registrant files or will file annual reports under cover of Form 20-F or Form 40-F:

Form 20-F ☐

Form 40-F ☐

Indicate by check mark if the registrant is submitting the Form 6-K in paper as permitted by Regulation S-T Rule 101(b)(1):

Yes ☐

No ☐

Indicate by check mark if the registrant is submitting the Form 6-K in paper as permitted by Regulation S-T Rule 101(b)(7):

Yes ☐

No ☐

Indicate by check mark whether by furnishing the information contained in this Form, the registrant is also thereby furnishing the information to the Commission pursuant to Rule 12g3-2(b) under the Securities Exchange Act of 1934:

Yes ☐

No ☐

If "Yes" is marked, indicate below the file number assigned to the registrant in connection with Rule 12g3-2(b): N/A

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Telefónica, S.A., as provided in article 82 of the Spanish Stock Market Act (Ley del Mercado de Valores), hereby reports the following

SIGNIFICANT EVENT

Further to the notice sent on February 27th, 2008 and because of the official calling of the Annual General Shareholders Meeting of the Company to be held on April 21st and 22nd, 2008, at first and second call respectively, the full text of the official announcement of the calling of the Annual General Shareholders Meeting, together with the proposals to be submitted for approval at the Meeting, are enclosed to this report.

The aforesaid proposals together with the additional information, are available to shareholders, for examination, at the Company's registered office. Additionally, these documents will be accessible on line via de Company's website: (www.telefonica.es)

We hereby highlight that the time for the Annual General Shareholders Meeting to be held, has been changed to 13.00 p.m.

Madrid, March 14th, 2008

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TELEFONICA, S.A.

Annual General Shareholders Meeting

By decision of the Board of Directors of TELEFÓNICA, S.A., the shareholders are hereby called to the Annual General Shareholders Meeting, **to be held in Madrid, at the premises of Casa de Campo, Pabellón de Cristal, Avenida de Portugal, s/n**, at 13 p.m. on April 22nd 2008 on second call, if the legally required quorum is not reached and therefore the Meeting cannot be held on first call on April 21st 2008 at the same place and time, according to the following

AGENDA

- I. Examination and approval, if appropriate, of the Individual Annual Accounts, of the Consolidated Financial Statements (Consolidated Annual Accounts) and of the Management Report of Telefónica, S.A. and its Consolidated Group of Companies, as well as of the proposed allocation of profits/losses of Telefónica, S.A. and of the management of its Board of Directors, all with respect to the Fiscal Year 2007.
- II. Re-election, ratification, and appointment, if appropriate, of Directors:
 - II.1 Re-election of Mr. José Fernando de Almansa Moreno-Barreda.
 - II.2 Ratification of the interim appointment of Mr. José María Abril Pérez.
 - II.3 Ratification of the interim appointment of Mr. Francisco Javier de Paz Mancho.
 - II.4 Ratification of the interim appointment of Ms. María Eva Castillo Sanz.
 - II.5 Ratification of the interim appointment of Mr. Luiz Fernando Furlán.
- III. Authorization to acquire the Company's own shares, either directly or through Group Companies.
- IV. Reduction of the share capital through the cancellation of shares of treasury stock, excluding creditors right to object, and amendment of the article of the By-Laws relating to the share capital.
- V. Appointment of the Auditors of the Company for the Fiscal Year 2008.
- VI. Delegation of powers to formalize, interpret, cure and carry out the resolutions adopted by the shareholders at the General Shareholders Meeting.

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After the presentation of the items included in the Agenda, the General Shareholders' Meeting will be informed about the amendment to the Board Regulations pursuant to Section 115 of the Securities Market Act. A Report will be presented explaining the subjects included in the Management Report pursuant to Section 116.bis, of the Securities Market Act.

SUPPLEMENT TO THE CALL TO GENERAL SHAREHOLDERS' MEETING

Pursuant to the provisions of Section 97.3 of the Companies Act, shareholders representing at least five percent of the share capital may request the publication of a supplement of this call to the General Shareholders' Meeting, including one or more items in the Agenda. This right must be exercised by means of verifiable notice (which will include the corresponding documents evidencing shareholder status) that must be received at the Company's registered office (Gran Vía, número 28, planta 12ª, Madrid, código postal 28013, to the attention of the General Secretary and Secretary of the Board of Directors) within five days of the publication of this call to Meeting.

PARTICIPATION OF A PUBLIC NOTARY IN THE ANNUAL GENERAL SHAREHOLDERS' MEETING

The Board of Directors has resolved to request the presence of a Public Notary to draw up the minutes of the Meeting, pursuant to Section 114 of the Companies Act in connection with Sections 101 and 103 of the Regulations of the Commercial Registry.

RIGHT TO RECEIVE INFORMATION

In connection with Items I and IV on the Agenda, and pursuant to the legal terms, it is stated for the record that shareholders have the right to examine and obtain at the Company's registered office, or to request the Company to send them, immediately and free of charge, a copy of the following documents:

Individual Annual Accounts, Consolidated Financial Statements (Consolidated Annual Accounts) and Management Report of Telefónica, S.A. and its Consolidated Group of Companies, the corresponding audit reports and the proposed allocation of profits/ losses of Telefónica, S.A.

Proposed reduction in share capital as set forth in Item IV on the Agenda, together with the mandatory Directors Report.

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Furthermore, the following documents are made available to the shareholders at the Company's registered office:
The text of the proposed resolutions relating to all other items on the Agenda.

Brief description of the professional profile for each of the Directors included in the proposed resolution under Item II on the Agenda.

Full text of the Regulations of the Board of Directors.

Report referred to Section 116. bis of the Securities Market Act.

Report on the Director's Remuneration Policy for the Fiscal Year 2007.

Annual Report on Corporate Governance for the Fiscal Year 2007.

All of the documents set forth above will be available electronically on the Company's website (www.telefonica.es). Pursuant to Section 112.1 of the Companies Act, the shareholders may, until the seventh day prior to the date on which the General Shareholders' Meeting is scheduled to be held by completing the form posted on the Company's website for such purpose, or by postal correspondence sent to the Company's registered office (Gran Vía, número 28, planta 11ª, Madrid, código postal 28013, to the attention of the *Oficina del Accionista* [Shareholder Office]), request such information or clarifications as they deem necessary, or ask such questions as they deem appropriate, regarding the matters included on the Agenda or about the information available to the public that has been provided by Telefónica, S.A. to the National Securities Market Commission since May 10, 2007, i.e., the date on which the last General Shareholders' Meeting was held.

RIGHT TO ATTEND THE MEETING IN PERSON OR BY PROXY

The right to attend the General Shareholders' Meeting hereby called applies to shareholders that hold at least 300 shares registered in their name in the corresponding book-entry registry five days in advance of the date on which the Meeting is to be held and who provide evidence thereof by means of the appropriate attendance card or by producing a certificate issued by any of the depositaries participating in the *Sociedad de Gestión de los Sistemas de Registro, Compensación y Liquidación de Valores* [Securities Registration, Clearing and Liquidation Systems Management Company] (IBERCLEAR) or by any other means allowed under applicable Law.

Any shareholder having the right to attend the General Shareholders' Meeting may be represented thereat by another person, who need not be a shareholder. A proxy may be granted by using the proxy-granting form printed on the attendance card or by any other means allowed by Law. The documents containing proxies for the General Shareholders' Meeting must set forth the instructions regarding the manner of voting, provided that, where no express instructions are given, the representative will vote in favor of the proposed resolutions submitted by the Board of Directors regarding the matters on the Agenda, and will vote against of those resolutions that are not included in the Agenda that might be put to the vote at the Meeting.

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If the proxy-granting form does not set forth a specific person to whom the shareholder grants the proxy, such proxy will be deemed granted in favor of the Chairman of the Board of Directors of the Company or of such other person as may replace him as Chairman of the General Shareholders Meeting. In the event that, in accordance with the foregoing, the representative is involved in a conflict of interest upon voting on any of the proposals, whether or not included in the Agenda, which are put to the vote at the General Shareholders Meeting, the proxy will be deemed granted to the Secretary of the General Shareholders Meeting in his capacity as a shareholder having the right to attend.

Shareholders who do not hold the minimum number of shares required to attend may grant a written proxy in respect thereof in favor of another shareholder having the right to attend, or come together with other shareholders that are in the same situation such that they reach the required number of shares and grant a written proxy to one of such shareholders.

DATA PROTECTION

The personal data that shareholders send to the Company in order to attend, grant proxy or vote at the Shareholders Meeting, or the data provided by the entities where those shareholders have deposited their shares, via de legal entity that registers the book entries, Iberclear, shall be used only by Telefónica, S.A. to draw up, complete and monitor the existing shareholder list. Likewise, those data shall be included into a computer file owned by Telefónica, S.A. whose purpose is sending to shareholders any information related to their investment and any other advantage in the sectors of telecommunications, IT, tourism, culture, insurance, financial and home assistance that may derive from their status of shareholders. Each shareholder will have a period of 30 days within the General Shareholders Meeting holding date to oppose to the data processing (by calling toll free at 900 111 004). The shareholder's approval will be deemed granted for this purpose once this period is over. The right of access, rectification, cancellation and opposition to the data processing may be exercised by postal correspondence by attaching a copy of the Identity Card addressed to the attention of the Telefónica, S.A. Shareholder Office located in Distrito C, Ronda de la Comunicación, Edificio Oeste 2, Planta baja 28050 Madrid.

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HOLDING OF THE MEETING ON SECOND CALL

Shareholders are advised that, based on experience from previous years, the General Shareholders Meeting is expected to be held on second call, at 13 p.m. on April 22nd 2008, at the place indicated above.

ENTRANCE AT THE RECINTO FERIA DE LA CASA DE CAMPO PABELLÓN DE CRISTAL

Entrance at the Paseo de Extremadura: Puerta del Ángel or Main Entrance

Metro Station Lago , lines 6 and 10

FOR ANY ADDITIONAL INFORMATION, SHAREHOLDERS MAY CONTACT TELEFÓNICA S SHAREHOLDER OFFICE BY CALLING TOLL-FREE AT 900 111 004, FROM 9:00 A.M. TO 7:00 P.M., MONDAY THROUGH FRIDAY.

Madrid, 14th March 2008

General Secretary and Secretary of the Board

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Telefónica, S.A.

***ANNUAL GENERAL SHAREHOLDERS MEETING
OF TELEFÓNICA, S.A. YEAR 2008 -
PROPOSED RESOLUTIONS SUBMITTED BY THE BOARD OF
DIRECTORS TO THE GENERAL SHAREHOLDERS MEETING***

21 / 22 April 2008

2008 ANNUAL GENERAL SHAREHOLDERS
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Telefónica, S.A.

Proposal regarding Item I on the Agenda: Examination and approval, if appropriate, of the Individual Annual Accounts, of the Consolidated Financial Statements (Consolidated Annual Accounts) and of the Management Report of Telefónica, S.A. and its Consolidated Group of Companies, as well as of the proposed allocation of profits/losses of Telefónica, S.A. and of the management of its Board of Directors, all with respect to Fiscal Year 2007.

A) To approve the Individual Annual Accounts (Balance Sheet, Profit and Loss Statement and Notes), the Consolidated Financial Statements -Consolidated Annual Accounts- (Balance Sheet, Income Statement, Cash Flow Statement, Statement of Recognized Income and Expense, and Notes), and the Management Reports of Telefónica, S.A. and its Consolidated Group of Companies for the Fiscal Year 2007 (ended December 31 of such year), as drawn up by the Board of Directors of the Company at its meeting on February 27, 2008, as well the management performed by the Board of Directors of Telefónica, S.A. during such Fiscal Year.

In the Individual Annual Accounts, the Balance Sheet as of December 31, 2007 reflects assets and liabilities in the amount of 83.159 million Euros each, and the Profit and Loss Account as of the end of the fiscal year reflects positive results of 6.620 million Euros.

In the Consolidated Financial Statements (Consolidated Annual Accounts), the Balance Sheets as of December 31, 2007 reflect assets, and equity and liabilities in the amount of 105.956 million Euros each, and the Income Statement as of the close of the Fiscal Year reflects positive results of 8.908 million Euros.

B) To approve the following Distribution of Telefónica, S.A.'s Profit from Financial Year 2007:

To use the profit obtained by Telefónica, S.A. in Financial Year 2007, adding up to 6,619,861,136.05 as follows:

1,651,746,290.95 to pay an interim dividend (fixed sum of 0.35 gross per share for the total of 4,773,496,485 shares comprising the Company's share capital, with the right to receive it. The said dividend was fully paid out on November 14th 2007).

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Telefónica, S.A.

A maximum of 1,909,398,594.00 to pay a final dividend (maximum amount to be distributed equal to 0.40 gross per share for the total of 4,773,496,485 shares comprising the Company's share capital).

The remaining profit (a minimum of 3,058,716,251.10) to the Voluntary Reserve.

The payment of the final dividend shall be made on May 13th, 2008 through the Entities participating in Sociedad de Gestión de los Sistemas de Registro, Compensación y Liquidación de Valores, S.A. (IBERCLEAR), the Spanish securities registrar, clearing and Settlement Company.

The gross amounts paid shall be subject, where appropriate, to the withholdings required by the applicable legislation from time to time.

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Telefónica, S.A.

Proposal regarding Item II on the Agenda: Re-election, ratification and appointment, if appropriate, of Directors:

II.1 To re-elect as an external Director Mr. Fernando de Almansa Moreno-Barreda, appointing him for a new period of five years.

II.2 To ratify the interim appointment as a Director of the Company, as previously approved by the Board of Directors, of Mr. José María Abril Pérez, appointing him as a proprietary Director for a period of five years, pursuant to the provisions of Law and the By-Laws.

Mr. José María Abril Pérez was appointed as a Director on an interim basis by resolution of the Board of Directors on July 25th, 2007 to fill the vacancy produced by the resignation of Mr. Gregorio Villalabeitia Galarraga.

II.3 To ratify the interim appointment as a Director of the Company, as previously approved by the Board of Directors, of Mr. Francisco Javier de Paz Mancho, appointing him as an independent Director for a period of five years, pursuant to the provisions of Law and the By-Laws.

Mr. Francisco Javier de Paz Mancho was appointed as a Director on an interim basis by resolution of the Board of Directors on December 19th, 2007 to fill the vacancy produced by the resignation of Mr. Enrique Used Aznar.

II.4 To ratify the interim appointment as a Director of the Company, as previously approved by the Board of Directors, of Ms. María Eva Castillo Sanz, appointing her as an independent Director for a period of five years, pursuant to the provisions of Law and the By-Laws.

Ms. María Eva Castillo Sanz was appointed as a Director on an interim basis by resolution of the Board of Directors on January 23rd, 2008 to fill the vacancy produced by the resignation of Mr. Antonio Viana-Baptista.

II.5 To ratify the interim appointment as a Director of the Company, as previously approved by the Board of Directors, of Mr. Luiz Fernando Furlán, appointing him as an independent Director for a period of five years, pursuant to the provisions of Law and the By-Laws.

Mr. Luiz Fernando Furlán was appointed as a Director on an interim basis by resolution of the Board of Directors on January 23rd, 2008 to fill the vacancy produced by the resignation of Mr. Maximino Carpio García, previously filled by Mr. Manuel Pizarro Moreno, whom resigned on January 23rd 2008.

Furthermore, the ratification of any interim appointments of Directors that may have been approved by the Board of Directors since the call to the General Shareholders Meeting and the meeting event will be proposed, if applicable.

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Telefónica, S.A.

Proposal regarding Item III on the Agenda: Authorization to acquire the Company's own shares, either directly or through Group Companies.

- A) To authorize, pursuant to the provisions of Sections 75 et. seq. and the first additional provision, paragraph 2, of the current Spanish Companies Act [*Ley de Sociedades Anónimas*], the derivative acquisition, at any time and as many times as deemed appropriate, of Telefónica, S.A.'s own fully paid-in shares -either directly or through any subsidiaries it controls- by purchase or by any other legal means of consideration.

The minimum acquisition price or consideration shall be equal to the par value of the shares acquired, and the maximum price or consideration shall be equal to the listing price of the shares acquired on an official secondary market at the time of acquisition.

Such authorization is granted for a period of 18 months from the date of this Meeting and is made expressly subject to the limitation that at no time may the nominal value of the Company's shares acquired through the use of this authorization, added to those already possessed by Telefónica, S.A. and any of its controlled subsidiaries, exceed 5 percent of the share capital thereof at the time of acquisition, and the limitations established by the regulatory authorities in the markets where shares of Telefónica, S.A. are admitted for listing must also be respected.

It is expressly stated for the record that the authorization to acquire the Company's own shares may be used in whole or in part for the acquisition of shares of Telefónica, S.A. that it must deliver or transfer to administrators or employees of the Company or companies within its Group, either directly or as a result of the exercise by them of options, all within the framework of duly approved compensation systems linked to the listing price of the Company's shares.

- B) To authorize the Board of Directors, upon the broadest terms possible, to exercise the authorization covered by this resolution and to carry out the other provisions hereof, and such powers may be delegated by the Board of Directors to the Executive Commission, the Executive Chairman of the Board of Directors, the Chief Operating Officer, or any other person that the Board of Directors expressly authorizes for such purpose.
- C) To rescind the unutilized portion of the authorization granted under item III of the Agenda of the Company's General Shareholders' Meeting of May 10th, 2007.

2008 ANNUAL GENERAL SHAREHOLDERS
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Telefónica, S.A.

Proposal regarding Item IV on the Agenda: Reduction of the share capital through the cancellation of shares of treasury stock, excluding creditors' right to object, and amendment of the article of the By-Laws relating to the share capital.

A) To reduce the share capital of the Company by the amount of 68,500,000 euros, by means of the cancellation of 68,500,000 shares of the Company's treasury stock, which were previously acquired in reliance on the authorization previously granted by the shareholders at the General Shareholders' Meeting, within the limits established in Sections 75 et seq. and in additional provision 1, paragraph 2, of the Spanish Companies Act. Accordingly, Article 5 of the By-Laws regarding the amount of the share capital is hereby amended and shall henceforth read as follows:

Article 5.- Share capital

- 1. The share capital is 4,704,996,485 euros, divided into 4,704,996,485 common shares of a single series, with a par value of one euro each, fully paid in.*
- 2. The shareholders at the General Shareholders' Meeting may, complying with the requirements and within the limits legally established for such purpose, delegate to the Board of Directors the power to increase the share capital.*

The reduction of the share capital is made with a charge to discretionary reserves, cancelling the corresponding amount of the restricted reserve mentioned in Section 79.3 of the Spanish Companies Act, and funding a reserve due to capital reduction in the amount of 68,500,000 euros (an amount equal to the par value of the cancelled shares) which may only be used complying with the same requirements as those established for the reduction of the share capital, pursuant to the provisions of item 3 of Section 167 of the Spanish Companies Act. Accordingly, as provided therein, the creditors of the Company shall not have the right to object mentioned in Section 166 of the Spanish Companies Act in connection with the capital reduction resolved to be made.

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Telefónica, S.A.

The reduction does not involve a return of contributions, since the Company itself is the owner of the cancelled shares. The purpose of the reduction will thus be to cancel the shares of treasury stock.

It is stated for the record, in order to comply with the provisions of Section 289.1 of the Spanish Companies Act, that the consent of the Bondholders Syndicates [*Sindicatos de Obligacionistas*] for the outstanding issues of debentures and bonds is not required since the capital reduction resolved to be made does not reduce the original ratio between the sum of capital plus reserves and the amount of the debentures pending repayment.

B) To authorize the Board of Directors, within one year from the date of adoption of this resolution, to determine the other matters that have not been expressly established in this resolution or that are a result hereof, and to adopt the resolutions, take the actions and execute the public or private documents that may be necessary or appropriate for the full implementation of this resolution including, without limitation, the publication of the legally required notices, the making of the appropriate applications and the giving of the appropriate notices required to delist the cancelled shares; such powers may be delegated by the Board of Directors to the Executive Commission, the Executive Chairman of the Board of Directors, the Chief Operating Officer, or to any other person expressly authorized by the Board of Directors for such purpose.

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Telefónica, S.A.

Proposal regarding Item V on the Agenda: Appointment of the Auditors of the Company for the Fiscal Year 2008.

According to the proposal made by the Audit and Control Committee, the Board of Directors submits the following resolution to the approval of the General Shareholders Meeting

Appoint Ernst & Young, S.L. as Auditor for the accounts of Telefónica, S.A. and its Consolidated Group of Companies for the Fiscal Year 2008. Ernst & Young, S.L. is registered in Madrid, at Plaza Pablo Ruiz Picasso, 1, and its tax code is B-8970506.

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Proposal regarding Item VI on the Agenda: Delegation of powers to formalize, interpret, cure and carry out the resolutions adopted by the Shareholders at the General Shareholders Meeting.

To jointly and severally authorize the Executive Chairman, the Chief Operating Officer, the Secretary and the Deputy Secretary of the Board of Directors, such that, without prejudice to any other delegations included in this foregoing resolutions and any powers-of-attorney to convert existing resolutions into public instruments, any of them may formalize and execute the foregoing resolutions, with the power for such purpose to execute the public or private documents that are necessary or appropriate (including those of interpretation, clarification, correction of errors and the curing of defects) for the most correct performance thereof and for the registration thereof, to the extent required, with the Commercial Registry [*Registro Mercantil*] or any other Public Registry.

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Telefónica, S.A

REPORT OF THE BOARD OF DIRECTORS OF TELEFÓNICA, S.A. REGARDING THE PROPOSED REDUCTION OF THE SHARE CAPITAL THROUGH THE CANCELLATION OF SHARES OF TREASURY STOCK, EXCLUDING CREDITORS' RIGHT TO OBJECT, AND AMENDMENT OF THE ARTICLE OF THE BY-LAWS RELATING TO THE SHARE CAPITAL, WHICH IS TO BE SUBMITTED TO THE SHAREHOLDERS FOR APPROVAL AT THE ORDINARY GENERAL SHAREHOLDERS' MEETING (ITEM IV ON THE AGENDA).

1. PURPOSE OF THE REPORT

Item IV of the Agenda for the Ordinary General Shareholders' Meeting of Telefónica, S.A., called for April 21 and 22, 2008, includes a proposal which is submitted to the shareholders for approval at the General Shareholders' Meeting regarding a reduction of the share capital by an amount equal to the par value of certain shares of the Company treasury stock that are to be cancelled, and the amendment of the article of the By-Laws relating to the share capital.

In order for the Board to be able to submit the above-mentioned proposal for the reduction in share capital and the amendment of the By-Laws for approval at the General Shareholders' Meeting, it is mandatory, pursuant to the provisions of Section 164.1 and Section 144.1.a) of the applicable Spanish Companies Act [*Ley de Sociedades Anónimas*], that the Board of Directors prepare a report providing the rationale for the proposal, inasmuch as the approval of such proposal and the implementation thereof necessarily entail an amendment of Article 5 of the By-Laws regarding the amount of share capital and the number of shares into which it is divided.

2. RATIONALE FOR THE PROPOSAL

Within the framework of the shareholder compensation policy established by the Company, the Board of Directors believes it advisable to reduce the share capital by an amount equal to the par value of certain shares held as treasury stock, through the cancellation of such shares, in order to increase earnings per share, which will thus benefit the shareholders.

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If the resolution providing for the reduction of the share capital contemplated in this report is adopted, Article 5 of the By-Laws of the Company would be amended to set forth the new amount of the share capital and the new number of outstanding shares into which such amount is divided (after deducting the shares of treasury stock acquired by the Company and whose cancellation is proposed).

In order to expedite the implementation of this resolution, it is further proposed that the shareholders at the General Shareholders Meeting authorize the Board of Directors to implement such resolution (with the power to delegate, in turn, to the Executive Commission, the Executive Chairman of the Board of Directors, the Chief Operating Officer or to any other person expressly authorized by the Board of Directors for such purpose) within a time limit of one year from the date of adoption of such resolution, without needing to first consult with the shareholders at a General Shareholders Meeting.

In addition, it is deemed appropriate, in order to provide for greater ease of implementation and as permitted by Section 167.3 of the Consolidated Text of the Spanish Companies Act, not to apply the right of creditors to object provided for in Section 166 of such Consolidated Text, and to allocate the amount of the par value of the cancelled shares to a reserve for repurchases of share capital, which may only be used complying with the same requirements as those established for a reduction in the share capital.

Based on these premises, it is proposed to the shareholders at the General Shareholders Meeting to reduce the share capital by the amount of 68,500,000 euros by cancelling 68,500,000 shares of the Company's treasury stock (representing approximately 1.435% of the current share capital of the Company) and to authorize the Board of Directors to implement such resolution within a period of one year.

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Telefónica, S.A

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

The resolutions that the Board of Directors proposes to the shareholders for approval at the Ordinary General Shareholders Meeting in connection with this matter are the following:

- A) *To reduce the share capital of the Company by the amount of 68,500,000 euros, by means of the cancellation of 68,500,000 shares of the Company's treasury stock, which were previously acquired in reliance on the authorization previously granted by the shareholders at the General Shareholders Meeting, within the limits established in Sections 75 et. seq. and in additional provision 1, paragraph 2, of the Spanish Companies Act. Accordingly, Article 5 of the By-Laws regarding the amount of the share capital is hereby amended and shall henceforth read as follows:*

Article 5.- Share capital

- 1. The share capital is 4,704,996,485 euros, divided into 4,704,996,485 common shares of a single series, with a par value of one euro each, fully paid in.*
- 2. The shareholders at the General Shareholders Meeting may, complying with the requirements and within the limits legally established for such purpose, delegate to the Board of Directors the power to increase the share capital.*

The reduction of the share capital is made with a charge to discretionary reserves, cancelling the corresponding amount of the restricted reserve mentioned in Section 79.3 of the Spanish Companies Act, and funding a reserve due to capital reduction in the amount of 68,500,000 euros (an amount equal to the par value of the cancelled shares) which may only be used complying with the same requirements as those established for the reduction of the share capital, pursuant to the provisions of item 3 of Section 167 of the Spanish Companies Act. Accordingly, as provided therein, the creditors of the Company shall not have the right to object mentioned in Section 166 of the Spanish Companies Act in connection with the capital reduction resolved to be made.

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Telefónica, S.A

The reduction does not involve a return of contributions, since the Company itself is the owner of the cancelled shares. The purpose of the reduction will thus be to cancel the shares of treasury stock.

It is stated for the record, in order to comply with the provisions of Section 289.1 of the Spanish Companies Act, that the consent of the Bondholders Syndicates [Sindicatos de Obligacionistas] for the outstanding issues of debentures and bonds is not required since the capital reduction resolved to be made does not reduce the original ratio between the sum of capital plus reserves and the amount of the debentures pending repayment.

- B) To authorize the Board of Directors, within one year from the date of adoption of this resolution, to determine the other matters that have not been expressly established in this resolution or that are a result hereof, and to adopt the resolutions, take the actions and execute the public or private documents that may be necessary or appropriate for the full implementation of this resolution including, without limitation, the publication of the legally required notices, the making of the appropriate applications and the giving of the appropriate notices required to delist the cancelled shares; such powers may be delegated by the Board of Directors to the Executive Commission, the Executive Chairman of the Board of Directors, the Chief Operating Officer or to any other person expressly authorized by the Board of Directors for such purpose.*

Madrid, February 27, 2008

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AUDIT REPORT

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TELEFÓNICA, S.A.

**Financial Statements and Management Report
for the year ended
December 31, 2007**

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Translation of a report and financial statements originally issued in Spanish. In the event of a discrepancy the Spanish-language version prevails (See Note 20)

AUDIT REPORT ON THE FINANCIAL STATEMENTS

To the Shareholders of
Telefónica, S.A.

1. We have audited the financial statements of Telefónica, S.A., which consist of the balance sheet as of December 31, 2007, 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 financial statements 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 financial statements 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 2007, those of 2006. Our opinion refers only to the financial statements for 2007. On March 1, 2007 we issued our audit report on the 2006 financial statements, in which we expressed an unqualified opinion.
3. In our opinion, the accompanying 2007 financial statements give a true and fair view, in all material respects, of the net equity and financial position of Telefónica, S.A. at December 31, 2007 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, 2007 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 financial statements. We have checked that the accounting information included in the report mentioned above agrees with the financial statements for the year ended December 31, 2007. 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.

/s/ José Luis Perelli Alonso

José Luis Perelli Alonso

February 28, 2008

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**TELEFÓNICA, S.A.
ANNUAL FINANCIAL STATEMENTS AND MANAGEMENT
REPORT FOR 2007**

Table of Contents**TELEFÓNICA, S.A.****BALANCE SHEET AT DECEMBER 31**

ASSETS (millions of euros)	2007	2006
A) NON-CURRENT ASSETS	71,348	74,333
I. Intangible assets (Note 5)	97	76
Computer software	188	177
Intellectual property	28	26
Other intangible assets	103	64
Accumulated amortization and provisions	(222)	(191)
II. Property, plant and equipment (Note 6)	765	742
Land and buildings	595	520
Plant and machinery	200	126
Furniture, tools and other items	36	22
Other items of property, plant and equipment	58	42
Property, plant and equipment under construction	22	144
Accumulated depreciation and provisions	(146)	(112)
III. Long-term investments (Note 7)	70,486	73,515
Investments in Group companies	69,274	61,375
Investments in associated companies	3,025	870
Other investments	752	614
Loans to Group and associated companies	10,281	12,501
Other loans	49	178
Long-term deposits and guarantees given	365	349
Tax receivables (Note 14.2)	2,116	3,166
Provisions	(15,376)	(5,538)
B) DEFERRED CHARGES (Note 8)	288	367
C) CURRENT ASSETS	11,514	7,748
I. Accounts receivable	584	314
Trade receivables	22	19
Receivable from Group companies	212	222
Receivable from associated companies	14	7
Other accounts receivable	31	12
Employee receivables		1
Tax receivables (Note 14.2)	327	63
Provision for bad debts	(22)	(10)
II. Short-term investments	8,758	6,154
Loans to Group and associated companies (Note 7.6)	8,216	5,915
Short-term investment securities (Note 7.9)	542	239
III. Short-term treasury stock (Note 9)	232	261
IV. Cash	1,913	981
V. Prepayments and accrued income	27	38
TOTAL ASSETS	83,150	82,448

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

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TELEFÓNICA, S.A.
BALANCE SHEET AT DECEMBER 31

LIABILITIES (millions of euros)	2007	2006
A) SHAREHOLDERS' EQUITY (Note 9)	18,253	16,956
I. Share capital	4,773	4,921
II. Share premium	521	2,589
III. Revaluation reserves	191	1,369
IV. Reserves	7,800	1,251
Legal reserve	984	984
Reserve for treasury stock	232	261
Other reserves	6,584	6
V. Profit for the year	6,620	8,284
VI. Interim dividend paid in the year	(1,652)	(1,458)
B) PROVISIONS FOR LIABILITIES AND CHARGES (Notes 7 and 16)	1,969	1,568
C) LONG-TERM LIABILITIES	42,276	49,264
I. Debentures, bonds and other marketable debt securities (Note 10)	1,097	1,827
Non-convertible debentures and bonds	916	1,332
Other marketable debt securities	181	495
II. Payable to credit institutions (Note 11)	8,435	10,755
III. Payable to Group and associated companies (Note 12)	32,372	36,318
IV. Other payables	8	7
V. Taxes payable (Note 14.2)	364	212
VI. Unpaid portion of investments in Group and associated companies (Note 7.1.b)		145
D) CURRENT LIABILITIES	20,652	14,660
I. Debentures, bonds and other marketable debt securities (Note 10)	1,691	2,098
Non-convertible debentures and bonds	421	500
Other marketable debt securities	1,237	1,541
Interest on debentures and other securities	33	57
II. Payable to credit institutions	671	329
Loans and other accounts payable (Note 11)	607	245
Accrued interest payable	64	84
III. Payable to Group and associated companies (Note 12)	18,008	11,916
IV. Trade accounts payable	95	132
V. Other non-trade payables	187	185
Taxes payable (Note 14.2)	27	27
Other non-trade payables (Note 15)	160	158
TOTAL LIABILITIES	83,150	82,448

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

Table of Contents**TELEFÓNICA, S.A.****INCOME STATEMENT FOR THE YEARS ENDED DECEMBER 31**

DEBIT (millions of euros)	2007	2006
A) EXPENSES		
Personnel expenses (Note 16.2)	156	197
Depreciation and amortization expense	65	51
Property, plant and equipment (Note 6)	34	21
Intangible assets (Note 5)	31	30
Other operating expenses	366	385
External services provided by Group companies (Note 16.8)	69	80
External services	275	291
Taxes other than income tax	17	14
Other operating expenses	5	
I. OPERATING PROFIT		
Financial and similar expenses		
From liabilities with Group companies (Notes 16.4 and 16.8)	2,585	2,149
From other liabilities and similar expenses (Note 16.4)	541	574
Change in provisions for writedown of short-term investments		(11)
Amortization of deferred charges	69	63
Exchange losses (Note 16.5)	1,193	1,031
II. FINANCIAL PROFIT	14,083	5,195
III. INCOME FROM ORDINARY ACTIVITIES	13,724	4,706
Changes in provisions for securities investments (Note 7.3)	9,875	(231)
Extraordinary expenses and losses (Note 16.7)	480	8
IV. EXTRAORDINARY INCOME		2,295
V. PROFIT BEFORE TAXES	5,178	7,001
Corporate income tax in Spain (Note 14)	(1,475)	(1,293)
Foreign taxes (Note 14)	33	10
VI. PROFIT FOR THE YEAR	6,620	8,284

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

Table of Contents**TELEFÓNICA, S.A.****INCOME STATEMENT FOR THE YEARS ENDED DECEMBER 31**

CREDIT (millions of euros)	2007	2006
B) REVENUES		
Net sales to Group companies (Note 16.1)	90	28
Other operating revenues	138	116
Non-core and other current operating revenues Group companies (Note 16.1)	118	98
Non-core and other current operating revenues Non-Group companies	20	18
I. OPERATING LOSS	359	489
Revenue from equity investments	15,335	6,835
Group companies (Note 16.8)	15,099	6,678
Associated companies	211	50
Non-Group companies	25	107
Revenues from other securities and loans (Note 16.4)	1,165	1,131
Group companies (Note 16.8)	1,002	1,033
Other companies	163	98
Exchange gains (Note 16.5)	1,971	1,035
II. FINANCIAL LOSS		
III. LOSSES ON ORDINARY ACTIVITIES		
Gains on disposal of fixed assets (Note 16.6)	1,785	1,872
Extraordinary revenues (Note 16.6)	24	200
IV. EXTRAORDINARY LOSS	8,546	
V. LOSSES BEFORE TAXES		
VI. LOSS FOR THE YEAR		

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

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TELEFÓNICA, S.A.
NOTES TO THE FINANCIAL STATEMENT FOR THE YEAR ENDED
DECEMBER 31, 2007

(1) INTRODUCTION AND GENERAL INFORMATION

Telefónica, S.A. (Telefónica or the Company) is a public limited company incorporated for an indefinite period on April 19, 1924, under the corporate name of Compañía Telefónica Nacional de España, S.A. It adopted its present name in April 1998.

The Company's registered office is at Gran Vía 28, Madrid (Spain), and its Employer Identification Number (CIF) is A-28/015865.

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

In keeping with the above, Telefónica is currently the parent company of a group that operates mainly in the telecommunications, media and entertainment industries, providing a wide range of services on the international stage.

The Company is taxed under the general tax regime established by the Spanish State, the Spanish Autonomous Communities and local governments, and files consolidated tax returns with most of the Spanish subsidiaries of its Group under the consolidated tax regime applicable to corporate groups.

Merger of Telefónica, S.A. and Telefónica Móviles, S.A.

At their respective meetings held on March 29, 2006, the Boards of Directors of Telefónica, S.A. and Telefónica Móviles, S.A. approved a merger agreement, whereby Telefónica, S.A. would take over Telefónica Móviles, S.A., resulting in the dissolution without liquidation of Telefónica Móviles, S.A. and the block transfer of all its equity.

The merger agreement was approved at the General Shareholders' Meetings of Telefónica Móviles S.A. and Telefónica, S.A. held on June 20 and June 21, 2006, respectively.

Pursuant to the agreement, Telefónica transferred shares from treasury stock to Telefónica Móviles shareholders at the exchange ratio established in the merger agreement of 4 Telefónica shares, par value of 1 euro, for every 5 Telefónica Móviles shares, par value of 0.50 euros. No additional cash payment was involved and no new shares were issued. Prior to the exchange, Telefónica Móviles, S.A. paid a dividend of 0.435 euros per share. This, coupled with the 0.205 euros per share dividend charged to 2005 profit, led to a total dividend of 0.64 euros per share, which was paid on July 21, 2006.

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July 28, 2006 was the last trading day for Telefónica Móviles, S.A. shares, which were cancelled as a result of the merger. The merger was registered in the Madrid Mercantile Register on July 29, 2006, effective for accounting purposes from January 1, 2006.

The economic effects of the merger are dated from January 1, 2006. The main effects of this transaction are detailed in the accompanying notes to the annual financial statements. In addition, the main financial statements also include the amounts of the merger transaction in different columns.

(2) BASIS OF PRESENTATION

True and fair view

The accompanying annual financial statements were prepared from Telefónica, S.A.'s accounting records by the Company's directors in accordance with the accounting principles and standards contained in the Commercial Code, as implemented by the Spanish Chart of Accounts in force at that date of these financial statements, and accordingly, give a true and fair view of the Company's equity, financial situation, results of operations and of the funds obtained and applied in 2007.

These annual financial statements will be submitted for approval by shares in the General Meeting, and it is expected that they will be approved with any changes. The annual financial statements for 2006 were approved at the General Shareholders' Meeting held on May 10, 2006.

Comparative information

There were no changes in the structure of the balance sheet or income statement with respect to the previous year. In addition, no material changes were made to accounting criteria with respect to 2006.

No additional significant events have taken place that prevent comparison of the figures for 2007 with those of 2006.

The figures in these annual financial statements and management report are expressed in millions of euros unless otherwise indicated.

New General Chart of Accounts

On November 20, 2007, Royal Decree 1514/2007 was published approving the new General Chart of Accounts (GCA). The new GCA went into effect on January 1, 2008 and its application is mandatory as of that date.

The Company is preparing a transition plan for adapting to the new accounting regulations, which includes, among other matters, analyzing the various differences in accounting criteria and principles, determining the date of the opening balance sheet, selecting the principles and criteria to be applied during the transition, and evaluating the necessary changes in procedures and information systems. The final accounting effects will be disclosed in the 2008 annual accounts.

Table of Contents**(3) PROPOSED APPROPRIATION OF PROFIT**

Telefónica, S.A. obtained 6,620 million euros of profit in 2007.

At its meeting of September 26, 2007, Telefónica, S.A.'s Board of Directors resolved to pay an interim dividend against 2007 profit of 0.35 euros per outstanding share carrying dividend rights. This dividend was paid on November 14, 2007, and the total amount paid was 1,652 million euros.

In addition, at its meeting of February 27, 2008, the Company's Board of Directors agreed to submit for approval at the Shareholders' Meeting the distribution of a final dividend charged to 2007 profit of a fixed amount of 0.40 euros per outstanding share carrying dividend rights, up to a maximum total amount of 1,909 million euros.

Accordingly, the Company's Board of Directors will submit the following proposed appropriation of 2007 profit for approval at the General Shareholders' Meeting:

	Millions of euros
Total distributable profit	6,620
Interim dividend (paid in November 2007)	1,652
Final dividend (maximum distributable amount of 0.40 euros per share for all shares into which the Company's share capital is divided: 4,773,496,485 shares)	1,909
Voluntary reserves	(minimum) 3,059
Total	6,620

Table of Contents**(4) VALUATION CRITERIA**

The main valuation criteria used in preparing the 2007 annual accounts were as follows:

a) *Intangible assets*

This heading includes mainly the following:

1. Computer software licenses, which are recorded at cost and amortized on a straight-line basis over three years.
2. Intellectual property, which is recorded at the amounts paid to acquire ownership of or rights to use patents and trademarks and amortized on a straight-line basis over a period of three to 10 years, depending on the estimated useful life of the patent or trademark.
3. The goodwill arising from the 2005 merger of Telefónica, S.A. and Terra Networks, S.A. This goodwill is amortized on a straight-line basis. It is estimated to have a useful life of 10 years and is included in Other intangible assets.

b) *Property, plant and equipment*

Property, plant and equipment are stated at cost.

Expenses incurred for expansion, remodeling or improvements which increase the productivity, capacity, or prolong the useful life of the asset are capitalized as an increase in the cost of the assets.

The interest and other financial expenses incurred during the construction of property, plant and equipment are also capitalized.

Repairs and maintenance expenses are charged to the income statement of the year incurred.

Property, plant and equipment are depreciated by the straight-line method at annual rates based on the following estimated useful lives:

	Years of estimated useful life
Buildings	40
Plant and machinery	3-25
Furniture, tools and other items	10
Other items of property, plant and equipment	4-10

Table of Contents***c) Long-term investments***

Investments in marketable securities are recorded as follows:

1. Listed securities (excluding shares in Group or associated companies).

At the lower of cost or market value. Market value is taken to be the lower of the average official listing for the fourth quarter or the listed value at year end.

2. Investments in Group and associated companies.

At the lower of acquisition cost or underlying book value of the holdings, adjusted by existing capital gains upon acquisition which prevail at a subsequent valuation date.

3. Other unlisted securities.

At cost, net of the writedown provisions required to reduce them to their underlying book value, adjusted for the amount of the existing capital gains upon acquisition which prevail at the subsequent valuation date.

Unrealized losses (i.e. where cost is higher than market value) are recorded under Provisions (see Note 7.3). However, an additional provision is recorded with a debit (or credit in the case of reversal) to Extraordinary income (or Extraordinary losses) to cover possible third-party liabilities arising from the negative net equity of investees. This provision is included in Provisions for liabilities and charges (see Notes 16.6 and 16.7).

Dividends are recorded as income as soon as their distribution is approved, and gains or losses on the disposal of holdings are recorded as income or expenses in the year in which they are realized.

As required under prevailing legislation, the Company has prepared separate consolidated annual accounts, drawn up in accordance with International Financial Reporting Standards (IFRS). The balances of the main headings of the Telefónica Group consolidated financial statements for 2007 are as follows:

Heading	Millions of euros
Total assets	105,873
Equity	
Attributable to equity holders of the parent	20,125
Attributable to minority interests	2,730
Revenue	56,441
Profit (loss) for the year	
Attributable to equity holders of the parent	8,906
Attributable to minority interests	213

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d) Deferred charges

This heading basically includes the following items:

1. Interest on long-term promissory notes.

This relates to the difference between the face value and the effective value of the promissory notes issued maturing over more than one year. This interest is charged to profit or loss based on financial criteria.

2. Debt issuance expenses.

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

3. Prepayments.

These relate to payments made on the purchase of services not yet received at the balance sheet date.

e) Treasury stock

Treasury stock is valued at the lower of average cost, comprising the total amount paid for the shares, or market value. When these shares are acquired without any prior resolution having been adopted at the Shareholders Meeting to use them to reduce share capital, it is considered that they can be used for subsequent sale or, alternatively, for a capital reduction. Accordingly, the market value is taken to be the lower of the average official market price or the related underlying book value. The allocated provision is recorded against the income statement for the difference between acquisition cost and the lower of the year-end market price or the average market price in the last quarter, and against reserves for the difference between this amount and the related underlying book value.

f) Foreign currency transactions

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

Exchange differences are classified by currency and due date, and for this purpose all currencies that, although different, are officially convertible are grouped together.

Any positive net differences in each group of currencies are recorded under *Deferred income* on the liability side of the balance sheet, unless exchange losses for the Group have been charged to profit and loss in prior years, in which case the positive net differences are credited to income up to the limit of the negative net differences charged to income in prior years.

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Deferred exchange gains are taken to income of the year in which they materialize, the corresponding credit/debit balances are cancelled in advance or as equal or higher exchange losses for each standard currency group are recognized.

g) Pensions and other commitments to employees

The Company has a defined contribution pension plan for employees. The obligations are limited to the regular payment of the contributions, which are taken to income as incurred.

h) Accounts payables

Accounts payable are recorded at repayment value, except in the case of zero-coupon debenture and bond issues, which are recorded in the balance sheet at issuance value plus the related accrued interest (see Note 10.3).

i) Derivatives

Transactions made to eliminate or significantly reduce exchange rate, interest and market risks on asset and liability positions or other transactions are considered hedges. The gains or losses arising during the life of these derivatives are taken to income using the same timing of recognition method as that used to recognize the gains or losses on the underlying hedged item or transaction.

Transactions that are not assigned to cover specific risks are not treated as hedging transactions. In transactions of this kind, which can arise because of hedges of risks at other Group companies and are not originally designated as hedges, the differences in market price are recorded when the transactions are cancelled or finally settled. However, if potential losses are anticipated at year end, the related provision is recorded, with a charge to the income statement.

j) Corporate income tax

The corporate income tax expense for each year is calculated on the basis of book profit before taxes, increased or decreased, as appropriate, by the permanent differences from taxable income. Allowances and deductions from gross tax payable, net of withholdings and prepayments on account, are deducted from the corporate income tax charge in the year in which they are taken. The difference between the accrued expense and the tax paid is due to revenue and expense recognition timing differences giving rise to deferred tax assets and liabilities (see Note 14).

k) Recognition of revenues and expenses

Revenues and expenses are recorded according to the accruals principle, that is, at the moment the goods or services represented by them take place, regardless of when actual payment or collection occurs.

In keeping with the principle of prudence, realized income is only recorded at the balance sheet date, while foreseeable risks and potential losses are recorded when known (see Note 16).

Table of Contents***l) Provision for liabilities and charges***

The Company records provisions for contingencies and expenses based on its best estimate in order to cover quantifiable probable or certain third-party liabilities arising from litigation in progress, indemnity payments and obligations or from expenses of undetermined amount, and collateral and other similar guarantees provided by the Company.

(5) INTANGIBLE ASSETS

The breakdown and movement in intangible asset accounts and the related accumulated amortization in 2007 and 2006 is as follows:

	Millions of euros				
	Balance at 12/31/06	Additions	Disposals	Transfers	Balance at 12/31/07
Cost:					
Computer software	177	6	(8)	13	188
Intellectual property	26	1		1	28
Other intangible assets	64	13		26	103
Intangible assets, gross	267	20	(8)	40	319
Accumulated amortization:					
Computer software	152	16			168
Intellectual property	23	1			24
Other intangible assets	14	14			28
Total accumulated amortization	189	31			220
Provisions	2				2
Intangible assets, net	76	(11)	(8)	40	97

	Millions of euros					
	Balance at 12/31/05	Merger with Telefónica Móviles	Additions	Disposals	Transfers	Balance at 12/31/06
Cost:						
Computer software	153	6	(8)			177
Intellectual property	20	5				26
Other intangible assets	62					64
Intangible assets, gross	235	11	(8)			267
Accumulated amortization:						
Computer software	124	6				152
Intellectual property	17	5				23
Other intangible assets	7					14
Total accumulated amortization	148	11				189
Provisions	2					2
Intangible assets, net	85		(8)			76

Table of Contents**6) PROPERTY, PLANT AND EQUIPMENT**

The breakdown and movement in this heading and related accumulated depreciation in 2007 and 2006 is the following:

	Millions of euros				
	Balance at 12/31/06	Additions	Disposals	Transfers	Balance at 12/31/07
Cost:					
Land and buildings	520	22	(1)	54	595
Plant and machinery	126	44		30	200
Furniture, tools and other items	22	14			36
Other items of property, plant and equipment	42	12		4	58
Property, plant and equipment under construction	144	6		(128)	22
Property, plant and equipment, gross	854	98	(1)	(40)	911
Accumulated depreciation:					
Buildings	62	12			74
Plant and machinery	19	17			36
Furniture, tools and other items	5	4			9
Other items of property, plant and equipment	22	1			23
Total accumulated depreciation	108	34			142
Provision	4				4
Property, plant and equipment, net	742	64	(1)	(40)	765

	Millions of euros					
	Balance at 12/31/05	Merger with Telefónica Móviles	Additions	Disposals	Transfers	Balance at 12/31/06
Cost:						
Land and buildings	214		54		252	520
Plant and machinery	6	5	69		46	126
Furniture, tools and other items	4	3	7		8	22
Other items of property, plant and equipment	29	5	2		6	42
	356		100		(312)	144

Property, plant and equipment
under construction

Property, plant and equipment, gross	609	13	232	854
Accumulated depreciation:				
Buildings	54		8	62
Plant and machinery	5	4	10	19
Furniture, tools and other items	2	2	1	5
Other items of property, plant and equipment	15	5	2	22
Total accumulated depreciation	76	11	21	108
Provision	4			4
Property, plant and equipment, net	529	2	211	742

Additions in 2007 and 2006 mostly relate to costs associated with the construction of the new Telefónica Group central offices (named District C) in a business park development in Las Tablas (Madrid). Land and buildings includes 86 million euros related to the value of the land.

Transfers from property, plant and equipment under construction to other asset accounts relate to the start-up of the various phases of District C, which were fully operational at year end.

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Firm commitments to acquire property, plant and equipment at December 31, 2007 amounted to 7 million euros.

Capitalized interest and other financial expenses incurred in the construction of property, plant and equipment in 2007 amounted to 1 million euros (4 million euros in 2006).

The Company has buildings with a total area of 550,413m² leased to other Telefónica Group companies. This is equivalent to an occupancy rate of 94% of total property available for lease. Revenue from property leases amounted to 31 million euros in 2007 (see Note 16.1), compared to 9 million euros in 2006.

In 2006, the Company recorded a gain of 7 million euros on the disposal of property, plant and equipment (see Note 16.6).

At December 31, 2007, the Company had 24 million euros of fully depreciated property, plant and equipment.

Telefónica, S.A. has taken out insurance policies with appropriate limits to cover the potential risks which could affect its property, plant and equipment.

(7) INVESTMENTS

7.1 The breakdown and movement in Long-term investments is the following:

Millions of euros					
	Balance at 12/31/06	Increases	Decreases	Transfers and other	Balance at 12/31/07
Investments in Group companies	61,375	9,005	(1,094)	(12)	69,274
Investments in associated companies	870	2,315	(160)		3,025
Other investments	614	138			752
Loans to Group and associated companies	12,501	33	(755)	(1,498)	10,281
Other loans	178	3	(15)	(117)	49
Deposits and guarantees	349	28	(12)		365
Tax receivables (Note 14.2)	3,166	1,691	(2,458)	(283)	2,116
Total	79,053	13,213	(4,494)	(1,910)	85,862

	Millions of euros					
	Balance at 12/31/05	Merger Telefónica Móviles, S.A.	Increases	Decreases	Transfers and other	Balance at 12/31/06
Investments in Group companies	23,128	9,043	27,939	(5)	1,270	61,375
Investments in associated companies	1,098	5	1	(202)	(32)	870
Other investments	1,848				(1,234)	614
	14,004	686	76	(378)	(1,887)	12,501

Loans to Group and associated companies						
Other loans	1	123	54			178
Deposits and guarantees	6	338	5			349
Tax receivables (Note 14.2)	3,256	467	1,725	(2,155)	(127)	3,166
Total	43,341	10,662	29,800	(2,740)	(2,010)	79,053

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Investments sold and acquired by Telefónica are as follows:

- a) Acquisitions of equity investments and capital increases:

2007

Company	Millions of euros
Subsidiaries:	
O2 Europe Ltd	8,520
Telefónica International Wholesale Services America, S.A	407
Atento, N.V.	70
Telefónica Ingeniería de Seguridad, S.A.	6
Others	2
Total subsidiaries:	9,005
Associated companies:	
Telco, S.p.A.	2,314
Others	1
Total associated companies:	2,315
Other investments	
PT Multimedia, S.G.P.S., S.A.	136
Others	2
Total other investments	138

On December 20, 2007, Telefónica O2 Europe Plc (formerly O2 Plc) paid Telefónica, S.A. a dividend in kind entailing the transfer of 100% of the shares it held of O2 Europe Ltd. O2 Europe Ltd is the parent to a group of Telefónica companies in Germany. The valuation of the dividend at the transfer date was 8,500 million euros (see Note 16.8). In addition, on December 27, 2007, O2 Europe Ltd increased capital by 20 million euros via the issuance of 100 new shares.

On July 2, 2007, approval was given at the Extraordinary General Shareholders Meeting of Telefónica International Wholesale Services America, S.A. to convert into equity the participating facility between this company at Telefónica, S.A., dated July 31, 2003, whose capital plus accrued interest amounted to 549 million US dollars (407 million euros). After this transaction, Telefónica, S.A. owned 80.56% of the share capital of Telefónica International Wholesale Services America, S.A.

On April 23, 2007, General de Participaciones Empresariales, S.L. (GPE), a subsidiary of Banco Bilbao Vizcaya Argentaria, S.A., announced its intention of exercising the put option granted by Telefónica on all the shares it owned in Atento N.V. at that date. As a result, on July 31, 2007, a purchase-sale contract was signed for Telefónica, S.A. to acquire 10,044 shares owned by GPE, representing 8.65% of Atento N.V.'s share capital, for 70 million euros. The acquisition price may be adjusted up to April 1, 2008, in accordance with certain conditions. After this operation, Telefónica, S.A. controlled 100% of the shares of Atento, N.V.

In addition, in July 2007 Telefónica, S.A. paid off before maturity two participating loans granted to Telefónica Ingeniería de Seguridad, S.A. for 5.5 million euros for their conversion into capital. Telefónica,

S.A. owns 100% of the shares of this company.

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On April 28, 2007, Telefónica, S.A., together with its partners Assicurazioni Generali S.p.A., Intesa Sanpaolo, S.p.A., Mediobanca S.p.A. and Sintonía, S.A. (Benetton), entered into a Co-Investment Agreement and Shareholders Agreement with a view to establishing the terms and conditions of their acquisition of an indirect shareholding in Telecom Italia S.p.A. through an Italian company, currently called Telco S.p.A., in which Telefónica has a 42.3% interest. Both agreements were modified on October 25, 2007 following the inclusion of the Assicurazioni Generali Group companies indicated hereafter and the Shareholders Agreement was further amended on November 19, 2007.

On October 25, 2007 Telco, S.p.A. acquired 100% of Olimpia, S.p.A., which held 17.99% of the voting shares of Telecom Italia, S.p.A. Also on that date, Assicurazioni Generali S.p.A. (together with its group companies Alleanza Assicurazioni S.p.A., INA Assitalia S.p.A., Volksfürsorge Deutsche Lebensversicherung A.G. and Generali Vie S.A.) and Mediobanca S.p.A. contributed a total share of 5.6% of Telecom Italia S.p.A.'s voting shares (4.06% and 1.54%, respectively) to Telco S.p.A.

On December 10, 2007, an agreement was reached to takeover and merge Olimpia S.p.A. into Telco S.p.A., making Telco S.p.A.'s entire stake in the voting shares of the Italian operator (23.6%) direct and leaving Telefónica with an indirect holding in the voting shares of Telecom Italia S.p.A. of 9.98% (6.88% of the dividend rights) for 2,314 million euros.

The Shareholders Agreement signed on April 28, 2007 contained a general clause whereby both Telefónica, at the shareholders meetings of Telco S.p.A. and Telecom Italia S.p.A., and the Telefónica directors appointed to the companies' respective boards, would abstain from participating in and voting at the meetings dealing with issues regarding the provision of telecommunications services by companies controlled by Telecom Italia S.p.A., in countries where there are legal or regulatory restrictions on the exercise of voting rights by Telefónica.

However, as indicated above, on November 19, 2007 the partners amended the Shareholders Agreement, as well as the bylaws of Telco S.p.A., to include the specific limitations imposed by the Brazilian telecommunications regulator, Agência Nacional de Telecomunicações (ANATEL), as initially posted on its website on October 23, 2007 and subsequently published on November 2, 2007 as ANATEL's Ato no. 68,276 dated October 31, 2007.

On November 7, 2007 Portugal Telecom, S.G.P.S., S.A. granted a dividend in kind whereby Telefónica, S.A. obtained the right to receive 0.176067 shares of PT Multimedia, S.G.P.S., S.A. (listed on the Lisbon Stock Exchange and whose main shareholder was Portugal Telecom) for each of the 90,150,075 shares of Portugal Telecom held by the Company. The valuation of the shares received upon their distribution was 9.18 euros per share. Accordingly, Telefónica, S.A. recorded dividend income of 160 million euros (see Note 16.9). The dividend received is subject to a 15% tax. As a result, the shares of PT Multimedia received by Telefónica, S.A. amounted to 14,838,497, representing 4.80% of the company's share capital, valued at 136 million euros.

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2006

Company	Millions of euros
Subsidiaries:	
O2 Plc	24,888
Telefónica Móviles, S.A.	2,978
Others	73
Total subsidiaries:	27,939

In 2006, Telefónica, S.A. acquired 100% of the shares of British company O2 plc. The total acquisition cost was 26,154 million euros (17,887 million pounds sterling), of which 1,266 million euros (859 million pounds) was paid in 2005. The value of the investments acquired in 2005 was recorded under Other investments in the balance sheet at December 31, 2005, until the merger took effect in January 2006. It was then restated to Investments in Group companies and recorded under Transfers in the table of movements.

Under the terms of the merger agreement between Telefónica, S.A. and Telefónica Móviles, S.A. (see Note 1), Telefónica acquired 927,917,620 shares of Telefónica Móviles, S.A., representing 21.43% of its share capital, which formerly belonged to Telefónica Internacional, S.A. (a wholly-owned subsidiary of Telefónica). This intragroup transfer meant that Telefónica, S.A.'s investment in Telefónica Móviles, S.A. was now directly wholly-owned, thereby avoiding creating any indirect treasury stock holdings as a result of the merger.

The shares transferred were priced at 8.653 euros per share. The acquisition cost of these shares, after deducting the margin on the transaction generated and paid by Telefónica Internacional, S.A., was 2,956 million euros.

Another 2 million Telefónica Móviles S.A. shares were acquired for a total of 22 million euros. Following these acquisitions, the percentage investment in Telefónica Móviles, S.A. before the share exchange was 92.5% (see Note 7.4).

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b) Disposals of investments

2007

Company	Millions of euros Gross book value
Subsidiaries	
Endemol Investment Holding, B.V.	842
Seguros de Vida y Pensiones Antares, S.A.	148
Ecuador Cellular Holdings, B.V.	77
Terra Lycos Intangibles, S.A.	19
Others	8
Total subsidiaries	1,094
Associated companies	
Portugal Telecom, S.G.P.S., S.A.	156
Others	4
Total associated companies	160

In May 2007, Telefónica, S.A. signed an agreement to sell its 99.7% holding in Endemol Investment Holding, B.V. to a newly created consortium. The sale was carried out on July 3, 2007, generating a capital gain of 1,776 million euros (see Note 16.6).

On May 31, 2007, a resolution was adopted at the General Shareholders Meeting of Seguros de Vida y Pensiones Antares, S.A. to reduce capital by condoning the unpaid dividend liability to its shareholders. After this operation, Telefónica owned 94.67% of the share capital of Seguros de Vida y Pensiones Antares, S.A.

In 2007, Ecuador Cellular Holdings, S.A. reimbursed its sole shareholder, Telefónica, S.A. for contributions amounting to 77 million euros. In addition, Terra Lycos Intangibles, S.A. was liquidated during the year.

On December 18, 2007, Telefónica, S.A. disposed of 18,558,181 shares representing 1.64% of the share capital of Portugal Telecom, S.G.P.S., S.A. This lowered Telefónica, S.A.'s direct holding in Portugal Telecom to 7.14%.

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2006

Company	Millions of euros Gross book value
Subsidiaries	
Telefónica Publicidad e Información, S.A.	4
Others	1
Total subsidiaries	5
 Associated companies	
Sogecable, S.A.	12
Uno-e Bank, S.A.	190
Total associated companies	202

In April 2006, Telefónica, S.A. agreed to a takeover bid for its investment in Telefónica Publicidad e Información, S.A. by British telephone directories company Yell Group plc. In July 2006, Telefónica S.A. accepted the takeover bid presented by Yell at a price of 8.5 euros per share, tendering 216,269,764 shares representing its 59.905% stake in the company's share capital. This transaction generated a gain of 1,834 million euros, which was recorded under Gains on disposal of fixed assets (see Note 16.6). In March 2006, Telefónica S.A. sold 590,656 shares in Sogecable S.A. for 22 million euros. This transaction generated a gain of 10 million euros, which was recorded under Gains on disposal of fixed assets (see Note 16.6).

Also, under the agreement signed January 10, 2003, between Banco Bilbao Vizcaya Argentaria, S.A. (BBVA) and Terra Networks, S.A. (now Telefónica, S.A.), which created a liquidity mechanism (put options) on the shares owned by Terra Networks, S.A. in Uno-e Bank, S.A., Telefónica S.A. sold its investment in Uno-e Bank to BBVA at the option strike price stated in the agreement. This transaction had no impact on the income statement for the year.

c) Other transactions

2007

On December 21, 2007, Telefónica, S.A. incorporated, as its sole shareholder, the Spanish limited liability company Atento Holding, Inversiones y Teleservicios, S.A. The share capital of this company was set at 24 million euros, divided up into 60 million shares, issued with a share premium of 138 million euros, at 2.306133 euros per share. The shares were fully subscribed and paid via the contribution to the newly created wholly-owned company of the 116,112 shares representing 100% of the share capital of Atento, N.V. owned by Telefónica, S.A.

In addition, on December 21, 2007, a resolution was adopted at the Extraordinary Shareholders' Meeting of Telefónica Móviles Holding Uruguay, S.A, a wholly-owned subsidiary of Telefónica, S.A., to liquidate and wind up the company, assigning all the assets and liabilities of the company to the sole shareholder. As a

result of this transaction, Telefónica, S.A. directly owns 62,700,000 shares, representing 32% of the share capital of Telefónica Móviles del Uruguay, S.A.

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The assets and liabilities assigned to Telefónica, S.A. are as follows:

	Valuation
Shares of Telefónica Móviles del Uruguay, S.A.	13
Receivables from Group companies (Telefónica Móviles del Uruguay, S.A.)	9
Payables to Group companies (Telefónica Móviles del Uruguay, S.A.)	1
2006	

On July 3, 2006, Telefónica de España S.A.U. and Terra Networks España S.A.U., both wholly owned subsidiaries of Telefónica S.A., merged. The transaction involved the merger and takeover of Terra Networks España, S.A.U. by Telefónica de España S.A.U. As a result, Terra Networks España, S.A.U. was dissolved without liquidation, and Telefónica de España, S.A.U. assumes all its rights and obligations. The gross acquisition cost of Terra Networks España, S.A.U. was 94 million euros, which was fully provisioned.

In 2006, there was a restructuring of the Company's wireless investments in Argentina. This culminated in the final quarter of 2006 with the Compañía de Radiocomunicaciones Móviles, S.A. and Telefónica Móviles Argentina, S.A. merger. Telefónica Móviles Argentina, S.A. took over Compañía de Radiocomunicaciones Móviles, S.A.'s operations once the Argentine securities exchange commission (*Comisión Nacional de Valores de Argentina*) lifted the merger conditions it had imposed on October 31, 2006. The merger took effect from January 1, 2006.

Also completed in 2006 was the merger between Telefónica Móviles Inversora, S.A. and Telefónica Móviles Argentina Holding, S.A., with effect from January 1, 2006. This corporate restructuring left Telefónica direct ownership of 15.4% of Telefónica Móviles Argentina, S.A., along with its 100% investment in the Telefónica Móviles Argentina Holding, S.A. holding company, which owns the remaining 84.6%.

7.2 The detail of subsidiaries, associated companies and investees is provided in Appendix I.

7.3 The breakdown and movement in provisions for long-term investments are as follows:

	Millions of euros				
	Balance at 12/31/06	Change in provision	Decreases	Transfers and other	Balance at 12/31/07
Investments in Group companies	5,530	9,876	(12)	(25)	15,369
Investments in associated companies	3	(1)			2
Other investments	5				5
Total investment writedown provisions	5,538	9,875	(12)	(25)	15,376

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	Millions of euros				
	Balance at 12/31/05	Merger with Telefónica Móviles, S.A.	Change in provision	Decreases	Balance at 12/31/06
				Transfers and other	
Investments in Group companies	3,440	2,420	(156)	(174)	5,530
Investments in associated companies	86	1	(43)	(41)	3
Other investments	37		(32)		5
Total investment writedown provisions	3,563	2,421	(231)	(41)	5,538

The main provisions recorded for investments in Group companies in 2007 relate to the investment in Telefónica O2 Europe, Plc for 9,947 million euros arising from the dilution to this company's equity from the dividends paid to Telefónica, S.A. in 2007 for a total amount of 11,272 million euros (see Notes 7.1.a and 16.8). The Company also allocated 91 million euros in 1997 to provisions for the investment in Telefónica de Contenidos, S.A.

In addition, a charge of 436 million euros was recorded to extraordinary income in 2007 (506 million euros in 2006) due to the negative equity of Telefónica Móviles México, S.A. de C.V. (see Notes 4.c and 16.7).

Conversely, in 2007 provisions were reversed for the improvement in equity of Atento, N.V., Telefónica Móviles Argentina Holding and Telefónica O2 Czech Republic, for 60, 54 and 36 million euros, respectively.

The main provisions recorded for investments in Group companies in 2006 relate to the investments in Telefónica Móviles Puerto Rico Inc. (48 million euros), Ecuador Cellular Holding, BV (32 million euros) and Telefónica O2 Czech Republic, a.s. (98 million euros) which paid a dividend of 354 million euros to Telefónica, S.A. (see Note 16.8).

Meanwhile, some provisions were reversed in 2006, owing to the improvement in equity of other companies, mainly Telefónica de Contenidos (192 million euros), Telefónica Datacorp, S.A.U. (65 million euros) and the Atento Group (45 million euros).

In addition, after the Terra Networks España, S.A.U. and Telefónica de España, S.A.U. merger (see Note 7.1.c), the outlook for the new company led to the reversal of a provision for liabilities and charges recorded for the negative equity of Terra Networks España, S.A. This generated 336 million euros of extraordinary income. Additionally, 292 million euros was reversed from the provision recorded for Telefónica Móviles Argentina Holding, S.A. in 2006, of which 242 million was recorded as extraordinary income (see Note 16.6).

In 2006 the entire 36 million euro provision for the investment in Portugal Telecom, S.G.P.S., S.A. was reversed from writedown provisions on Investments in associated companies.

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The reversals from investment writedown provisions on Other investments in 2006 included the 22 million euro provision recorded for Telefónica, S.A.'s stake in Banco Bilbao Vizcaya Argentaria, S.A.

Retirements recorded in 2007 and 2006 correspond to investments sold, liquidated or transferred in the course of the year (see 7.1 of this Note).

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7.4 Impact on long-term investments of the merger of Telefónica, S.A. and Telefónica Móviles, S.A. (2006)

As indicated in Note 1, on July 29, 2006 the merger between Telefónica, S.A. y Telefónica Móviles, S.A. was registered in the Madrid Mercantile Register on January 1, 2006.

Telefónica transferred to Telefónica Móviles, S.A. shareholders 244,344,012 of its treasury share at the exchange ratio established in the merger agreement of four Telefónica S.A. shares for every five Telefónica Móviles, S.A. shares. The acquisition cost of the treasury stock transferred amounted to 3,179 million euros, was recorded as an increase in value of Long-term investments.

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The detail of Telefónica Móviles, S.A.'s contributions on January 1, 2006 to Investments in Group companies, and the corresponding investment writedown provisions shown in the financial statements of Telefónica, S.A., was the following:

	Millions of euros		
	Acquisition cost	Investment writedown provisions	Additional provision for negative net book value of the investment (see Note 4.c)
Investments in Group companies			
Telefónica Móviles España, S.A.	933		
TES Holding, S.A. de C.V.	161	(96)	
Telefónica Móviles Argentina Holding, S.A.	790	(790)	(242)
Telefónica Móviles Inversora, S.A.	370	(33)	
Compañía Radiocomunicaciones Móviles, S.A.	142	(5)	
Telefónica Móviles Chile, S.A.	308	(9)	
Telefónica Móviles Chile Inversiones, S.A.	10	(5)	
TCG Holdings, S.A.	239	(104)	
Redanil, S.A.	8		
TEM eServices Latin America Inc.	3		
Telefónica Móviles Perú Holding, S.A.A.	254	(31)	
Telefónica Móviles México, S.A. de C.V.	1,176	(1.176)	(942)
Brasilcel, N.V.	2,179		
Telefónica Móviles Soluciones y Aplicaciones, S.A.	11	(6)	
Telefónica Móviles Puerto Rico, Inc.	63	(63)	(3)
Panamá Cellular Holding B.V.	238	(3)	
Telefónica Móviles Holding Uruguay, S.A.	26		
Telefónica Móviles Colombia, S.A.	116	(1)	
Cellular Holdings (Central America), Inc.	38		
Comtel Comunicaciones Telefónicas, S.A.	0		
Telefónica Móviles Perú, S.A.	0		
Ecuador Cellular Holding, B.V.	658	(75)	
Guatemala Cellular Holding, B.V.	29	(3)	
Inversiones Telefónicas Móviles Holding, S.A.	424		
Latin American Cellular Holding, B.V.	1,227	(19)	
Multi Holding Corporation	301	(1)	
Telcel, C.A.	134		
Others	1		
Total Group companies	9,839	(2,420)	(1,187)
Investments in associated companies			
MobiPay Internacional, S.A.	5	(1)	
Total associated companies	5	(1)	

The effect of the inclusion of the investments of Telefónica Móviles, S.A. described above, combined with the retirement of Telefónica S.A.'s pre-merger investment in Telefónica Móviles, S.A. is shown in the Merger with Telefónica Móviles, S.A. column of the tables of changes in long-term investments and investment writedown provisions.

7.5 Transactions protected for tax purposes.

Transactions carried out in 2007 and 2006 that are considered protected for tax purposes, as defined in Articles 83 and 94, of Chapter VII of Title VII of Legislative Royal Decree 4/2004 of March 5 approving the Revised Spanish Corporate Income Tax Law, are detailed in the following paragraphs. Transactions prior to 2006 were duly disclosed in prior years' financial statements.

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2007

On December 21, 2007, the public deed was registered for the contribution of 100% of the shares of Dutch company Atento N.V. to Spanish company Atento Holding, Inversiones y Teleservicios, S.A. The share exchange was registered in the Mercantile Registry on January 15, 2008.

In addition, the following transactions protected for tax purposes involving subsidiaries belonging to the tax group headed by Telefónica, S.A also took place in 2007:

In July 2007, the agreement for the merger of Maptel Networks, S.A. by Telefónica Soluciones de Informática y Comunicaciones, S.A. was executed. As a result of this merger the absorbing company Telefónica Soluciones de Informática y Comunicaciones, S.A. acquired by universal succession all the rights and obligations of Maptel Networks, S.A.

On October 5, the agreement for the merger and takeover of Telefónica Cable Galicia, S.A.U. by Telefónica Cable, S.A. was executed. As a result of this merger, the absorbing company Telefónica Cable, S.A. acquired by universal succession all the rights and obligations of Telefónica Cable Galicia, S.A.U. The merger was registered in the Mercantile Registry in October 2007.

On October 17, the agreement for the merger and takeover of Procesos Operativos, S.A. by Atento Teleservicios España, S.A.U. was executed. As a result of this merger, the absorbing company Atento Teleservicios España, S.A.U. acquired by universal succession all the rights and obligations of Procesos Operativos, S.A. The merger was registered in the Mercantile Registry on December 26, 2007.

On November 2, the agreement for the merger and takeover of Fonditel Valores, Agencia de Valores, S.A.U. by Fonditel Gestión, Sociedad Gestora de Instituciones de Inversión Colectiva, S.A.U. was executed. The merger was registered in the Mercantile Registry on November 15, 2007.

2006

On July 29, 2006, the merger of Telefónica Móviles S.A into Telefónica S.A., which held 100% of the outstanding shares, was registered in the Mercantile Registry. As a result of this merger the surviving company Telefónica S.A. acquired by universal succession all the rights and obligations of Telefónica Móviles S.A.

On July 7, 2006, the merger and takeover of Terra Networks España, S.A. by Telefónica de España, S.A. was registered in the Mercantile Registry, with Telefónica de España, S.A. retaining by universal succession all the rights and obligations of Terra Networks España S.A.

On June 15, 2006, Telefónica Móviles, S.A. contributed 97.97% of Peruvian company Telefónica Móviles Perú Holding, S.A. to the Dutch company Latin American Cellular Holdings B.V. a wholly owned subsidiary of Telefónica Móviles, S.A. The transaction was carried out through a share exchange.

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Finally, on May 31, 2006, Telefónica Móviles, S.A. contributed 91.54% of Venezuelan company Telcel, C.A. to the Dutch company Latin American Cellular Holdings, B.V., a wholly owned subsidiary of Telefónica Móviles, S.A. The transaction was carried out through a share exchange.

The following transactions protected for tax purposes involving subsidiaries belonging to the tax group headed by Telefónica, S.A. also occurred in 2006:

On September 22, the agreement for the takeover and merger of Telefónica Soluciones de Informática y Comunicaciones, S.L. by Telefónica DataCorp, S.A, its sole shareholder, was executed. As a result of this merger, the absorbing company Telefónica DataCorp., S.A. acquired by universal succession all the rights and obligations of Telefónica Soluciones de Informática y Comunicaciones, S.L. The merger was registered in the Mercantile Registry on November 28, 2006.

On June 30, the takeover and merger of Telefónica Data España, S.A. by Telefónica de España, S.A. was registered in the Mercantile Registry, with Telefónica de España, S.A. obtaining all the rights and obligations of Telefónica Data España, S.A.

On June 12, the takeover and merger of Sociedad General de Cablevisión Canarias, S.A. by Telefónica Cable, S.A. was registered in the Mercantile Registry, with Telefónica Cable, S.A. taking over by universal succession all the rights and obligations of Sociedad General de Cablevisión Canarias, S.A.

7.6 The breakdown of loans to Group and associated companies is as follows:

Company	Millions of euros			
	2007		2006	
	Long-term	Short-term	Long-term	Short-term
Telefónica de España, S.A.U.	3,188	3,096	4,207	1,734
Telefónica Móviles España, S.A.U.	3,102	1,112	3,135	1,241
Telefónica Móviles México, S.A. de C.V.	2,330	682	2,445	452
Telefónica O2 Europe Plc		2,727		
Telefónica de Contenidos, S.A.U.	1,221	81	1,329	40
Telefónica Internacional, S.A.		218	346	1,619
Telefónica Móviles Argentina, S.A.	284	85	490	33
Atento, N.V.	38	65	99	38
Telefónica International Wholesale Services America, S.A.				400
Comunicapital Inversiones, S.A.U.			54	
Lotca, Servicios Integrales, S.A.U.	57	5	65	5
Terra Networks Asociadas, S.L.	16	19	35	1
Telefónica B2B Licencing Inc.	9		11	
Telefónica Internacional Wholesale Services, S.L.		28	60	
Inversiones Telefónica Móviles Holding Limitada	29		142	
Telefónica Móviles El Salvador Holding, S.A. de C.V.		49	48	27
Latin America Cellular Holdings, B.V.				218
Panama Cellular Holdings, B.V.		5		40
Others	7	44	35	67
Total	10,281	8,216	12,501	5,915

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As a consequence of the merger with Telefónica Móviles, S.A. (see Note 1), Telefónica, S.A. assumed all the loans granted to finance the wireless operators, including those to Telefónica Móviles España, S.A., Telefónica Móviles México, S.A. de C.V., Telefónica Móviles Argentina, S.A. and Latin America Cellular Holdings, B.V.

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The main loans granted to Group companies are:

Financing granted to Telefónica de España, S.A.U. consists mainly of a loan dated January 4, 1999 resulting from the company's spin-off from Telefónica on January 1, 1999, that bears interest at 6.80% and had an outstanding balance of 3,488 million euros at December 31, 2007, of which 2,791 million euros are long term and 697 million euros are short term.

2006 featured the takeover and merger of Terra Networks España, S.A.U. by Telefónica de España, S.A.U., both wholly owned direct subsidiaries of Telefónica, S.A. As a result, Terra Networks España, S.A.U. was dissolved without liquidation, and Telefónica de España, S.A.U. assumed the 397 million euro participating loan granted by Telefónica, S.A. to Terra Networks España, S.A.U. The loan matures on November 15, 2009 and bears interest linked to the Euribor rate.

Financing granted to Telefónica Móviles España, S.A.U. mainly comprises a long-term participating loan dated October 1, 2002, for 3,102 million euros, paying annual fixed interest plus a floating interest rate based on the performance of the company. The loan matures on December 22, 2009.

Financing granted to Telefónica Móviles México, S.A. de C.V. comprises:

A 1,330 million euro loan, drawn down in full at December 31, 2007. The loan matures on December 31, 2011 and interest is linked to the 12M Euribor rate.

Several loans in Mexican pesos, wholly drawn down for a total of 8,518 million pesos (533 million euros). These loans mature between 2009 and 2011 and bear a fixed interest rate.

Two loans denominated in US dollars, totaling 685 million dollars (467 million euros). These loans mature in 2009 and interest is linked to the 12M Libor rate.

Financing granted to Telefónica de Contenidos, S.A.U. mainly comprises a 1,142 million euro participating loan, fully drawn down at December 31, 2007, which bears interest based on Telefónica de Contenidos, S.A.U.'s business performance. In addition, Telefónica, S.A. granted a new participating loan of 79 million euros maturing in 2015 to provide Telefónica de Contenidos, S.A.U. with funding to cover the financial charges linked to the participating loan detailed above.

A multi-currency credit facility of 1,962 million US dollars granted to Telefónica Internacional, S.A., of which 318 million US dollars (216 million euros) had been drawn down at December 31, 2007. This facility matures April 15, 2008.

Financing granted to Telefónica Móviles Argentina, S.A. comprises a number of US dollar-denominated loans, maturing between 2008 and 2017 and bearing a fixed interest rate.

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Financing granted to Atento, N.V. consists of the following:

A participating loan for 75 million euros, repayable in 2013. The loan bears interest based on Atento, N.V.'s operating profit. The outstanding amount at December 31, 2007 was 45 million euros.

Loan of 214 million euros to support Atento Holding's ability to pay its liabilities to its subsidiaries, bearing interest at market rates and maturing in 2008. The balance outstanding at December 31, 2007 was 57 million euros.

The Company has also extended loans in connection with the taxation of Telefónica, S.A. as the head of the tax Group pursuant to the consolidated tax regime applicable to corporate groups (see Note 14), mainly 2,350 million euros to Telefónica Móviles España, S.A. and 1,060 million euros to Telefónica de España, S.A.U., with short-term maturities.

At December 31, 2007, pending receipt is the interim dividend against 2007 profit by Telefónica O2 Europe Plc for 2,000 million pounds sterling (equivalent to 2,727 million euros), which will be paid in the first quarter of 2008.

Loans to Group companies includes accrued interest payable at December 31, 2007 amounting to 814 million euros (583 million euros at December 31, 2006).

Transfers under Loans to Group and associated companies in the table of movements in investments relate mainly to short-term movements required to meet the repayment schedules of the loans listed above.

7.7 Other loans

The heading mainly includes the cost of share options arranged in 2006 to cover the Telefónica, S.A. share option plan (see Note 16.2), amounting to 46 million euros.

7.8 Deposits and guarantees

The main components of this heading are the 335 million euros of guarantees of IPSE 2000, S.p.A. at December 31, 2007. These deposits will decrease in line with the respective obligations they guarantee.

7.9 Other short-term investments

This heading consists mainly of temporary cash surpluses placed in short-term investments. At December 31, 2006, it included 111 million euros pending payment on the sale of the investment in Uno-e Bank (see Note 7.1.b), which was collected in 2007.

Table of Contents**(8) DEFERRED CHARGES**

The detail of this heading and the related amortization schedule at December 31, 2007 and 2006 are as follows:

	Maturity						Balance at 12/31/07	Balance at 12/31/06
	2008	2009	2010	2011	2012	Subsequent years		
Interest on long-term promissory notes	11	7	8	1			27	44
Debt issuance costs	67	34	29	25	23	30	208	271
Other deferred charges	20	10	7	6	6	4	53	52
Total	98	51	44	32	29	34	288	367

(9) SHAREHOLDERS EQUITY

The amount and movements in this heading in 2007 and 2006 was the following:

	Balance at 12/31/05	Appropriation of 2005 profit	Distribution of dividends	Other movements	Balance at 12/31/06	Appropriation of 2006 profit	Distribution of dividends	Other movements	Balance at 12/31/07
Share capital	4,921				4,921			(148)	4,773
Share premium	1,671			918	2,589			(2,068)	521
Revaluation reserves	1,369				1,369			(1,178)	191
Legal reserve	920	64			984				984
Reserve for treasury stock	348			(87)	261			(29)	232
Other reserves	6	521		(521)	6	5,400		1,178	6,584
Profit (loss) for the year	1,754	(1,754)		8,284	8,284	(8,284)		6,620	6,620
Interim dividend			(1,458)		(1,458)	1,458	(1,652)		(1,652)
Total	10,989	(1,169)	(1,458)	8,594	16,956	(1,426)	(1,652)	4,375	18,253

a) Share capital

At December 31, 2007, Telefónica, S.A.'s share capital amounted to 4,773,496,485 euros and consisted of 4,773,496,485 fully paid ordinary shares of a single series, par value 1 euro, all recorded by the book-entry system and traded on the Spanish electronic trading system (Continuous Market), where they form part of the Ibex 35 Index, on the four Spanish Stock Exchanges (Madrid, Barcelona, Valencia and Bilbao) and listed

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on the New York, London, Paris, Frankfurt, Tokyo, Buenos Aires, Sao Paulo and Lima Stock Exchanges. In October 2007, Telefónica, S.A. began taking steps to delist shares of Telefónica from the Paris and Frankfurt stock exchanges. This will take place in the first quarter of 2008.

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At the Shareholders' meeting of Telefónica S.A. on June 21, 2006, the Board of Directors was authorized under Article 153.1.b) of the Spanish Corporation Law, to increase the Company's capital by up to 2,460 million euros, equivalent to half the Company's current capital stock, one or several times within a maximum of five years of that date, with no need for further meetings or authorization, where the Board considered it in the Company's interests, by issuing for this purpose the corresponding new common shares or shares of any other type permitted by law, at a fixed or variable premium and, in all cases, paid in cash with the possibility explicitly allowed of partial subscription for shares issued in accordance with Article 161.1 of the Corporation Law. The Board was also authorized to fully or partly disapply pre-emptive subscriptions rights under Article 159.2 of the Corporation Law and associated provisions.

In addition, at the May 10, 2007 Shareholders' Meeting, authorization was given for the Board of Directors to issue fixed-income securities and preferred shares at one or several times within a maximum period of five years from the date of adoption of the related resolution. The fixed-income securities may be debentures, bonds, promissory notes or any other kind of fixed-income security, plain, or, in the case of debentures and bonds, convertible into shares of the Company and/or exchangeable for shares of any of the group companies. They may also be preferred shares. The total maximum amount of the securities issued agreed under this authorization is 25,000 million euros or the equivalent in another currency. As at December 31, 2007, the Board of Directors had exercised these powers, approving a program to issue corporate promissory notes for 2008.

In addition, on May 10, 2007, shareholders voted to authorize the derivative acquisition by the Board of Directors of treasury shares, for a consideration, up to the limits and pursuant to the terms and conditions established by the Shareholders' Meeting, within a maximum period of 18 months from that date. However, it specified that in no circumstances could the par value of the shares acquired, added to that of the treasury shares already held by Telefónica, S.A. and by any of its controlled subsidiaries, exceed 5% of Telefónica's share capital.

At December 31, 2007 and 2006, Telefónica, S.A. held the following shares of treasury stock:

		Euros per share			
	No. of shares	Acquisition price	Market price	Market Value	%
<i>Treasury stock at 12/31/07</i>	64,471,368	16.67	22.22	1.433	1.35061%
<i>Treasury stock at 12/31/06</i>	75,632,559	14.04	16.12	1.219	1.53689%

In 2007, the Company paid 2,392 million euros to acquire 149,099,044 of its own shares (including a 68 million euros premium on the share options arranged in 2007 and exercised in 2007) and sold 12,621,573 treasury shares at a total selling price of 210 million euros. As a result of these transactions, the Company recorded extraordinary income of 23 million euros (see Note 16.6) and a decrease in expenses of 11 million euros from the sale of treasury shares allocated to the share option plan for Endemol Group employees.

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In addition, the Company used 147,633,912 shares of treasury stock at an acquisition cost of 2,202 million euros to reduce its share capital. Finally, 4,750 shares of treasury stock were delivered as part of the share option plan for Endemol Group employees (own shares were also sold to compensate).

The balance sheets at December 31, 2007 and 2006 include the cost of acquiring own shares (1,075 and 1,062 million euros, respectively) net of provisions of 843 and 801 million euros, respectively, recorded in accordance with current accounting regulations (see Note 4.e), against extraordinary results for the difference between the acquisition cost and market price and against Unrestricted reserves for the difference between the market price and the underlying book value. The movement in the provision charged to Other reserves in 2007 and 2006 were a credit of 42 million euros and a debit of 590 million euros, respectively. In 2006, the Company reserved a 38 million euro provision charged against extraordinary income (see Note 16.6).

The Company has set up the corresponding restricted reserve in the amount of the underlying book value of the shares comprising treasury stock.

Changes in subscribed capital and share premium in 2007

The movements in these headings in 2007 are as follows:

		Millions of euros	
	Number of Shares	Subscribed capital	Share premium
Balance at 12/31/06	4,921,130,397	4,921	2,589
Restricted reserve for treasury stock			29
Valuation of treasury stock			(43)
Capital reduction	(147,633,912)	(148)	(2,054)
Balance at 12/31/07	4,773,496,485	4,773	521

Authorization was given at the General Shareholders Meeting of Telefónica, S.A. of May 10, 2007 to reduce the Company's share capital by 147,633,912 via the cancellation of own shares held in treasury stock. The capital decrease was carried out with a charge to voluntary reserves, with the corresponding amount released from the restricted reserve provided for in Article 79.3 of the Spanish Corporation Law, and reserve recorded for cancelled share capital for 147,633,912 euros (an amount equal to the par value of the cancelled shares), which can only be used if the same requirements as those applicable to the reduction of share capital indicated in section 3 of Article 167 of the Spanish Corporation Law are met.

Table of Contents**Changes in subscribed capital and share premium in 2006**

The movements in these headings in 2006 are as follows:

	Number of Shares	Millions of euros Subscribed capital	Share premium
Balance at 12/31/05	4,921,130,397	4,921	1,671
Restricted reserve for treasury stock			87
Valuation of treasury stock			1,111
Reserve for merger with Telefónica Móviles, S.A.			(280)
Balance at 12/31/06	4,921,130,397	4,921	2,589

As mentioned in Note 1, the proposed merger and takeover of Telefónica Móviles, S.A. by Telefónica, S.A. was approved at the General Shareholders Meetings held on June 20 and 21, 2006, respectively. The merger deed was registered in the Madrid Mercantile Register on July 29, 2006, effective retrospectively, for financial purposes, from January 1, 2006. The effect of the merger on Telefónica, S.A.'s shareholders' equity was a 280 million euros decrease in Share premium.

b) Legal reserve

According to the revised text of the Spanish Corporation Law, companies must transfer 10% of profits for the year to a legal reserve until this reserve reaches the equivalent to at least 20% of share capital. The legal reserve can be used to increase capital by the amount exceeding 10% of the increased share capital. Except for this purpose, until the legal reserve exceeds the limit of 20% of capital, it can only be used to offset losses, if there are no other reserves available.

c) Revaluation reserves

The balance of Revaluation reserves arose as a result of revaluations made from 1946 to 1987 and of the revaluation carried out pursuant to Royal Decree-Law 7/1996, of June 7. The balance of the revaluation reserve may be used, without incurring taxes, to offset any losses from future years or to increase capital. From January 1, 2007, the reserve may also be transferred to unrestricted reserves, provided that the capital gain is recorded. This capital gain will be considered realized for the amount of depreciation recorded or when the revalued assets have either been sold or eliminated from the accounting records. In this respect, an amount of 1,178 million euros corresponding to reserves subsequently considered unrestricted has been reclassified under Other reserves.

d) Dividends

At its meeting of February 28, 2006, Telefónica, S.A.'s Board of Directors resolved to pay an interim dividend against 2005 profit of a gross 0.25 euros per share for each of the Company's outstanding shares carrying dividend rights. This dividend was paid on May 12, 2006, and the total amount paid was 1,169 million euros.

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At its meeting of September 27, 2006, Telefónica, S.A.'s Board of Directors resolved to pay an interim dividend against 2006 profit of a gross 0.30 euros per share for each of the Company's outstanding shares carrying dividend rights. This dividend was paid on November 10, 2006, and the total amount paid was 1,458 million euros.

At its meeting held on February 28, 2007, the Company's Board of Directors agreed to propose to the Shareholders Meeting the payment of a final dividend against 2006 profit of a gross 0.30 euros per share for each of the Company's outstanding shares carrying dividend rights. A total of 1,426 million euros was paid in May.

At its meeting of September 26, 2007, Telefónica, S.A.'s Board of Directors resolved to pay an interim dividend against 2007 profit of a fixed gross 0.35 euros for each of the Company's outstanding shares carrying dividend rights. This dividend was paid on November 14, 2007, and the total amount paid was 1,652 million euros.

In addition, at its meeting of February 27, 2008, the Company's Board of Directors agreed to submit for approval at the Shareholders Meeting the distribution of an additional dividend charged to 2007 profit of a fixed amount of 0.40 euros gross per outstanding share carrying dividend rights, up to a maximum total amount of 1,909 million euros (see Note 3).

(10) DEBENTURES, BONDS AND OTHER MARKETABLE SECURITIES

10.1 The balances and movements in this heading at December 31, 2007 and 2006 are the following:

	Millions of euros		
	Non-convertible Debentures and bonds	Other marketable debt securities	Total
Balance at 12/31/05	1,828	1,334	3,162
New issues		2,885	2,885
Redemptions		(2,188)	(2,188)
Adjustments and other movements	4	5	9
Balance at 12/31/06	1,832	2,036	3,868
New issues		1,096	1,096
Redemptions	(500)	(1,725)	(2,225)
Adjustments and other movements	5	11	16
Balance at 12/31/07	1,337	1,418	2,755
Maturity			
Long-term	916	181	1,097
Short-term	421	1,237	1,658
Accrued interest pending maturity	33		33

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10.2 The detail and main features of debentures and bonds outstanding at December 31, 2007 are as follows:

Debentures and bonds	Type of Interest rate	% interest rate	Maturity					Subsequent years	TOTAL	
			2008	2009	2010	2011	2012			
DEBENTURES										
FEBRUARY 1990 SERIES C	FIXED	12.60			4					4
FEBRUARY 1990 SERIES F	ZERO COUPON	12.58			12					12
APRIL 99	FIXED	4.50		500						500
JUNE 99	FLOATING	5.16		300						300
JULY 99	ZERO COUPON	6.37						50		50
MARCH 00	FLOATING	5.30(*)						50		50
BONDS										
MARCH 98	FIXED	4.84	421							421
Total issues			421	800	16				100	1,337

(*) The applicable interest rate (floating, set annually) is the sterling 10-year swap rate multiplied by 1.0225.

10.3 Zero-coupon debentures and bonds are recognized in the balance sheet at their issue value plus the related accrued interest.

The detail of the maturities and redemption values of these debentures and bonds is as follows:

			Present	Redemption
Issue	Redemption date	Redemption rate	value	value
DEBENTURES				
FEBRUARY 1990 SERIES F	02/26/2010	1,069.47%	12	15
JULY 99	07/21/2029	637.64%	50	191
Total			62	206

The remaining debentures and bonds have been stated at nominal value.

10.4

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At December 31, 2007, Telefónica, S.A. has a program of promissory note issues of up to 2,000 million euros. The outstanding balance at year end was 1,230 million euros.

With respect to the transaction with La Estrella, S.A. de Seguros consisting of the issuance of bearer promissory notes, on February 15, 2001 Telefónica, S.A. issued 74 bearer promissory notes with a face value of 126 million euros and final maturity in February 2011. The principal outstanding at year end was 80 million euros.

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In 2006, the Company acquired shares in O2 plc (see Note 7) payment for which was deferred through the arrangement of a 207 million pounds sterling (308 million euro) loan program. This program, enacted under UK law, gives the seller of the shares rights to of a security that pays semi-annual interest and the option to collect the principal on demand at the interest payment dates (June 30 and December 31) until December 31, 2010 when the program ends. The outstanding balance of the program at December 31, 2007 amounted to 79 million pounds sterling (108 million euros).

10.5 The average interest rate in 2007 on debentures and bonds outstanding during the year was 4.90% (4.83% in 2006), and the average interest rate on corporate promissory notes was 4.57% (3.50% in 2006).

(11) PAYABLE TO CREDIT INSTITUTIONS

11.1 The balances of this heading at December 31, 2007 and 2006 are the following:

Item	Millions of euros					
	2007			2006		
	Short-term	Long-term	Total	Short-term	Long-term	Total
Loans and credits	556	8,150	8,706	188	9,736	9,924
Foreign-currency loans and credits	51	285	336	57	1,019	1,076
Total	607	8,435	9,042	245	10,755	11,000

11.2 Maturities at December 31, 2007 are as follows:

Item	Maturity						Balance at 12/31/07
	2008	2009	2010	2011	2012	Subsequent years	
Loans and credits	556		862	6,058	39	1,191	8,706
Foreign-currency loans and credits	51	256	27			2	336
Total	607	256	889	6,058	39	1,193	9,042

11.3 On April 21, 2006, Telefónica S.A. arranged a 700 million euro syndicated loan, denominated in euros and bearing interest linked to the Euribor rate. This loan was fully drawn down at December 31, 2006, thus there were no movements in 2007. It will be repaid in two equal installments, due April 2015 and 2017, respectively.

On February 20, 2006, the Company repaid 556 million euros on the last installment of the syndicated loan. Banco Santander Central Hispano acted as agent bank. This loan had been taken out in 1999 with a number of financial institutions for a total of 1,200 million euros.

On June 28, 2005 Telefónica, S.A. arranged a syndicated loan with 40 national and international financial institutions for 6,000 million euros, maturing on June 28, 2011. The loan is denominated in euros and can be drawn either in this currency or in US dollars, sterling, yen, Swiss francs or any other currency subject to prior agreement by the banking institutions. At December 31, 2006, this loan had been fully drawn down, so there were no movements in 2007.

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On July 6, 2004, Telefónica arranged a 3,000 million euro syndicated loan with several Spanish and foreign banks. This loan matures in five years (July 6, 2009) and bears interest of Euribor/Libor plus a spread based on the Company's credit rating. The total balance drawn down at December 31, 2006 was 1,800 million euros and 1,152 million dollars. In 2007, the Company repaid 1,800 million euros and 850 million dollars, taking the total amount drawn down at December 31, 2007 to 302 million dollars.

On November 26, 2004, Telefónica, S.A. and several branches of ABN Amro Bank N.V. agreed to a credit facility, secured by the export credit agencies of Finland (Finnvera) and Sweden (EKN), bearing fixed interest of 3.26% and with final maturity on November 15, 2010. This financing is to cover up to 85% of the purchases of network equipment to be made by Telefónica Móviles Group companies from Ericsson and Nokia. In 2006, a total of 153 million dollars was drawn down, leaving a total sum available at December 31, 2006, of 266 million dollars. In 2007, a total of 75 million dollars was repaid, leaving an outstanding balance at December 31, 2007 of 191 million dollars.

11.4 Average interest on loans and credits

The average interest rate in 2007 on loans and credits denominated in euros was 4.41% (3.27% in 2006) and on foreign-currency loans and credits was 4.97% (5.45% in 2006).

11.5 Unused credit facilities

The Loans and credit balances relate only to amounts drawn down.

At December 31, 2007, Telefónica had undrawn credit facilities amounting to 5,779 million euros.

(12) PAYABLE TO GROUP AND ASSOCIATED COMPANIES

12.1 The breakdown of this heading at December 31, 2007 and 2006 is as follows:

	Millions of euros					
	2007		Total	2006		Total
	Long-term	Short-term		Long-term	Short-term	
Loans	32,372	17,284	49,656	35,427	10,861	46,288
Accounts payable to Group companies for purchases and services		108	108		91	91
Accounts payable to subsidiaries due to taxation on consolidated basis		616	616	891	964	1,855
Total	32,372	18,008	50,380	36,318	11,916	48,234

Total financing raised by Telefónica S.A. through Telefónica Europe, B.V. at December 31, 2007 amounted to 13,805 million euros (18,885 million euros at December 31, 2006). This financing is arranged by these companies through a number of loans, paying market rates of interest calculated on a Euribor plus spread basis. The average interest rate in 2007 was 5.62% (4.80% in 2006).

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This financing mainly derives from the syndicated multicurrency loan arranged between Telefónica Europe, B.V. and a group of financial institutions for an amount of up to 18,500 million pounds sterling at October 31, 2005 to fund the acquisition of O2 Plc (see Note 7.1.a), which at December 14, 2006 was reduced to 7,000 million pounds sterling, while the maturity was extended from 2008 to 2013. The outstanding balance on this loan at December 31, 2007 was 4,279 million pounds sterling (5,834 million euros).

Total financing raised by Telefónica, S.A. through Telefónica Emisiones, S.A.U. at December 31, 2007 amounted to 16,206 million euros (12,642 million euros at December 31, 2006). This financing is arranged as loans from these companies on the same terms as those of the issuance programs. The average interest rate in 2007 was 5.08% (5.09% in 2006). The financing arranged includes, as a related cost, the fees or premiums charged to the income statement for the period corresponding to the financing (see Note 8).

Telefónica Emisiones, S.A.U. raised financing mainly by tapping the European and US capital markets, issuing a total amount in 2007 of 1,929 million euros, 8,000 million Czech crowns (equivalent to 301 million euros) and 2,300 million US dollars (equivalent to 1,562 million euros). In 2006, issues totaled 6,050 million euros, 1,750 million pounds sterling (equivalent to 2,606 million euros at the 2006 year-end exchange rate) and 5,250 million dollars (equivalent to 3,986 million euros at the 2006 year-end exchange rate)

Meanwhile, as at December 31, 2007, Telefónica, S.A. had raised financing from Telefónica Finanzas, S.A., in charge of the integrated cash management of the companies comprising the Telefónica Group, amounting to 14,737 million euros (9,807 million euros at December 31, 2006) in a series of loans earning market interest rates.

There were also loans at December 31, 2007 to Telefónica, S.A. by Telefónica Móviles España, S.A.U. for 3,404 million euros (from the merger with Telefónica Móviles, S.A.) and from Telefónica de España, S.A.U. for 1,042 million euros (1,042 million euros at December 31, 2006).

Loans to Group companies includes accrued and unpaid interest at December 31, 2007 amounting to 685 million euros (475 million euros at December 31, 2006).

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12.2 The short-term accounts payable to Group companies for purchases and services are as follows:

	Millions of euros	
	2007	2006
Telefónica de España, S.A.U.	15	1
Telefónica de Contenidos, S.A.U.	11	11
Telefónica Móviles España, S.A.U.	3	6
Telefónica Móviles Argentina Holding, S.A.	4	11
Terra Lycos Intangibles, S.A.		14
Telefónica Investigación y Desarrollo, S.A.U.	27	11
Telefónica Gestión de Servicios Compartidos, S.A.U.	2	2
Telefónica Ingeniería de Seguridad, S.A.	3	8
Telefónica Internacional Wholesale Services, S.L.		5
Telefónica Soluciones de Informática y Comunicaciones, S.L.	16	5
Telefónica Servicios Audiovisuales, S.A.	4	
Telefónica Móviles Puerto Rico, Inc	4	
Other	19	17
Total	108	91

12.3 The balance of Accounts payable to subsidiaries due to taxation on a consolidated basis was 616 million euros at December 31, 2007 (1,855 million euros at December 31, 2006). This basically includes accounts payable to Group companies for their contribution of tax losses to the tax group headed by Telefónica, S.A. (see Note 14). The Company classifies this balance as short- or long-term on the basis of the projected maturity of the payments.

The main amounts are those relating to Telefónica Internacional, S.A. (423 million euros), Telefónica Móviles España, S.A.U. (65 million euros), Telefónica de Contenidos, S.A.U. (59 million euros) and Telefónica Data Corp, S.A.U. (42 million euros).

(13) DERIVATIVES

In 2007 the Company continued to use derivatives both to limit interest and exchange rate risks on otherwise unhedged positions and to adapt its debt structure to market conditions.

At December 31, 2007, the total outstanding balance of the derivatives portfolio was 78,089 million euros (68,078 million euros at December 31, 2006), of which 51,723 million euros related to interest rate risk and 26,366 million euros to exchange rate risk (48,968 million euros and 19,110 million euros, respectively, at December 31, 2006).

It should be noted that at December 31, 2007, Telefónica S.A. had arranged transactions with financial institutions to hedge interest and exchange rate risks for other Telefónica Group companies amounting to 532 million euros and 804 million euros, respectively (1,287 million euros and 3,072 million euros, respectively, at December 31, 2006). These external transactions are matched by parallel intragroup arrangements, with identical terms and maturities, and therefore involve no risk for Telefónica, S.A. External derivatives not backed by identical intragroup transactions consist of hedges on net investment and future acquisitions, that, by their nature, cannot be transferred to Group companies and/or transactions to hedge financing raised by Telefónica, S.A. as parent company of the Telefónica Group, which are transferred to Group subsidiaries in the form of financing rather than via derivative transactions.

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The breakdown of the portfolio by type of derivative at December 31, 2007, is the following:

Type of risk	Value in euros	Millions of euros 2007			
		Telefónica receives		Telefónica pays	
		Amount	Currency	Amount	Currency
Euro interest rate swaps	23,388				
Fixed to floating	13,319	13,319	EUR	13,319	EUR
Floating to fixed	7,677	7,677	EUR	7,677	EUR
Floating to floating	2,392	2,392	EUR	2,392	EUR
Foreign currency interest rate swap	13,641				
Fixed to floating	8,314				
GBP/GBP	954	700	GBP	700	GBP
USD/USD	7,269	10,700	USD	10,700	USD
JPY/JPY	91	15,000	JPY	15,000	JPY
Floating to fixed	3,282				
USD/USD	551	811	USD	811	USD
MXN/MXN	3	47	MXN	47	MXN
CZK/CZK	1,098	29,241	CZK	29,241	CZK
GBP/GBP	1,630	1,195	GBP	1,195	GBP
Floating to floating	2,045				
GBP/GBP	2,045	1,500	GBP	1,500	GBP
Exchange rate swaps	15,762				
Fixed to fixed	2,683				
EUR/CLP	183	176	EUR	134,106	CLP
USD/EUR	2,500	2,357	USD	2,500	EUR
Fixed to floating	336				
EUR/CLP	17	16	EUR	12,217	CLP
USD/EUR	224	200	USD	224	EUR
JPY/EUR	95	15,000	JPY	95	EUR
Floating to fixed	1,125				
EUR/BRL	111	112	EUR	288	BRL
EUR/MAD	88	90	EUR	1,000	MAD
USD/ARS	776	1,167	USD	3,598	ARS
USD/COP	116	149	USD	344,580	COP
USD/MXN	4	5	USD	58	MXN
USD/PEN	30	40	USD	132	PEN
Floating to floating	11,618				
EUR/CLP	15	14	EUR	10,646	CLP
EUR/CZK	1,289	1,150	EUR	34,321	CZK
EUR/GBP	4,084	4,460	EUR	2,995	GBP
EUR/USD	351	423	EUR	516	USD

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USD/EUR	5,692	7,233	USD	5,692	EUR
USD/MXN	9	14	USD	152	MXN
JPY/EUR	178	30,000	JPY	178	EUR
Forwards	8,467				
ARS/USD	81	385	ARS	119	USD
EUR/CZK	1,487	1,480	EUR	39,592	CZK
EUR/GBP	38	40	EUR	28	GBP
EUR/USD	1,319	1,356	EUR	1,941	USD
GBP/EUR	3,825	2,743	GBP	3,825	EUR
PEN/USD	10	47	PEN	15	USD
USD/BRL	74	106	USD	193	BRL
USD/COP	255	3,729	USD	755,732	COP
USD/EUR	755	1,105	USD	755	EUR
USD/MXN	447	650	USD	7,147	MXN
USD/PEN	7	10	USD	30	PEN
GBP/USD	46	34	GBP	67	USD
COP/USD	19	58,709	COP	29	USD
MXN/USD	104	1,665	MXN	153	USD
Subtotal	61,258				

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Notional amounts of structured products with options	EUR	Notional	
Interest rate options	14,694		
Caps & Floors	13,154		
External counterparties			
US DOLLAR	900	1,325	USD
EURO CURRENCY	9,732	9,732	EUR
GBP CURRENCY	2,522	1,850	GBP
Swaptions	1,540		
EURO CURRENCY	1,540	1,540	EUR
Currency options	2,137		
External counterparties			
USD/EUR	2,273	3,346	USD
USD/BRL	(136)	(200)	USD
Subtotal	16,831		
TOTAL	78,089		

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The detail of the portfolio by type of derivative at December 31, 2006 is as follows:

Type of risk	Value in euros	Millions of euros 2006			
		Telefónica receives Amount	Currency	Telefónica pays Amount	Currency
Euro interest rate swaps	24,997				
Fixed to floating	11,135	11,135	EUR	11,135	EUR
Floating to fixed	13,412	13,412	EUR	13,412	EUR
Floating to floating	450	450	EUR	450	EUR
Foreign currency interest rate swap	11,125				
Fixed to floating	7,503				
GBP/GBP	745	500	GBP	500	GBP
USD/USD	6,758	8,900	USD	8,900	USD
Floating to fixed	3,622				
USD/USD	661	871	USD	871	USD
MXN/MXN	56	803	MXN	803	MXN
CZK/CZK	976	26,841	CZK	26,841	CZK
GBP/GBP	1,929	1,295	GBP	1,295	GBP
Exchange rate swaps	12,247				
Fixed to fixed	2,822				
USD/EUR	2,560	2,433	USD	2,560	EUR
EUR/CLP	262	243	EUR	183,405	CLP
Fixed to floating	241				
EUR/CLP	17	16	EUR	12,217	CLP
USD/EUR	224	200	USD	224	EUR
Floating to fixed	1,234				
EUR/BRL	102	103	EUR	288	BRL
EUR/MAD	90	90	EUR	1,000	MAD
USD/ARS	653	860	USD	2,634	ARS
USD/COP	263	330	USD	776,005	COP
USD/MXN	11	15	USD	153	MXN
USD/PEN	115	146	USD	483	PEN
Floating to floating	7,950				
EUR/CLP	15	14	EUR	10,646	CLP
EUR/CZK	1,248	1,150	EUR	34,321	CZK
EUR/GBP	1,408	1,373	EUR	945	GBP
EUR/USD	540	587	EUR	711	USD
USD/EUR	4,664	5,830	USD	4,664	EUR
USD/MXN	75	105	USD	1,070	MXN
Forwards	6,335				

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EUR/USD	735	750	EUR	968	USD
USD/EUR	382	500	USD	382	EUR
EUR/CZK	601	589	EUR	16,522	CZK
EUR/GBP	1,689	1,676	EUR	1,134	GBP
GBP/EUR	1,975	1,333	GBP	1,975	EUR
USD/ARS	128	165	USD	516	ARS
ARS/USD	53	215	ARS	70	USD
USD/BRL	73	94	USD	206	BRL
BRL/USD	72	206	BRL	94	USD
USD/PEN	11	15	USD	48	PEN
PEN/USD	96	402	PEN	126	USD
USD/COP	93	119	USD	273,033	COP
USD/MXN	427	557	USD	6,114	MXN
Subtotal	54,704				

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Notional amounts of structured products with options	EUR	Notional	
Interest rate options	12,846		
Caps & Floors	12,767		
External counterparties			
US DOLLAR	1,006	1,325	USD
EURO CURRENCY	11,239	11,239	EUR
GBP CURRENCY	522	350	GBP
Swaptions	79		
EURO CURRENCY	79	79	EUR
Currency options	528		
External counterparties			
USD/EUR	398	525	USD
USD/ARS	130	171	USD
Subtotal	13,374		
TOTAL	68,078		

The detail by average maturity is as follows:

Hedged underlying item	Amount	Up to 1 year	2007	From 3 to 5 years	Over 5 years
			From 1 to 3 years		
Loans	21,819	10,394	4,428	4,757	2,240
In national currency	13,588	6,157	3,677	3,110	644
In foreign currencies	8,231	4,237	751	1,647	1,596
Debentures and MTN bonds	34,464	4,238	7,921	8,635	13,670
In national currency	11,082	4,238	3,143	3,584	117
In foreign currencies	23,382		4,778	5,051	13,553
Liabilities	21,806	12,980	658	4,389	3,779
Swaps	9,702	2,594	658	4,525	1,925
Currency options	1,540	1,540			
Interest rate options	2,137	419		(136)	1,854
Forward	8,427	8,427			
Total	78,089	27,612	13,007	17,781	19,689

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The hedged debentures and bonds relate to those issued by both Telefónica, S.A. and by Telefónica Europe, B.V.

The fair value of Telefónica, S.A.'s derivatives portfolio at December 31, 2007, was equivalent to a liability of 827 million euros (923 million euros at December 31, 2006). The detail by type of derivative is as follows:

	Millions of euros	
	2007	2006
Interest rate hedge (asset)	(402)	(254)
Exchange rate hedge (liability)	794	958
Interest and exchange rate hedge (liability)	435	219
Total liability	827	923

(14) 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. A total of 39 companies comprised the consolidated tax group in 2007.

On November 28, 2006, the Spanish Corporate Income Tax Law was amended to reduce the tax rate at that time (35%) to 32.5% for all years beginning on or after January 1, 2007 and to 30% for all years beginning on or after January 1, 2008.

This amendment reduces the tax on Spanish companies' profits, but also means less can be claimed back on tax loss carried forwards from previous years capitalized on the balance sheet.

Based on estimates of the taxable profit and the carrying value of deferred tax assets and liabilities on the balance sheet, the company quantified the impact of this change on the 2006 financial statements, recording a 58 million euro expense under Corporate income tax. Due to the changes in estimates made as a result of operations during the year, an additional charge of 39 million euros was recorded in 2007.

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14.1 Deferred tax assets and liabilities

The balance at December 31, 2007 and 2006 and movement in these headings is the following:

	Millions of euros		
	Deferred tax assets Long-term	Deferred tax liabilities Long-term	Inter-company deferred tax liabilities Long-term
Balance at December 31, 2005	55		43
Reversal	(135)		
Arising in the year	208	202	1
Merger with Telefónica Móviles, S.A.	459		1
Impact of change in corporate income tax rate	(47)	(29)	(6)
Balance at December 31, 2006	540	173	39
Reversal	(31)		
Arising in the year	164	162	2
Impact of change in corporate income tax rate	(47)	(12)	
Balance at December 31, 2007	626	323	41

Telefónica's deferred tax assets relate mainly to accounting provisions recorded for investments in companies with negative underlying book values.

The other inter-company timing differences relate to the effects of consolidated taxation.

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14.2 Tax payables and tax receivables

The balances of these headings at December 31, 2007 and 2006 are as follows:

	Millions of euros	
	Balance at 12/31/07	Balance at 12/31/06
Taxes payable:		
<i>Long-term tax payables:</i>	364	212
Deferred tax liabilities	364	212
<i>Short-term tax payables:</i>	27	27
Personal income tax withholdings	4	3
Withholding on investment income, VAT and other	22	23
Accrued social security taxes	1	1
	391	239
Tax receivables:		
<i>Long-term tax receivables: (Note 7)</i>	2,116	3,166
Deferred tax assets	626	540
Tax loss carryforwards	99	1,272
Deductions and other (Note 14.3)	1,391	1,354
<i>Short-term tax receivables:</i>	327	63
Tax loss carryforwards	283	
Withholdings	22	12
VAT and Canary Islands general indirect tax refundable	22	51
	2,443	3,229

At December 31, 2007 the tax Group had tax loss carryforwards pending application amounting to 3,382 million euros. Of this total, 187 million euros were generated in 2003 and 3,195 million euros in 2002. These losses must be applied within 15 years. The balance at December 31, 2007 includes tax credits carryforwards amounting to 382 million euros corresponding to tax losses of 1,245 million euros that have yet to be offset.

Unused tax loss carryforwards relate mainly to a negative adjustment made to the taxable base for corporate income tax on Telefónica Móviles, S.A. (now Telefónica, S.A.) in 2002 as a result of the transfer of certain holdings acquired in previous years where the market value differed from the book value at which they were recognized.

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14.3 Reconciliation of book profit to taxable income and calculation of corporate income tax charge and the net tax refundable.

The calculation of the corporate income tax charge and the net tax refundable for 2007 and 2006 is based on the following.

	Millions of euros	
	2007	2006
Book profit before taxes	5,178	7,001
Permanent differences	(9,728)	(7,165)
Timing differences		
Arising in the year	480	79
Arising in prior years	(566)	(386)
Tax base	(4,636)	(471)
Gross tax payable	(1,507)	(165)
Tax credits capitalized	(35)	(1,282)
Corporate income tax refundable	(1,542)	(1,447)
Timing differences	28	107
Corporate income tax accrued in Spain	(1,514)	(1,340)
Foreign taxes	33	10
Impact of change in tax rate	39	58
Adjustments to prior year's corporate income tax expense		(11)
Corporate income tax	(1,442)	(1,283)

The permanent differences relate mainly to changes in investment writedown provisions recorded by the tax group companies included in the consolidated corporate income tax return, to dividends received from tax group companies or foreign companies taxed at source and to the writedown provisions related to dividends paid by subsidiaries up to the amount of the dividend recorded as non-deductible income at Telefónica, S.A. and to non-deductible provisions.

In 2007, the Company recognized a tax benefit arising from the recognition of a higher tax loss carryforward amounting to 2,812 million euros generated on the disposal of the stake in Endemol Investment Holding, B.V. (see Note 7.1b) as a difference between the tax and book value of the Endemol shares at the time of disposal. The benefit recognized in Corporate income tax amounts to 914 million euros, presented in the table above under Permanent differences.

Also included under Permanent differences is the accounting gain on this disposal of 1,776 million euros (see Note 7.1.b).

In 2007, the Company capitalized 35 million euros of tax credits, mainly for double taxation. The cumulative amount relates mainly to tax credits in connection with export activity tax credits and tax credits related to the reinvestment of capital gains. In 2006, the deduction for reinvestment arising from the capital gain on the sale of the stake in Telefónica Publicidad e Información, S.A. (see Note 16.6) was 359 million euros, equivalent to 20% of the income subject to tax (1,793 million euros), from which the reversal was made in accordance with legislation through holdings acquired in 2005.

Taxes incurred abroad relate mainly to corporate income tax for the Company's permanent establishment in Argentina and tax withholdings abroad.

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14.4 On June 27, 2006, tax audits commenced at several 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 2001 to 2004), VAT, tax withholdings and payments on account in respect of personal income tax, tax on investment income, property tax and non-resident income tax (2002 to 2004). The inspections are not yet complete, but it is considered unlikely that the current actions of the tax authorities will give rise to significant additional liabilities.

In addition, the Company does not expect that any additional significant liabilities will arise from the other years open to inspection.

As a result of the tax inspection under way, Telefónica, S.A has open all tax years subsequent to 2002 for inspection of applicable taxes (except corporate income tax for 2001), as well as those for the last five years for all applicable taxes of its permanent establishment in Argentina.

Meanwhile, the courts have yet to rule on the appeal filed in relation to the assessments arising from the inspection of corporate income tax for the years 1998 to 2000. These assessments, which were signed in disagreement in October 2004 and July 2005, gave rise to settlement agreements and imposed fines on Telefónica, S.A. The total amount appealed is 140 million euros.

In April 2007, Telefónica, S.A. filed an administrative appeal before the National Court of Justice. The company also requested that the execution of the appealed settlements and penalties be suspended by providing the appropriate guarantees. On July 26, 2007 the lawsuit was formalized, with Telefónica, S.A. providing expert testimonies supporting its allegations. In December, the parties submitted the evidence on which their cases were based.

In relation to the sale by Terra Networks, S.A. (now Telefónica, S.A.) of its stake in Lycos Inc. in 2004, the Company began procedures to recognize a higher tax loss of up to 7,418 million euros because of measuring as acquisition value for tax purposes, the market value of Lycos Inc. shares received, rather than the book value at which they were recorded, in conformity with Article 159 of the Spanish Corporation Law. However, no accounting adjustments have been recorded until the Company receives a definitive ruling on this procedure.

(15) OTHER NON-TRADE PAYABLES

This heading consists of compensation payable and other payables relating mainly to the construction of the Telefónica Group's headquarters (see Note 6). It also includes provisions for commitments assumed that are due to be settled within the next 12 months.

Table of Contents**(16) REVENUES AND EXPENSES****16.1 Operating revenue**

In November 1990 Telefónica and Telefónica Argentina, S.A. entered into a management agreement which regulates the consultancy and advisory services provided by Telefónica and the price of such services. Revenues received for this concept in 2007 and 2006 totaled 15 million euros and 20 million euros, respectively, and are recorded under Net sales to Group companies.

Operating revenues also include income from property leases amounting to 31 million euros (9 million euros in 2006), mainly from the lease of office space in District C to several Telefónica Group companies (see Note 6).

Non-core and other current operating revenues Group companies relates to revenues on centralized services that Telefónica, S.A., as head of the Group, provides to its subsidiaries. Telefónica, S.A. bears the full cost of these services and then charges each individual subsidiary for the applicable portion. The amount mainly includes billings to Telefónica Móviles España, S.A.U. for 34 million euros (38 million euros in 2006) and to Telefónica de España, S.A.U. for 32 million euros (37 million euros in 2006).

16.2 Personnel expenses and employee benefits

The detail of Personnel expenses is as follows:

Concept	2007	2006
Wages and salaries	128	126
Pension plans (Note 4.g)	10	50
Social security costs, et al	18	21
Total	156	197

Telefónica has reached an agreement with its staff to provide an Occupational Pension Plan pursuant to Legislative Royal Decree 1/2002, of November 29, approving the revised Pension Plans and Funds Law. The features of this Plan are as follows:

Defined contribution of 4.51% of the participating employees base salary. The defined contributions of employees transferred to Telefónica from other Group companies with different defined contributions (e.g. 6.87% in the case of Telefónica de España) will be maintained.

Mandatory contribution by participants of a minimum of 2.2% of their base salary.

Individual and financial capitalization systems.

This fund was outsourced to Telefónica subsidiary, Fonditel Entidad Gestora de Fondos de Pensiones, S.A., which has added the pension fund assets to its Fonditel B fund.

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At December 31, 2007 and 2006, 795 and 782 employees, respectively, have signed up for the plan. The cost for the Company amounted to 2.87 million euros and 2.70 million euros in 2007 and 2006, respectively.

In 2006, a Pension Plan for Senior Executives, wholly funded by the Company, was created and complements the previous plan and involves additional defined contributions at a certain percentage of the executive's fixed remuneration, based on professional category, plus some extraordinary contributions depending on the circumstances of each executive, payable in accordance with the terms of the Plan.

Telefónica, S.A. has recorded costs related to the contributions to this executive plan of 6 million euros in 2007 (6 million euros in 2006). In 2006, it also recorded an expense of 39 million euros for extraordinary contributions. No provision was made for this plan as the funds are held in external funds.

Compensation systems linked to the share price

a) Telefónica S.A. share plan: Performance Share Plan

At the Shareholders' Meeting of Telefónica S.A. on June 21, 2006, shareholders approved the introduction of a long-term incentive plan for managers and senior executives of Telefónica, S.A. and other Telefónica Group companies. Under this plan, selected participants who met the qualifying requirements were given a certain number of Telefónica, S.A. shares as a form of variable remuneration.

The Plan is initially intended to last seven years. It is divided into five cycles or phases, each three years long, beginning on July 1 (the Start Date) and ending on June 30 three years later (the End Date). At the start of each phase the number of shares to be awarded to Plan beneficiaries is determined based on their success in meeting targets set. The shares are delivered, assuming targets are met, at the End Date of each phase. Each phase is independent from the others. The first started on July 1, 2006 (with shares to be delivered, if targets are met, from July 1, 2009) and the fifth phase begins on July 1, 2010 (with any shares earned delivered from July 1, 2013).

Award of the shares is subject to a number of conditions:

The beneficiary must continue to work for the company throughout the three years of the phase, subject to certain special conditions related to departures.

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The actual number of shares awarded at the end of each phase will depend on success in meeting targets and the maximum number of shares assigned to each executive. Success is measured by comparing the total shareholder return (TSR), which includes both share price and dividends offered by Telefónica shares, with the TSRs offered by a basket of listed telecoms companies that comprise the comparison group. Each employee who is a member of the plan is assigned at the start of each phase a maximum number of shares. The actual number of shares awarded at the end of the phase is calculated by multiplying this maximum number by a percentage reflecting their success at the date in question. This will be 100% if the TSR of Telefónica is equal to or better than that of the third quartile of the Comparison Group and 30% if Telefónica's TSR is in line with the average. The percentage rises linearly for all points between these two benchmarks. If the TSR is below average there will be no delivery.

The maximum number of shares assigned to Telefónica, S.A. senior executives in 2007 was 1,102,711 (1,275,552 shares in 2006). The average remaining vesting period on these shares at December 31, 2007, was two years.

When each phase matures, it is Telefónica, S.A. that is responsible for delivering the appropriate number of shares, determined as described above, to all the senior managers of Telefónica Group taking part in the plan. The share of the costs attributable to other Group companies, which employ the executives in the plan, will be recovered from these companies.

The Company therefore recorded a 4.7 million euro provision against personnel expenses in 2007 (1.6 million in 2006 for the period between the launch of the plan and year end).

To ensure the company had enough shares to meet its obligations at the end of the phase begun in 2006, Telefónica bought an instrument from a financial institution that will deliver to Telefónica, at the end of the phase, a number of shares determined using the same measure of success as the Plan, i.e. an instrument that mirrors the features of the plan. The cost of this instrument was 46 million euros (see Note 7.7), which in unit terms is 6.43 euros for each maximum number of shares for the Telefónica Group companies included in the plan. This value is consistent with the estimate of the cost of the phase begun in July 2006.

b) Terra Networks, S.A. (now Telefónica, S.A.) share option plan

The Terra Networks, S.A. share option plan was approved at the Shareholders' 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 share options by their holders, for the ownership by the employees and executives of the Terra-Lycos Group companies of a portion of the capital of Terra Networks, S.A. up to a maximum of 14,000,000 shares of Terra Networks, S.A.

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As a result of the Telefónica, S.A. and Terra Networks, S.A. merger approved at the General Shareholders meeting held on May 31, 2005 and recorded in the Madrid Mercantile Register on July 16, 2005, Telefónica, S.A. took over responsibility for Terra Networks, S.A.'s outstanding share option plans.

Consequently, the options on Terra Networks, S.A. shares were automatically converted into options on Telefónica, S.A. shares at the exchange ratio used in the merger.

At December 31, 2007 all options outstanding were cancelled.

The movements in 2007 and 2006 are as follows:

	Number of options	Average strike price
Options outstanding at December 31, 2005	117,900	28.28
Options granted	13,278	22.70
Options expired/cancelled	(78,067)	31.12
Options outstanding at December 31, 2006	53,111	22.70
Options granted		
Options expired/cancelled	(53,111)	22.70
Options outstanding at December 31, 2007		

c) Share option plan of Terra Networks, S.A. (now of Telefónica, S.A.) resulting from the assumption of Lycos, Inc.'s share option plan

Under the agreements entered into for the acquisition of Lycos, Inc., 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, a resolution was passed at the Shareholders Meeting of Terra Networks, S.A. to take over Lycos, Inc.'s share option plan.

At the time of the sale of all the shares in Lycos, Inc. in 2004, it was agreed that Terra Networks, S.A. would remain responsible for the obligations arising from share options on Terra Networks, S.A. shares to beneficiaries of Lycos, Inc. although Lycos, Inc. could carry out, on behalf of and at the expense of Terra Networks, S.A. whatever actions were necessary or convenient in relation to the exercise of the options by the beneficiaries.

After the merger of Terra Networks, S.A. into Telefónica, S.A., these options became options on Telefónica, S.A. shares.

At December 31, 2007, employees of Lycos, Inc. had been assigned options on 93,269 shares, at a post-merger weighted average strike price of 68.18 USD.

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The movements in 2007 and 2006 are as follows:

	Number of options	Average exercise price (USD)	Average share price (USD)
Options outstanding at December 31, 2005	527,425	59.57	
Options exercised	(124,974)	14.37	15.68
Options expired/cancelled	(287,204)	76.15	
Options outstanding at December 31, 2006	115,247	67.26	
Options exercised			
Options expired/cancelled	(21,978)	63.38	
Options outstanding at December 31, 2007	93,269	68.18	

The detail of options outstanding at December 31, 2007 is as follows:

	Number of options outstanding	Average exercise price (USD)	Average Remaining term to maturity (years)
Range of strike prices (USD)			
54.90 - 68.90	72,682	58.25	2.30
74.65 - 136.13	20,587	103.22	1.74
Options outstanding at December 31, 2007	93,269	68.18	2.17

16.3 Average number of employees

Category	2007	2006
University graduates and other line personnel	631	722
Junior college graduates and technicians (draftsmen)	6	5
Supervisors, data processing and other assistants	174	189
Total	811	916

The total number of employees at December 31, 2007 was 797 (792 at December 31, 2006). The number of employees from Telefónica Móviles, S.A. who joined the Company in 2006 was 91.

The breakdown of average staff in 2007 by sex showed 425 women and 386 men, with 423 women and 374 men at December 31, 2007 (412 and 380, respectively at December 31, 2006). The breakdown by sex and category at December 31, 2007 is as follows:

Category	Women	Men	Total
University graduates and other line personnel	262	358	620
Junior college graduates and technicians (draftsmen)	4	2	6
Supervisors, data processing and other assistants	157	14	171
Total	423	374	797

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16.4 Other finance costs for debt and similar expenses and revenues from other equity investments and loans

The detail of these headings is as follows:

	2007	2006
Issues	131	135
Euro loans and credits	1,667	1,313
Foreign currency loans and credits	1,328	1,275
Total finance costs on debt and similar expenses	3,126	2,723
Interest on loans to subsidiaries and associated companies (Note 16.8)	1,002	1,033
On long-term investments in other companies	156	88
Revenues from financial derivatives	7	10
Total revenues from other equity investments and loans	1,165	1,131

2,585 million euros and 2,149 million euros of the expenses related to interest on debts to Group companies in 2007 and 2006, respectively (see Note 16.8).

16.5 Exchange rate differences

The detail of exchange losses charged against income was as follows:

	2007	2006
Amortization of loans maturing in the year	9	57
Current operations and derivatives	1,184	974
Total	1,193	1,031

The detail of exchange gains taken to income is as follows:

	2007	2006
Amortization of loans maturing in the year	57	39
Current operations and derivatives	1,914	996
Total	1,971	1,035

The change in exchange gains and exchange losses in 2007 with respect to 2006 was due mainly to fluctuations in the US dollar/euro exchange rate (the dollar lost 10.54% in 2007 and 10.43% in 2006) and in the pound sterling/euro exchange (the euro appreciated 8.43% after depreciating 2.06% in 2006), which was offset by the effect of hedges arranged for this purpose.

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16.6 Extraordinary income

This heading in the income statement relates to non-recurring revenues obtained by the Company during the year. The detail is as follows:

	2007	2006
Gains on disposal of assets	1,785	1,872
Gains on transactions with treasury shares (see Note 9.a)	23	48
Reversal of provisions for negative book value of investees		70
Reversal of provisions for treasury shares charged against income (see Note 9.a)		38
Other extraordinary income	1	44
Total	1,809	2,072

Gains on disposal of assets in 2007 mainly includes the gain on the sale of 99.7% of Endemol Investment Holding, B.V. amounting to 1,776 million euros (see Note 7.1.b).

In 2006, this heading mainly included the 1,834 million euro gain on the disposal of Telefónica Publicidad e Información, S.A. (see Note 7.1.b), and the 10 million euro gain on the sale of 590,656 Sogecable, S.A. shares (see Note 7.1.b). It also included the 7 million euro gain on the disposal of property, plant and equipment (see Note 6).

In 2006, 70 million euros was reversed from provisions for liabilities and charges in respect of the negative book value on Group investee companies (see Note 7.3).

16.7 Extraordinary expenses

The detail of extraordinary expenses was as follows:

	2007	2006
Provisions for negative book value of investees	440	
Losses on disposal of fixed assets	4	2
Losses on transactions with own shares (see Note 9)		1
Other extraordinary expenses	36	5
Total	480	8

In 2007, a credit for 440 million euros was allocated to Provisions for liabilities and charges in respect of the negative book value on Group investee companies (see Note 7.3).

16.8 Transactions with Group companies

Telefónica's main transactions with Group companies in 2007 and 2006 are as follows:

	2007	2006
Dividends received	15,099	6,678
Accrued interest	1,002	1,033
Financial expenses (Note 16.4)	2,585	2,149
Acquisitions of goods and services from Telefónica Group companies	69	80

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On December 20, 2007, Telefónica O2 Europe Plc (formerly O2 Plc) paid Telefónica, S.A. a dividend in kind entailing the transfer of 100% of the shares it held of O2 Europe Ltd., valued at 8,500 million euros (see Note 7.1.a). On the same date, Telefónica O2 Europe Plc resolved to pay Telefónica, S.A. an interim dividend charged against 2007 for 2,000 million pounds sterling (equivalent to 2,772 million euros) to be paid in the first quarter of 2008.

Dividends received in 2007 include the following: 1,363 million euros from Telefónica de España, S.A.U. (1,369 million euros in 2006), Telefónica Móviles España for 1,625 million euros (1,781 million euros in 2006), Telefónica O2 Czech Republic, a.s. for 397 million euros (354 million euros in 2006) and Latin America Cellular Holdings, B.V. for 403 million euros. In 2006, 2,988 million euros of dividends were received from Telefónica Internacional, S.A. and 183 million euros from Telcel, C.A.

Accrued interest in 2007 on financing granted to Group companies (see Note 7.6) included 293 million euros (336 million euros in 2006) on loans to Telefónica de España, S.A.U., 266 million euros (251 million euros in 2006) on loans to Telefónica Móviles México, S.A. de C.V., 220 million euros (223 million euros in 2006) on loans to Telefónica Móviles España, S.A.U. and 91 million euros (90 million euros in 2006) on the loans granted to Telefónica de Contenidos, S.A.U.

Total financial expenses in 2007 on financing received from Group companies (see Note 12) included 890 million euros to Telefónica Europe, B.V. (1,131 million euros in 2006), 773 million euros to Telefónica Emisiones, S.A. (409 million euros in 2006), 696 million euros to Telefónica Finanzas, S.A.U. (432 million euros in 2006) and 161 million euros to Telefónica Móviles España, S.A.U. (119 million euros in 2006).

16.9 Revenue from equity investments in associated companies

Revenue from equity investments in associated companies mainly relate to dividends received from the Telefónica, S.A.'s investment in Portugal Telecom, which amounted to 207 million euros in 2007 (47 million euros in 2006), of which 160 million euros correspond to shares of PT Multimedia, S.G.P.S., S.A. received as a dividend in kind (see Note 7.1.a).

(17) OTHER INFORMATION

a) Financial guarantees

At December 31, 2007 Telefónica, S.A. had provided guarantees for its subsidiaries and investees to secure their transactions with third parties (see Note 12.1) amounting to 31,973 million euros (33,722 million euros at December 31, 2006).

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The main guarantees provided are for:

Telefónica Emisiones, S.A.U., with an outstanding nominal value equivalent to 15,795 million euros, for outstanding bonds and debentures, of which the equivalent of 3,792 million euros was issued in 2007.

Telefónica Europe, B.V., with an outstanding nominal value of 4,729 million euros for bonds and debentures (30,000 million yen equivalent to 182 million euros issued in 2007) and 4,221 million pounds sterling (equivalent to 5,755 million euros) for the outstanding balance on the syndicated loan arranged by Telefónica Europe, B.V. to finance the acquisition of O2 shares.

The preferred shares issued by Telefónica Finanzas USA, LLC in December 2002 totaling 2,000 million euros.

Telefónica Finanzas, S.A. related to financing from the European Investment Bank, which at December 31, 2007 amounted to the equivalent of 1,305 million euros.

The peso bonds issued by Telefónica Finanzas México, S.A. de C.V., with an outstanding balance of 11,500 million Mexican pesos (equivalent to 719 million euros at the 2007 year-end exchange rate).

No significant losses are expected to arise for the Company in connection with these commitments.

b) Litigation

Telefónica, S.A. and its group companies are party to several lawsuits that are currently before the courts and the arbitration bodies of the various countries in which the Telefónica group is present.

Based on the reports of the Company's legal counsel, it is reasonable to assume that this litigation will not significantly affect the financial position or solvency of Telefónica, S.A., even in the event the company should lose. We highlight the following unresolved cases:

1) Procedures deriving from bankruptcy proceeding of Sistemas e Instalaciones de Telecomunicación, S.A.U. (Sintel).

Sintel, a former subsidiary of Telefónica, was declared bankrupt in 2001. As a result of the voluntary bankruptcy proceeding heard by Madrid Court of First Instance no. 42 (case 417/2001), two criminal proceedings commenced which affect Telefónica.

Abbreviated proceeding no. 273/2001 being heard before Central Examining Court no. 1, in relation to which, on September 24, 2002, Telefónica, S.A. and Telefónica de España, S.A. filed a civil suit for damages against the directors of Sintel and of Mastec Internacional, S.A.

Preliminary proceeding no. 362/2002, before Central Examining Court no. 1 for a possible offence of extortion. This proceeding was subsequently assimilated to the preliminary proceedings in case no. 273/2001 above.

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The two proceedings were combined, in April 2004, the motion filed by counsel for Telefónica, S.A. to have the case dismissed was rejected and it was ruled that the preliminary proceedings should continue. So far no liability has been established and the plaintiffs' claim in this regard has been explicitly dismissed.

In its judgment of December 12, 2007, Examining Court no. 1 changed into an Abbreviated proceeding the suit for bankruptcy due to criminal negligence and against the Spanish Treasury, charging those responsible, managers and directors of Sintel, S.A. long after the sale of the company by Telefónica.

2) Contentious proceedings in connection with the takeover bid for Terra Networks, S.A. and its subsequent merger with Telefónica

Proceedings derived from the takeover bid

On May 29, 2003, certain Terra Networks, S.A. shareholders filed two class actions with the Supreme Court of New York State against Telefónica, Terra Networks, S.A. and certain directors of Terra Networks, S.A.

Both actions alleged mainly that the takeover bid by Telefónica was the result of non-compliance with the fiduciary commitments of this company, and of the Board of Directors of Terra Networks, S.A. Since the actions were brought, both have remained virtually inactive.

The World Association of Shareholders of Terra Networks, S.A. (ACCTER) filed an appeal for judicial review No. 6/461/03 at the National Appellate Court -Telefónica appears as an intervening non-party- against the ruling of June 19, 2003 by the Spanish National Securities Market Commission (CNMV) authorizing the takeover offer by Telefónica, S.A. for Terra Networks.

The appeal was rejected by the National Appellate Court via ruling issued January 27, 2006, against which ACCTER filed an administrative appeal. The Third Section of the Supreme Court has yet to rule on the admissibility of this appeal.

Proceedings derived from the merger

On June 30, 2005, ACCTER and its President, on his own account, filed a complaint contesting the merger resolution adopted at the Shareholders' Meeting of Terra Networks, S.A. of June 2, 2005.

The Court of First Instance rejected the claim and the plaintiffs filed an appeal which has yet to be resolved.

On September 26, 2006, Telefónica and one of its directors were notified of the claim filed by former shareholders of Terra Networks, S.A. (Campoaguas, S.L., Panabeni, S.L. and others) alleging breach of contract by Telefónica with the shareholders of Terra in respect of the terms and conditions set forth in the Prospectus of the Initial Public Offering of shares of Terra Networks, S.A. The court date has been set for July 19, 2008.

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3) Claim at the ICSID

As a result of the enactment by the Argentine government of Public Emergency and Exchange Rules Reform Law 25561, of January 6, 2002, Telefónica considered that the terms and conditions of the Share Transfer Agreement approved by Decree 2332/90 and the Pricing Agreement ratified by Decree 2585/91, both of which were executed by the Company with the Argentine government, were affected appreciably, since the Law renders ineffective any dollar or other foreign currency adjustment clauses, or indexation clauses based on price indexes of other countries, or any other indexation mechanism in contracts with the public authorities. The law also required that prices and rates derived from such clauses be denominated in pesos at an exchange rate of one peso (ARS 1) to one US dollar (US\$1).

Accordingly, since negotiations with the Argentine Government were unsuccessful, on May 14, 2003, Telefónica filed a request for arbitration with the International Center for Settlement of Investment Disputes (ICSID) pursuant to the Agreement for the Promotion and Reciprocal Protection of Investments between the Argentine Republic and the Kingdom of Spain. On July 6, 2004, the first hearing at the ICSID took place in Washington and a 90-day stay was ordered in an attempt to reach a settlement. Following the expiration of the stay without any settlement having been achieved, on December 6, 2004, Telefónica filed the memorial or claim with the ICSID together with the initial supporting testimonies. The Court is currently considering a plea filed by the Argentine government alleging that the matter is outside the jurisdiction of the arbitration court.

On February 15, 2006, Telefónica Argentina signed a memorandum of understanding with the Argentine government as a prerequisite to reaching an agreement to renegotiate the transfer contract approved by Royal Decree-Law 2332/90 pursuant to the provisions of Article 9° of Law 25,561.

Among other issues, this memorandum of understanding envisaged the suspension by Telefónica de Argentina, S.A. and Telefónica, S.A., for a period of 210 working days, of proceedings for all claims, appeals and demands planned or underway, with the administrative, arbitrational or legal courts of Argentina or abroad, which were based on events or measures taken as a result of the emergency situation established by Law N° 25,561 with regard the Transfer Agreement and the license granted to the Company. The suspension came into force on October 6, 2006.

This preliminary agreement could put an end to the litigation.

As the initial stay expired, Telefónica requested a six-month extension starting October 5, 2007 which the Argentina government did not oppose. The courts agreed to extend the stay.

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4) Appeal against the European Commission ruling of July 4, 2007 against Telefónica de España, S.A.U. s broadband pricing policy.

On February 22, 2006, Telefónica S.A. was sent a statement of objections, initiating disciplinary proceedings for conduct that goes against Article 82 of EC Treaty rules. Subsequently, on July 9, 2007, the European Commission issued a decision, imposing a 152 million euro fine on Telefónica and Telefónica de España, S.A.U. The ruling charged Telefónica with applying a margin squeeze between the prices it charged competitors to provide regional and national wholesale broadband services and its retail broadband prices using ADSL technology between September 2001 and December 2006. Telefónica de España and Telefónica both filed appeals to overturn the decision before the Court of First Instance of the European Communities. The Kingdom of Spain also lodged an appeal to overturn the decision.

5) Appeal for judicial review against the ruling of the Central Economic-Administrative Tribunal dated February 15, 2007 rejecting several economic-administrative claims filed by Telefónica against assessments from the National Inspection Office of the Spanish Treasury related to consolidated taxes in 1998, 1999 and 2000 (see Note 14).

c) *Commitments*

Agreements with Portugal Telecom (Brazil).

On January 23, 2001, Telefónica, S.A. and its subsidiary Telefónica Móviles, S.A. (merged with Telefónica, S.A. in 2006, see Note 1), and Portugal Telecom S.G.P.S., S.A. and its subsidiary PT Móveis, S.G.P.S., S.A. agreed to combine all their wireless telephony businesses in Brazil. They therefore undertook to contribute all their wireless telephony assets in Brazil to a joint venture, which, subject to the necessary regulatory authorizations, would be a subsidiary of the two groups, and in which they would each have a 50% ownership interest. In addition, under the terms of this agreement, the two parties expressed their interest in increasing their reciprocal ownership interests, subject to compliance with the applicable regulations and bylaws.

On October 17, 2002, Telefónica Móviles, S.A., and Portugal Telecom S.G.P.S., S.A. and its subsidiary PT Móveis S.G.P.S., S.A. entered into the definitive agreements (Shareholders 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, 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 ownership of either of the parties falls below 40% during an uninterrupted period of six months. In this event, Brasilcel N.V.'s governing bodies would deliberate with a simple majority. As for the quorum required to hold the Shareholders Meeting, attendance by shareholders representing the majority of share capital would suffice.

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Also, in accordance with the definitive agreements, the Portugal Telecom Group will be entitled to sell to Telefónica, 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., or at any other subsidiary of the latter that held a direct or indirect ownership interest in Brasilcel N.V. Similarly, Telefónica, S.A. will be entitled to sell to the Portugal Telecom Group, which will be obliged to buy, its holding in Brasilcel, N.V. if there is a change of control at Portugal Telecom S.G.P.S., S.A., at PT Móveis S.G.P.S., S.A or at 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 put option, in cash or in shares of the wireless telephony operators contributed by the related party, making up the difference, if any, in cash.

d) Directors compensation and other benefits

The compensation of Telefónica, S.A.'s directors is governed by Article 28 of the bylaws, which states that the compensation paid by the Company to its directors shall be determined at the General Shareholders Meeting and shall remain in force until a resolution is adopted at the Shareholders Meeting to amend it. The Board of Directors is responsible for setting the exact amount to be paid within the stipulated limits and distributing it among the directors. On April 11, 2003, shareholders set the maximum gross annual amount to be paid to the Board of Directors at 6 million euros. This includes a fixed payment and fees for attending meetings of the Board of Directors advisory or control committees.

Therefore, the compensation of Telefónica's directors in their capacity as members of the Board of Directors and/or of the Standing Committee and the advisory and control committees consists of a fixed amount payable monthly plus fees for attending the meetings of the Board's advisory or control committees. It should be noted that a resolution has been adopted whereby from September 2007, executive directors will not receive the fixed amounts established for their membership of the Board of Directors and Standing Committee, but only the corresponding amounts for discharging their executive duties as stipulated in their respective contracts.

In 2007, the members of the Board of Directors of Telefónica, S.A. earned the following total compensation for discharging their duties as such: fixed payments of 3,704,333 euros and attendance fees of 211,250 euros for attending the Board of Directors advisory committee meetings. It should also be noted that the compensation paid to Company directors sitting on the Boards of other Telefónica Group companies amounted to 405,192 euros. In addition, the six Company directors who are members of the Catalonia, Andalusia and Valencia advisory committees received a total 73,750 euros in 2007.

In addition, in their capacity as company executives, the executive directors César Alierta Izuel, Julio Linares López, José María Álvarez-Pallete López, Peter Erskine (who stepped down from his executive duties on December 31, 2007) and Antonio Viana-Baptista (who stepped down from his executive duties on January 31, 2008) received: 12,368,727 euros in salaries and variable compensation; 33,018 euros in contributions made to Company-sponsored pension plans and 126,302 euros of compensation in kind, which included other insurances (general medical and dental insurance), as well as life insurance premiums.

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In addition, it should be noted that Peter Erskine received the following amounts: (i) 615,283 euros as periodic payment in cash relating to the commitments previously acquired by O2 plc in connection with his pension plan, this item set forth in the Document containing the Tender offer, (ii) 3,838,077 euros under the 2005 O2 Share Plan, which was likewise set forth in the Document containing the Tender offer, and (iii) in accordance with the conditions of O2 acquisition, 24,331,831 euros for stepping down from his executive duties, broken down as follows: variable compensation for 2007, a payment for the advance notice clause in his employment contract, a payment for his employment commitment in accordance with the terms of the Framework Agreement signed in relation to the takeover bid for O2 plc shares and the payment of the obligations acquired at the time by O2 plc regarding pension plans, this concept was included likewise in the takeover document. The bulk of this last payment was made in 2007, with the remainder paid in January 2008.

In order to make this information more transparent and easier to understand, the following table present the detail by concept, remuneration and benefits (in euros) paid to Telefónica directors in 2007:

Director	Board of Directors	Standing Committee	Board Committees		TOTAL
			Fixed compensation	Attendance fees	
Chairman					
César Alierta Izuel	290,000	96,667	0	0	386,667
Vice chairmen					
Isidro Fainé Casas	241,667	96,667	0	0	338,334
Gregorio Villalabeitia Galarraga ⁽¹⁾	137,500	55,000	22,500	20,000	235,000
Vitalino Manuel Nafría Aznar	186,667	0	7,000	3,750	197,417
Members					
Julio Linares López	95,000	63,333	8,667	7,500	174,500
José María Abril Pérez ⁽²⁾	62,500	41,667	3,500	1,250	108,917
José Fernando de Almansa					
Moreno-Barreda	145,000	0	40,000	20,000	205,000
José María Álvarez-Pallete López	95,000	0	0	0	95,000
David Arculus	145,000	0	0	0	145,000
Maximino Carpio García ⁽³⁾	145,000	96,667	40,833	26,250	308,750
Carlos Colomer Casellas	145,000	96,667	13,333	2,500	257,500
Peter Erskine	95,000	63,333	0	0	158,333
Alfonso Ferrari Herrero	145,000	0	60,333	26,250	231,583
Gonzalo Hinojosa Fernández de Angulo	145,000	0	73,667	35,000	253,667
Pablo Isla Álvarez de Tejera	145,000	0	50,500	17,500	213,000
Antonio Massanell Lavilla	145,000	0	47,000	23,750	215,750
Enrique Used Aznar ⁽⁴⁾	145,000	0	60,333	27,500	232,833
Antonio Viana-Baptista	95,000	63,333	0	0	158,333

(1) Gregorio Villalabeitia Galarraga was a director of Telefónica until July 25, 2007, being replaced as Vicechairman by Vitalino Nafría Aznar.

- (2) José María
Abril Pérez was
appointed direct
of Telefónica on
July 25, 2007.
- (3) Maximino
Carpio García
was a director of
Telefónica until
December 19,
2007.
- (4) Enrique Used
Aznar was a
director of
Telefónica until
December 19,
2007.

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For a better understanding of the information provided above, the following table presents the amounts established for fixed compensation and attendance fees, where appropriate, of the Board of Directors, Standing and Advisory or Control Committees.

Board of Directors. Fixed payment for each director (euros):

Position	2007
Chairman	290,000
Vice chairmen	241,667
Directors:	
Executives	95,000
Non-independent external directors	145,000
Independent external directors	145,000
Other external directors	145,000

Directors do not receive any attendance fees for attending Board and Standing Committee meetings.

Standing Committee. Fixed payment for each director forming part of the Standing Committee, by position (euros):

Position	2007
Chairman	96,667
Deputy Chairman	96,667
Members	96,667

Directors do not receive any attendance fees for attending Board and Standing Committee meetings.

Other Board committees.

Fixed payment for each director forming part of one of the Board committees, by position (euros):

Position	2007
Chairman	26,667
Members	13,333

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Total fees paid to directors in 2007 for attending meetings of the advisory or control committees (euros):

Committee	2007
Audit and Control	Attendance fee per meeting: 1,250 Number of meetings paid: 11
Appointments, Compensation, and Good Governance	Attendance fee per meeting: 1,250 Number of meetings paid: 10
Human Resources, Reputation and Corporate Responsibility	Attendance fee per meeting: 1,250 Number of meetings paid: 4
Regulation	Attendance fee per meeting: 1,250 Number of meetings paid: 11
Service Quality and Customer Service	Attendance fee per meeting: 1,250 Number of meetings paid: 4
International Affairs	Attendance fee per meeting: 1,250 Number of meetings paid: 5

In addition, the total compensation paid to César Alierta Izuel, Julio Linares López, José María Álvarez-Pallete López, Peter Erskine and Antonio Viana-Baptista for discharging their executive duties by component (in euros) is as follows:

Component	2007
Salary ⁽¹⁾	5,688,154
Variable compensation ⁽²⁾	6,680,573
Compensation in kind	126,302
Contributions to pension plans	33,018

(1) It is stated for the record that in addition, Mr. Peter Erskine received the amount of 615,283 euros as periodic payment in cash relating to the commitments previously acquired by O2 plc. in connection with his pension plan, this item set forth in the Document containing the Tender offer.

(2) In addition, it is stated, for the

record, that
Mr. Peter
Erskine received
the following
amounts: (i) in
accordance with
the conditions
of O2
acquisition,
24,331,831
euros for
relinquishing his
status as a
Company
executive under
the terms
indicated above,
and
(ii) 3,838,077
euros under the
2005 O2 Share
Plan, which was
likewise set
forth in the
Document
containing the
Tender offer.

In addition, related to the Performance Share Plan authorized at the General Shareholders Meeting of June 21, 2006 (see Note 20), the maximum number of shares corresponding to the first and second phases of the Plan will be given (on July 1, 2009 and July 1, 2010) to each of the executive directors of Telefónica, S.A. if all the terms established for such delivery are met, is as follows: César Alierta Izuel (129,183 shares in the first phase and 116,239 shares in the second); Julio Linares López (65,472 and 57,437 shares, respectively); José María Álvarez-Pallete López (62,354 and 53,204 shares, respectively); Antonio Viana-Baptista (62,354 and 53,204 shares, respectively). With respect to Peter Erskine (who was allocated 181,762 shares in the first phase and 151,863 shares in the second), he will receive, within the first three months of the year, the number of shares he is entitled to, if any, based on the period of each phase during which he was an executive of the Telefónica Group.

It should be noted that the non-executive directors do not receive and did not receive in 2007 any compensation in the form of pensions or life insurance, and they do not participate in the compensation plans linked to the market share price.

In addition, the Company does not grant and did not grant in 2007 any advances, loans or credits to the directors, or to its top executives, thus complying with the requirements of the Sarbanes-Oxley Act passed in the U.S. which is applicable to Telefónica as a listed company in that market.

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Meanwhile, the four senior executives¹ of the Company, excluding those that are also members of the Board of Directors, received a total for all items in 2007 of 4,813,277 euros.

In addition, the maximum number of shares corresponding to the first and second phases of the Performance Share Plan to be delivered to all the Company's senior executives if all the established terms are met is 157,046 shares and 130,911 shares, respectively.

In addition, with respect to the Pension Plan for directors (see Note 16.2), the total amount of contributions made by the Telefónica Group in 2007 was 1,707,237 euros for executive directors and 786,2621 euros for directors who held positions of senior executives at the Company in 2007.

Finally, we would note that the senior executive contracts, including those of executive directors, generally include a severance clause entailing three years of salary plus another year based on years of service at the Company. The annual salary on which the indemnity is based is the director's last fixed salary and the average amount of the last two variable payments received by contract.

e) Detail of the equity investments in companies engaging in an activity that is identical, similar or complementary to that of the Company and the performance of similar activities by the directors on their own behalf or on behalf of third parties

Pursuant to Article 127 ter. 4 of the Spanish Corporation Law, introduced by Law 26/2003 July 17, which amends Securities Market Law 24/1988 July 28, and the revised Spanish Corporation Law, in order to reinforce the transparency of listed corporations, details are given below of the companies engaging in an activity that is identical, similar or complementary to the corporate purpose of Telefónica, S.A., in which the members of the Board of Directors own equity interests, and of the functions, if any, that they discharge in them:

¹ For these purposes, Senior Executives are understood to be individuals who perform senior management functions in a company reporting directly to the management bodies, executive committees or CEOs, including the person in charge of the internal audit.

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Director	Investee	Activity	Percentage of ownership %⁽¹⁾	Position
David Arculus	Vodafone Group, Plc.	Telecommunications	< 0.01%	
	British Sky Broadcasting Group, Plc.	Telecommunications	< 0.01%	
	BT Group, Plc.	Telecommunications	< 0.01%	
Isidro Fainé Casas	Abertis Infraestructuras, S.A.	Telecommunications	< 0.01%	Chairman
Antonio Viana-Baptista	PT Multimedia-Serviços de Telecomunicações e Multimedia, S.G.P.S., S.A.	Internet	< 0.01%	
	Portugal Telecom, S.G.P.S., S.A.	Telecommunications	< 0.01%	Director

(1) If the holding is less than 0.01% of the share capital, < 0.01% is shown.

The table below, in accordance with the same Law, gives details of activities carried out, on their own account or on behalf of third parties, by the various members of the Company Board of Directors that are identical, similar or complementary to the corporate purpose of Telefónica, S.A.

Name	Activity	Arrangement under which the activity is performed⁽²⁾	Company through which the activity is performed	Position held or functions performed
César Alierta	Telecommunications	On behalf of third parties	Telefónica O2 Europe, Plc. ⁽³⁾	Director
Izuel	Telecommunications	On behalf of third parties	Telecom Italia, S.p.A.	Director
	Telecommunications	On behalf of third parties	China Netcom Group Corporation	Director
Isidro Fainé Casas	Telecommunications	On behalf of third parties	Abertis Infraestructuras, S.A.	Chairman

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Name	Activity	Arrangement under which the activity is performed(2)	Company through which the activity is performed	Position held or functions performed
Julio Linares López	Telecommunications	On behalf of third parties	Telefónica de España, S.A.U.	Director
	Telecommunications	On behalf of third parties	Telefónica DataCorp, S.A.	Director
	Telecommunications	On behalf of third parties	Telefónica O2 Europe, Plc.	Director
	Telecommunications	On behalf of third parties	Telefónica O2 Czech Republic, a.s	1 st Vice Chairman of Supervisory Board
	Television, telecommunications and audiovisual production services	On behalf of third parties	Sogecable, S.A.	Director
	Telecommunications	On behalf of third parties	Telecom Italia, S.p.A.	Director

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Name	Activity	Arrangement under which the activity is performed(2)	Company through which the activity is performed	Position held or functions performed
Fernando de Almansa Moreno-Barreda	Telecommunications	On behalf of third parties	Telefónica Internacional, S.A.U.	Director
	Telecommunications	On behalf of third parties	Telefónica del Perú, S.A.A.	Director
	Telecommunications	On behalf of third parties	Telefónica de Argentina, S.A.	Director
	Telecommunications	On behalf of third parties	Telecomunicações de Sao Paulo, S.A.	Director
	Telecommunications	On behalf of third parties	Telefónica Móviles México, S.A. de C.V.	Director
José María Alvárez-Pallete López ⁽⁷⁾	Telecommunications	On behalf of third parties	Telefónica Internacional, S.A.	Executive Chairman
	Telecommunications	On behalf of third parties	Telefónica Móviles España, S.A.U.	Director
	Telecommunications	On behalf of third parties	Telefónica de España, S.A.U.	Director
	Telecommunications	On behalf of third parties	Telefónica Datacorp, S.A.U.	Director
	Telecommunications	On behalf of third parties	Telefónica O2 Europe, Plc ⁽⁴⁾	Director
	Telecommunications	On behalf of third parties	Telefónica de Argentina, S.A. ⁽⁸⁾	Director/Vice Chairman
	Telecommunications	On behalf of third parties	Telecomunicações de Sao Paulo, S.A.	Director/Vice Chairman
	Telecommunications	On behalf of third parties	Compañía de Telecomunicaciones de Chile, S.A.	Acting Director
	Telecommunications	On behalf of third parties	Telefónica Móviles México, S.A. de C.V.	Director/Vice Chairman
	Telecommunications	On behalf of third parties	Colombia Telecomunicaciones, S.A. ESP	Director

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Name	Activity	Arrangement under which the activity is performed(2)	Company through which the activity is performed	Position held or functions performed
José María Alvárez-Pallete López (7)	Telecommunications	On behalf of third parties	Telefónica del Perú, S.A.A.	Acting Director
	Telecommunications	On behalf of third parties	China Netcom Group Corporation.	Director
	Telecommunications	On behalf of third parties	Brasilcel, N.V.	Chairman of Supervisory Board
	Telecommunications	On behalf of third parties	Telefónica Móviles Colombia, S.A.	Director
David Arculus	Telecommunications	On behalf of third parties	Telefónica O2 Europe, Plc.	Director
Peter Erskine	Telecommunications	On behalf of third parties	Telefónica O2 Europe, Plc. ⁽⁵⁾	Executive Chairman
	Telecommunications	On behalf of third parties	Telefónica O2 Czech Republic, a.s. ⁽⁹⁾	Chairman of Supervisory Board
Alfonso Ferrari Herrero	Telecommunications	On behalf of third parties	Compañía de Telecomunicaciones de Chile, S.A.	Director
	Telecommunications	On behalf of third parties	Telefónica de Perú, S.A.A.	Director
	Telecommunications	On behalf of third parties	Telefónica Móviles Chile, S.A.	Director

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Name	Activity	Arrangement under which the activity is performed(2)	Company through which the activity is performed	Position held or functions performed
Antonio Viana	Telecommunications	On behalf of third parties	Portugal Telecom, S.G.P.S., S.A. ⁽⁶⁾	Director
Baptista	Telecommunications	On behalf of third parties	Telefónica O2 Europe, Plc.	Director

(2) Only assigned when the activity is carried out through a third party and, accordingly, through a company.

(3) On January 16, 2008, César Alierta Izuel stepped down from his post as director of Telefónica O2 Europe, Plc.

(4) On January 16, 2008, José María Álvarez-Pallete López stepped down from his post as director of Telefónica O2 Europe, Plc.

(5) On December 31, 2007, Peter Erskine stepped down from his post as director and executive chairman of Telefónica O2 Europe, Plc. Subsequently, on February 1, 2008, he was reappointed a director of the

Company.

- (6) On January 31, 2008, Antonio Viana-Baptista stepped down from his post as director of Portugal Telecom, SGPS, S.A.
- (7) On February 12, 2008, José María Álvarez- Pallete López was appointed a director of Portugal Telecom, SGPS, S.A.
- (8) On February 21, 2008, José María Álvarez-Pallete López stepped down from his post as director of Telefónica de Argentina, S.A. and became acting director.

On the same date, Francisco Javier de Paz Mancho was appointed director Telefónica de Argentina, S.A.

- (9) On February 21, 2008, Peter Erskine stepped down from his post as member of the Supervisory Board of Telefónica O2 Czech Republic, a.s. and, therefore, his post as Chairman of this board.

On February 19,
2008 Francisco
Javier de Paz
Mancho was
appointed director
Telecomunicaçoes
de Sao Paulo, S.A.

Pursuant to Article 114.2 of the Spanish Corporation Law, also introduced by Law 26/2003 of July 17, it is stated that in the year to which these annual financial statements refer, the directors, or persons acting on their behalf, did not perform any transactions with Telefónica or any other company in the Telefónica Group other than in the normal course of the Company's business or that were not at arm's length.

f) Auditors fees

Fees paid to the various companies forming part of the Ernst & Young International Group, to which Ernst & Young, S.L. (the auditors of Telefónica, S.A.) belongs, totaled 4.3 million euros and 3.6 million euros in 2007 and 2006, respectively, as follows.

	Millions of euros	
	2007	2006
Audit of financial statements	1.2	1.2
Other audit services	3.1	2.4
Non-audit work	0.0	0.0
TOTAL	4.3	3.6

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g) Environmental matters

As head of the Telefónica Group, Telefónica, S.A. engages in activities relating to the ownership of shares and the provision of financing and corporate advisory services to various Group companies. In view of the business activities in which the Company engages, it has no environmental liabilities, expenses, assets, provisions or contingencies that could have a significant effect on its equity, financial situation and results. Consequently, the 2007 annual financial statements do not include specific details regarding environmental issues.

(18) EVENTS AFTER THE BALANCE SHEET DATE

Significant events affecting Telefónica taking place from December 31, 2007 to the date of preparation of these financial statements included:

EIB financing

On January 15, 2008 Telefónica Finanzas, S.A. paid off at maturity the balance on the 200 million euro loan taken out with the European Investment Bank (EIB) on January 9, 1998, guaranteed by Telefónica.

On January 17, 2008, Telefónica Finanzas, S.A. arranged a 75 million euro facility (Tranche B of the Telefónica Mobile Telephony II project) with a bank guarantee and counter guarantees by Telefónica maturing January 29, 2016.

On January 30, 2008 Telefónica Finanzas, S.A. drew down the amounts of the facilities arranged with the EIB on December 3, 2007 and January 17, 2008 of 375 and 75 million euros, respectively, comprising Tranches A and B of the Telefónica Mobile Telephony II project.

Dividend received from Telefónica O2 Europe, Plc.

On February 14, 2008, Telefónica O2 Europe Plc paid the interim dividend charged against 2007 profit granted to Telefónica, S.A. for 2,000 million pounds sterling.

Table of Contents**(19) STATEMENT OF SOURCE AND APPLICATION OF FUNDS**

APPLICATIONS OF FUNDS	2007	2006	SOURCES OF FUNDS	2007	2006
- Funds applied in operations			- Funds obtained from operations	5,145	4,851
- Start-up and debt arrangement expenses		44	- Long-term deferred tax liabilities	2,644	2,009
- Acquisition of fixed assets:			- Long-term debt		22,100
a) Intangible assets	19	17	- Disposal of fixed assets	3,816	2,414
b) Property, plant and equipment	98	232	- Transfer to short term of loans	1,615	1,709
c) Long-term investments	2,899	28,075			
- Capital reduction and distribution of treasury stock	2,203				
- Cash dividend	3,078	2,627			
- Long-term debt	7,130				
- Change in working capital due to inclusion of Telefónica Móviles, S.A. in 2006 (Note 1)		4,051			
TOTAL FUNDS APPLIED	15,427	35,046	TOTAL FUNDS OBTAINED	13,220	33,083
FUNDS OBTAINED IN EXCESS OF FUNDS APPLIED			FUNDS APPLIED IN EXCESS OF FUNDS OBTAINED	2,207	1,963
(INCREASE IN WORKING CAPITAL)			(DECREASE IN WORKING CAPITAL)		
	15,427	35,046		15,427	35,046

Table of Contents**CHANGES IN WORKING CAPITAL**

INCREASE IN WORKING CAPITAL	2007	2006
Accounts receivable	270	94
Short-term investments	2,604	
Cash	932	959
Prepayments and accrued income		3
Accounts payable		1,240
TOTAL	3,806	2,296
CHANGE IN WORKING CAPITAL	2,207	1,963
	6,013	4,259

DECREASE IN WORKING CAPITAL	2007	2006
Accounts receivable		
Short-term investments		3,498
Treasury shares	10	761
Prepayments and accrued income	11	
Accounts payable	5,992	
TOTAL	6,013	4,259
CHANGE IN WORKING CAPITAL		
	6,013	4,259

The reconciliation of the balances of the income statement to the funds obtained from operations is as follows:

	Millions of euros	
	2007	2006
Profit for the year	6,620	8,284
Plus:		
Depreciation and amortization expense	65	51
Amortization of debt arrangement expenses	69	63
Short-term investment writedown provisions		(11)
Period provisions	401	520
Changes in provisions for securities investments	9,875	(231)
Losses on disposal of fixed assets	2	2
Losses on transactions with own shares		1
Less:		
Dividend in kind received	8,636	
Gains on disposal of long-term investments	1,785	1,872
Gains on transactions with own shares	23	48
Reversal of provisions		621

Capitalized interest expense	1	4
Corporate income tax	1,442	1,283
Funds obtained from operations	5,145	4,851

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(20) ADDITIONAL NOTE FOR ENGLISH TRANSLATION

These financial statements are presented on the basis of accounting principles generally accepted in Spain. Consequently, certain accounting practices applied by the Company may not conform with generally accepted principles in other countries.

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APPENDIX I
Details of subsidiaries,
associated companies and investees
at December 31, 2007

Table of Contents**DETAILS OF SUBSIDIARIES, ASSOCIATES AND INVESTEEES AT December 31, 2007**

Millions of euros				Interim	Profit	Carrying
	Ownership	Capital	Reserves	Dividend	(loss)	Amount
Subsidiaries and investments	%					
Telefónica O2 Europe plc (UK) (1) (6)	100.00 %	12	16,169	(2,727)	2,418	26,153
<i>Mobile communications services operator</i>						
<i>Wellington Street, Slough, SL1 1YP</i>						
O2 (Europe) Ltd. (UK) (1)	100.00 %	14	355		1,048	8,520
<i>Mobile communications services operator</i>						
<i>Wellington Street, Slough, SL1 1YP</i>						
Telefónica Internacional, S.A. (SPAIN) (1)	100.00 %	2,839	1,354		964	8,132
<i>International investment in Telecoms sector</i>						
<i>C/ Gran Vía, 28 - 28013 Madrid</i>						
Telefónica Móviles España, S.A.U. (SPAIN) (1)	100.00 %	423	468		2,524	5,775
<i>Mobile communications services provider</i>						
<i>Plaza de la Independencia, 6 - Pta. 5 - 28001 Madrid</i>						
Telefonica O2 Czech Republic, a.s. (CZECH REPUBLIC) (1) (6) (10)	69.41 %	745	1,068		209	3,663
<i>Telecoms services provider</i>						
<i>Olsanska 55/5 - Praga 3, 130 34</i>						
Telefónica de España, S.A.U. (SPAIN) (1)	100.00 %	1,024	1,880		2,282	3,034
<i>Spanish Telecoms service provider</i>						
<i>Gran Vía, 28 - 28013 Madrid</i>						
Telefónica de Contenidos , S.A.U. (SPAIN) (1)	100.00 %	1,865	(1,678)		(10)	2,242
<i>Multimedia services</i>						
<i>Jorge Manrique, 12 - 28006 Madrid</i>						
Brasilcel, N.V. (NETHERLANDS) (1) (6)	50.00 %		6,560		91	2,179
<i>Joint Venture and mobile services holding company</i>						
<i>Strawinskylaan 3105 - 1077ZX</i>						
<i>Amsterdam</i>						
Latin America Cellular Holdings, B.V. (NETHERLANDS) (1)	100.00 %	980	(403)		256	1,635
<i>Holding company</i>						
<i>Strawinskylaan 3105, Atium 7th, Amsterdam</i>						
Telefónica Datacorp, S.A.U. (SPAIN) (1)	100.00 %	700	36		6	1,343

Telecoms services provider and operator**Gran Vía, 28 - 28013 Madrid****Telefónica Móviles México, S.A. de C.V. (MEXICO) (1) (6)**

100.00 %	1,267	(2,256)	(544)	1,176
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Holding company**Prolongación Paseo de la Reforma****1200 Col. Cruz Manca, Mexico City****CP.05349****Telefónica Móviles Argentina Holding, S.A. (ARGENTINA) (1)**

100.00 %	258	185	151	1,141
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Holding company**Ing Enrique Butty 240, piso 20-Capital****Federal-Argentina****Ecuador Cellular Holdings, B.V.****(NETHERLANDS) (1)**

100.00 %	46		(1)	581
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Holding company**Strawinskylaan 3105, Atium 7th,****Amsterdam****Inversiones Telefónica Móviles****Holding Limitada (CHILE) (1)**

100.00 %	428	(85)	160	424
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Holding company**Av El Bosque Sur 090, Los Condes,****Santiago de Chile****Telefónica International Wholesale Services America, S.A. (URUGUAY) (1)**

80.56 %	469	17	(15)	407
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Broadband services provider**Luis A. de Herrera, 1248 Piso 4 -****Montevideo**

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Millions of euros				Interim	Profit	Carrying
	Ownership	Capital	Reserves	Dividend	(loss)	Amount
Subsidiaries and investments	%					
Atento Holding, Inversiones y Teleservicios, S.A. (SPAIN) (1)	100.00 %	24	138			373
<i>Telecoms services provider</i>						
<i>C/ Santiago de Compostela, 94 - 28.035 Madrid</i>						
Inversiones Telefónica Móviles Holding II Limitada (CHILE) (1)	100.00 %	334	(43)		72	318
<i>Mobile communications services operator</i>						
<i>Avda. El Bosque Sur 090, Las Condes, Santiago de Chile</i>						
Multi Holding Corporation (PANAMA) (7)	100.00 %	N/D	N/D	N/D	N/D	301
<i>Dormant company</i>						
<i>Edificio HSBC, Piso 11, Avd Samuel Lewis Panamá</i>						
TCG Holdings, S.A. (GUATEMALA) (1)	100.00 %	281	(169)		31	239
<i>Holding company</i>						
<i>Bulevar Los Próceres 5-56 Zona 10, Unicentro nivel 10 - Guatemala City</i>						
Panamá Cellular Holdings, B.V. (NETHERLANDS)	100.00 %	40			(2)	238
<i>Holding company</i>						
<i>Strawinskylaan 3105, Atium 7th, Amsterdam</i>						
Telefónica International Wholesale Services, S.L. (SPAIN) (1)	92.51 %	230	7		(15)	213
<i>International services provider</i>						
<i>Gran Vía, 28 - 28013 Madrid</i>						
Telefónica Móviles El Salvador Holding, S.A. de C.V. (EL SALVADOR) (1))	100.00 %	127	(79)		21	161
<i>Holding company</i>						
<i>Alameda Roosevelt y Avenida Sur. Torre Telefónica nivel 10 - San Salvador</i>						
Telefónica Móviles Argentina, S.A. (ARGENTINA) (1)	15.40 %	107	N/D	N/D	N/D	139
<i>Holding company</i>						
<i>Ing Enrique Butty 240, piso 20-Capital Federal-Argentina</i>						
Telcel, C.A. (VENEZUELA) (1)	0.08 %	109	634	(264)	700	123
<i>Operadora de comunicaciones móviles</i>						
<i>Av. Francisco de Miranda, Edif Parque Cristal, Caracas 1060</i>						

Telefónica Móviles Colombia, S.A. (COLOMBIA) (1) <i>Mobile communications operator</i> <i>Calle 100, N° 7-33, Piso 15,</i> <i>Bogotá, Colombia</i>	22.44 %		1,028		20	116
Telefónica Móviles Puerto Rico, Inc. (PUERTO RICO) <i>Holding vehicle for investments in</i> <i>Puerto Rico mobile operators</i> <i>Metro Office Park Calle Edificio #17,</i> <i>Suite 600 - 00968 Guaynabo</i>	100.00 %	98	(98)			110
Ateseco Comunicación, S.A. (SPAIN) <i>Holding company</i> <i>C/ Gran Vía, 28 - 28.013 Madrid</i>	100.00 %	6	43		1	108
Terra Networks Asociadas, S.L. (SPAIN) (4) <i>Holding company</i> <i>C/ Gran Vía, 28 - 28.013 Madrid</i>	100.00 %	7	(28)		(3)	64
Seguros de Vida y Pensiones Antares, S.A. (SPAIN) (1) <i>Life insurance, pensions and health</i> <i>insurance</i> <i>Avda. General Perón, 38 Master II - 17ª</i> <i>P. - 28020 Madrid</i>	89.99 %	51	49		3	59
LE Holding Corporation (USA) <i>Holding company</i> <i>Corporation Trust Center, 1209 Orange</i> <i>Street Wilmington, Delaware 19801</i>	100.00 %	N/D	N/D	N/D	N/D	48
Telefónica Móviles Guatemala, S.A. (GUATEMALA) (1) <i>Wireless, wireline and radio paging</i> <i>communications services</i> <i>Bulevar Los Próceres 5-56 Zona 10,</i> <i>Unicentro nivel 11 - Guatemala City</i>	13.60 %	279	12		(178)	38

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Millions of euros	Ownership	Capital	Reserves	Interim Dividend	Profit (loss)	Carrying Amount
Subsidiaries and investments	%					
Guatemala Cellular Holdings, B.V. (NETHERLANDS) (1)	100.00%	19				29
<i>Holding company Strawinskylaan 3105, Atium 7th, Amsterdam</i>						
Taetel, S.L. (SPAIN) (1)	100.00%	28	6		1	28
<i>Purchase, holding and sale of shares and investments in other companies Beatriz de Bobadilla, 3 - 28040 Madrid</i>						
Telefónica Gestión de Servicios Compartidos, S.A. (SPAIN) (4)	100.00%	8	1		8	24
<i>Management and administration services provider Gran Vía, 28 - 28013 Madrid</i>						
Telefónica Capital, S.A. (SPAIN) (3)	100.00%	7	63		9	18
<i>Finance Company Gran Vía, 28 - 28013 Madrid</i>						
Lotca Servicios Integrales, S.L. (SPAIN) (4)	100.00%	17				17
<i>Holding and operation of aircraft and aircraft leasing Gran Vía, 28 - 28013 Madrid</i>						
Comet, Compañía Española de Tecnología, S.A. (SPAIN) (3)	100.00%	5	2			14
<i>Promotion of business initiatives and holding of real estate assets Villanueva, 2 duplicado planta 1ª Oficina 23 - 28001 Madrid</i>						
Telefónica Móviles del Uruguay, S.A. (URUGUAY)	100.00%	6	27		15	13
<i>Mobile communications services operator Plza de la Independencia 8, planta baja, Montevideo</i>						
Telefónica Finanzas, S.A. (TELFISA) (SPAIN) (1)	100.00%	3	17		5	13
<i>Integrated cash management, consulting and financial support for Group companies Gran Vía, 30 - 4ª Plta. - 28013 Madrid</i>						
Corporation Real Time Team, S.L. (SPAIN)	87.96%	0	N/D	N/D	N/D	12
<i>Internet design, advertising and consulting Claudio Coello, 32, 1º ext. Madrid</i>						

Telefónica Móviles Soluciones y Aplicaciones, S.A. (CHILE) (1) <i>IT and communications services provider</i> <i>Avenida del Cóndor N°720, piso 4, comuna de Huechuraba, de la Ciudad de Santiago de Chile</i>	100.00%	11	(5)			11
Centro de Investigación y Experimentación de la Realidad Virtual, S.L. (SPAIN) <i>Design of communications products</i> <i>Vía de Dos Castillas, 33 - Comp. Ática Ed. 1, 1ª Plta. Pozuelo de Alarcón - 28224 Madrid</i>	100.00%		N/D	N/D	N/D	10
Telefónica Ingeniería de Seguridad, S.A. (SPAIN) (2) <i>Security services and systems</i> <i>Condesa de Venadito, 1 - 28027 Madrid</i>	100.00%	1			2	9
Telefónica Investigación y Desarrollo, S.A. (TIDSA) (SPAIN) (3) <i>Telecommunications research activities and projects</i> <i>Emilio Vargas, 6 - 28043 Madrid</i>	100.00%	6	69		(12)	6
Venturini España, S.A. (SPAIN) (2) <i>Printing, graphic arts and direct marketing</i> <i>Avda. de la Industria, 17 Tres Cantos - 28760 Madrid</i>	100.00%	3	1			4
Casiopea Reaseguradora, S.A. (LUXEMBOURG) (1) <i>Reinsurance</i> <i>6D, route de Trèves, L-2633 Senningerberg, Luxembourg</i>	99.97%	4	191		17	3
Telefónica Finanzas Perú, S.A.C. (PERU) (1) <i>Integrated cash management, consulting and financial support for Group companies</i> <i>Lima</i>	100.00%	3	(0)			3

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Millions of euros				Interim	Profit	Carrying
	Ownership	Capital	Reserves	Dividend	(loss)	Amount
Subsidiaries and investments	%					
Telefónica del Perú, S.A.A. (PERU) (1)						
(6) (10)	0.15%	589	85		(15)	2
<i>Operator of local, domestic and international long distance telephony services in Peru</i>						
<i>Avda. Arequipa, 1155 Santa Beatriz Lima</i>						
Telfisa Global, B.V. (NETHERLANDS)	100.00%		2			2
<i>Integrated cash management, consulting and financial support for Group companies</i>						
<i>Strawinskylaan 1259 ; tower D ; 12th floor 1077 XX Amsterdam</i>						
Telefónica de Centroamérica, S.L. (SPAIN) (8)	100.00%	N/D	N/D	N/D	N/D	1
<i>Dormant company</i>						
<i>Gran Vía, n° 28, Madrid</i>						
Telefónica Brasil Sul Celular Participações, Ltda. (BRAZIL) (5)	1.12%	N/D	N/D	N/D	N/D	1
<i>Holding company</i>						
<i>Avda. Martiniano de Carvalho, 851, 20 andar, parte Sao Paulo, Sao Paulo</i>						
Telefónica (USA) Advisors, Inc. (USA) (8)	100.00%					1
<i>All the activities permitted by Delaware State law</i>						
<i>1013 Center Road, Wilmington County of Newcastle Delaware 19805</i>						
Comtel Comunicaciones Telefónicas, S.A. (VENEZUELA) (1)	65.14%	19	1		3	
<i>Holding company</i>						
<i>Av. Francisco de Miranda, Edif Parque Cristal, Caracas 1060, Venezuela</i>						
Pléyade Peninsular, Correduría de Seguros y Reaseguros del Grupo Telefónica, S.A. (SPAIN) (3)	16.67%		1		3	
<i>Distribution, promotion or preparation of insurance contracts, operating as a broker</i>						
<i>Avda. General Perón, 38 Master II - 17ª P.- 28020 Madrid</i>						
Fisatel Mexico, S.A. de C.V. (MEXICO) (1)	100.00%		1			

*Integrated cash management,
consulting and financial support for
Group companies*

*Boulevard Manuel Avila Camacho, 24 -
16ª Plta. Lomas de Chapultepec -
11000 Mexico D.F.*

Telefónica Participaciones, S.A.

(SPAIN) (1) **100.00%** **(0)** **(0)**

*Issuance of preferred securities and/or
other debt financial instruments*

Gran Vía, 28 - 28013 Madrid

Telefónica Emisiones, S.A. (SPAIN) (1) **100.00%** **(3)** **1**

*Issuance of preferred securities and/or
other debt financial instruments*

Gran Vía, 28 - 28013 Madrid

Telefónica Europe, B.V.

(NETHERLANDS) (1) **100.00%** **9** **(4)** **2**

Fund raising in capital markets

*Strawinskylaan 1259 ; tower D ; 12th
floor 1077 XX Amsterdam*

Telco, S.p.A. (ITALY) **42.30%** **5** **2,314**

Holding company

Galleria del Corso, 2 - Milan

Portugal Telecom, S.G.P.S., S.A.

(PORTUGAL) (5) (6) (10) **7.14%** **34** **379** **1,010** **676**

Holding company

*Avda. Fontes Pereira de Melo, 40 - 1089
Lisbon*

Aliança Atlântica Holding B.V.

(NETHERLANDS) **50.00%** **40** **2** **(2)** **10** **21**

*Holder of 5,225,000 Portugal Telecom,
S.A. shares*

Strawinskylaan 1725, 1077 XX

Amsterdam

MobiPay Internacional, S.A. (SPAIN) **50.00%** **12** **(9)** **(1)** **5**

*Provision of payment services through
wireless telephony*

*Avenida de Europa 20, Alcobendas,
Madrid*

Telefónica Factoring España, S.A.

(SPAIN) (5) **50.00%** **5** **2** **3** **3**

Factoring

Pedro Teixeira, 8 - 28020 Madrid

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Millions of euros				Interim	Profit	Carrying
	Ownership	Capital	Reserves	Dividend	(loss)	Amount
Subsidiaries and investments	%					
Torre de Collçerola, S.A. (SPAIN) (2)	30.40 %	6	1			2
<i>Operation of a telecommunications mast and technical assistance and consulting services</i>						
<i>Ctra. Vallvidrera-Tibidabo, s/nº - 08017 Barcelona</i>						
Telefónica Factoring México, S.A. de C.V. SOFOM ENR (MEXICO)	40.50 %	2				1
<i>Factoring Mexico City</i>						
Adquiria Spain, S.A. (SPAIN) (2)	20.00 %	2	5		2	1
<i>E-commerce Goya, 4, 4ª planta Madrid</i>						
Telefónica Factoring Perú, S.A.C. (PERU)	40.50 %	1				1
<i>Factoring Lima</i>						
Telefónica Factoring Do Brasil, Ltd. (BRAZIL) (5)	40.00 %	1	3	(3)	3	1
<i>Factoring Avda. Paulista, 1106</i>						
Banco Bilbao Vizcaya Argentaria, S.A. (SPAIN) (5) (6) (10)	0.97 %	1,837	21,641	(1,661)	6,126	556
<i>Banking San Nicolás, 4 - 48005 Bilbao (Vizcaya)</i>						
PT Multimedia Serviços de Telecomunicações e Multimédia, SGPS, S.A. (PORTUGAL)	4.80 %	3	328		52	136
<i>Multimedia business Avda. 5 de Outubro, 208 - Lisbon</i>						
Sogecable, S.A. (SPAIN) (5) (6) (10)	1.20 %	277	(64)		62	35
<i>Indirect management of public service television Gran via, 32 - 3ª Pta. - 28013 Madrid</i>						
Amper, S.A. (SPAIN) (5) (6) (10)	6.10 %	29	48		2	12
<i>Development, manufacture and repair of telecommunications systems and equipment and related components Torrelaguna, 75 - 28027 Madrid</i>						
I-CO Global Communications (HOLDINGS) Limited (UK)	N/D	N/D	N/D		N/D	6
Other investments	N/A	N/A	N/A		N/A	7
TOTAL SUBSIDIARIES (Note 7)						69,274
TOTAL ASSOCIATES (Note 7)						3,025
TOTAL INVESTEEES (Note 7)						752

- (1) *Audited by Ernst & Young.*
- (2) *Audited by
PriceWaterhouseCoopers.*
- (3) *Audited by K.P.M.G. Peat
Marwick.*
- (4) *Audited by B.D.O. Audiberia*
- (5) *Audited by Deloitte & Touche.
En España Deloitte & Touche
España, S.L..*
- (6) *Consolidated figures*
- (7) *Dormant company*
- (8) *Company in liquidation.*
- (10) *Companies listed on
international markets at
December 31, 2007.*
- N/D *No data available.*
- N/A *Not applicable.*

Provisional figures for associates and investees.

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**MANAGEMENT REPORT
TELEFÓNICA, S.A.
2007**

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Telefónica Group results for 2007 once again reflect the Company's differentiated profile, supported by its capacity to deliver on strategy and continuously hit financial targets. The solid growth seen in 2007 shows the Group's potential for organic expansion, the high value of its geographical and business diversification, its efficient cost structure and the realization of synergies made possible by the integrated management of the Company.

The pace of commercial activity accelerated in the last quarter of 2007, thanks to successful marketing campaigns to attract and retain customers. As a result, Telefónica Group ended the year with a customer base of 228.6 million, up by 12.5% on December 2006.

Telefónica Spain has 46.4 million customers, a 5% increase on December 2006. Growth was driven by the expanding base of mobile and broadband customers and limited losses in wireline, where the year-on-year fall in customer numbers was the lowest since 2001 (-0.3%).

Telefónica Latin America increased the pace of growth in its customer base (134.1 million: +16.9% year-on-year), with big gains in broadband, a strong upward trend in mobile telephony and a near doubling of pay-TV subscribers since end-2006.

Telefónica Europe grew its customer base by 8.7% to nearly 42 million, boosted by strong trends in the mobile business, particularly the contract segment.

By access type, Telefónica Group had 169.2 million mobile customers in 2007, up by 16.6% on December 2006.

At December 31, 2007, the Group had more than 10.2 million retail broadband customers, with year-on-year growth of 28.9%. Demand remained strong for the Group's bundled ADSL, TV and voice offer, a key factor in developing the broadband market and securing the loyalty of the customer base. Retail broadband customers numbered over 4.5 million in Spain (+22.1% year-on-year), 5 million in Latin America (+33.2% year-on-year) and 670,000 in Europe outside Spain (+48.3%).

Pay TV customers totaled more than 1.7 million at end 2007, a 64.3% increase on the year, with the offering now available in Spain, the Czech Republic, Peru, Chile, Colombia and Brazil.

Looking forward, the Telefónica Group plans to continue with its strategy of making the customer the cornerstone of the Group by focusing on operating excellence, convergence and innovation as sources of competitive advantage and motivation for personnel. This global dimension poses a challenge for Telefónica to maximize the synergies derived from the inclusion of new companies so it can leverage economies of scale and offer customers higher quality service

Results of Telefónica, S.A.

The Company generated 6,620 million euros of profit in 2007, compared to 8,284 million euros in 2006.

Highlights of the 2007 income statement include:

An operating loss of 359 million euros, which represents a 27% reduction on 2006, mainly due to increased billings for services provided to Telefónica Group subsidiaries.

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An increase in financial income to 14,083 million euros in 2007, compared to 5,195 million in 2006, reflecting an increase in dividends received from Group companies, mainly the 11,272 million euros from Telefónica O2 Europe plc.

The combination of these two figures produced income from ordinary activities of 13,724 million euros, far outstripping the 4,706 million euros recorded in 2006.

However, the company also recorded an extraordinary loss of 8,546 million euros compared to an extraordinary profit of 2,295 million euros in 2006. This was chiefly due to a 9,947 million euros impairment provision taken on the investment in Telefónica O2 Europe due in turn to the reduction in equity from the dividend paid to Telefónica, S.A. in 2007. On the positive side, the Company made a 1,776 million euro profit on the sale of 99.7% of Endemol Investment Holding, B.V.

Investment activity

The main investments made by Telefónica, S.A. in 2007 were as follows:

In July 2007 Telefónica, S.A. acquired 10,044 shares representing it an 8.65% stake in Atento, N.V. for 70 million euros from a BBVA Group company. After this transaction, Telefónica, S.A.'s holding in Atento, N.V. was 100%.

In October 2007, Telefónica, S.A. contributed 2,314 million euros to set up the Italian company Telco, S.p.A., of which it owns 42.3%. This company in turn owns approximately 23.6% of the voting shares in Telecom Italia, S.p.A..

In addition, the Company continued work on Telefónica Group's new operational complex, District C. As a result, additions to Telefónica, S.A.'s property, plant and equipment in 2007 totaled 99 million euros, compared with 232 million euros in 2006.

Financing

The following debt issues under Telefónica Emisiones, S.A.U.'s European Medium Term Note (EMTN) program, underwritten by Telefónica, S.A., registered on July 8, 2005 on the London Stock Exchange and renewed on July 3, 2007:

Two issues on January 31, 2007, for 55 million euros and 24 million euros maturing December 31, 2021 and January 31, 2018, respectively.

An issue on February 7, 2007, of bonds for 1,500 million euros maturing February 7, 2014.

Another issue on March 30, 2007, for 350 million euros maturing March 30, 2009.

A bond issue on June 19, 2007 for a total of 8,000 million Czech crowns divided up into three tranches: one for 2,400 million Czech crowns with a floating coupon maturing in 2010, one for 3,000 million Czech crowns with a fixed coupon maturing in 2012, and one for 2,600 million Czech crowns with a fixed coupon due in 2014.

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On July 2, 2007, Telefónica Emisiones, S.A.U. issued 2,300 million dollars of US dollar-denominated bonds under the program filed with the Securities and Exchange Commission (SEC). The issue was divided up into three tranches, two bond tranches maturing in 2013 (750 million US dollars with a fixed coupon and 850 million US dollars with a floating coupon) and one in 2017 (700 million US dollars with a fixed coupon). The securities issued under this program are guaranteed by Telefónica.

On 19 July 2007, Telefónica Europe, B.V. (Telefonica Europe) issued bonds in the Japanese market guaranteed by Telefónica, S.A. for a total amount of 30,000 million Japanese yen maturing in 2012 divided into two tranches, one for 15,000 million yen with a fixed coupon and one for 15,000 million yen with floating rates.

On August 23, 2007 Telefonica Europe arranged a facility guaranteed by Telefónica, S.A., for 15,000 million Japanese yen divided up into three tranches with a 30-year maturity.

On December 3, 2007 Telefónica Finanzas, S.A., a subsidiary of Telefónica, S.A., took out a 375 million euro loan with the European Investment Bank (EIB) maturing 7 years from the date of receipt (Tranche A of the Telefonie Mobile Telephony II project). The loan is underwritten by Telefónica, S.A. and had not been drawn at December 31, 2007.

Meanwhile, Telefónica Europe, B.V. continued its issuance activity in 2007 under its European commercial paper (ECP) program, underwritten by Telefónica, S.A., with short-term issues maturing between one week and 364 days. At December 31, 2007, the final balance of outstanding commercial paper totaled 906.8 million euros (at face value).

Treasury shares

At the start of 2007 Telefónica held treasury shares of 1.53689%, made up of 75,632,559 shares, with a par value of 14.04 euros each, a balance of 1,062 million euros and a nominal value of 76 million euros.

In the course of 2007 the Company bought 149,099,044 and sold 12,621,573 of its own shares, generating extraordinary profit of 23 million euros.

Also, the Company used 147,633,912 treasury shares at an acquisition cost of 2,202 million euros to reduce its share capital.

In addition, 4,750 treasury shares were allocated in 2007 to the share option plan established for employees of the Endemol Group.

As a result of the transactions described above, at the close of 2007 the Company held 64,471,368 shares in treasury stock (representing 1.35061% of share capital) acquired at an average price of 16.67 euros per share, implying a total outlay of 1,075 million euros and total nominal value of 64 million euros. Pursuant to current accounting legislation, these shares were measured at their underlying book value and, consequently, a provision of 843 million euros was recorded.

Table of Contents***Disclosures required under Article 116.bis of the Spanish Securities Market Law***

Disclosures required under Article 116.bis of the Spanish Securities Market Law:

a. Capital structure

On December 31, 2007, the share capital of Telefónica, S.A. was 4,773,496,485 euros, represented by 4,773,496,485 fully paid ordinary shares of a single series, par value of 1 euro each, recorded under the book-entry system and traded on the Spanish electronic trading system (Continuous Markets) where they form part of the Ibex 35 index), on the four Spanish stock exchanges (Madrid, Barcelona, Valencia and Bilbao) and listed on the New York, London, Paris, Frankfurt, Tokyo, Buenos Aires, Sao Paulo and Lima Stock Exchanges. In October 2007, Telefónica, S.A. began taking steps to delist its shares from the Paris and Frankfurt stock exchanges. This will take place in the first quarter of 2008.

At the time of writing, Telefónica, S.A. has no securities in issue that are convertible into Telefónica, S.A. shares.

b. Restrictions on the transfer of securities.

Nothing in the Company bylaws imposes any restriction or limitation on the free transfer of Telefónica, S.A. shares.

c. Major shareholdings

The table below lists shareholders who, at December 31, 2007, to the best of the Company's knowledge, had significant direct or indirect shareholdings in the Company as defined in Royal Decree 1362/2007 implementing the Spanish Securities Markets Law 24/1998 as it relates to the need for transparent information on issuers whose securities are listed for trading in an official secondary market or other regulated market of the European Union :

	Total		Direct shareholding		Indirect shareholding	
	%	Shares	%	Shares	%	Shares
BBVA ⁽¹⁾	6.258	298,717,001	6.257	298,699,855	0.000	17,146
la Caixa ⁽²⁾	5.483	261,746,565	0.002	102,233	5.481	261,644,332

(1) Based on the information contained in Banco Bilbao Vizcaya Argentaria, S.A.'s 2007 Annual Report on Corporate Governance at December 31, 2007.

(2)

Based on
information
provided by
Caja de Ahorros
y Pensiones de
Barcelona, la
Caixa as at
December 31,
2007 for the
2007 Annual
Report on
Corporate
Governance.
The 5.481%
indirect
shareholding in
Telefónica, S.A.
Telefónica
Group is
owned by
Criteria
CaixaCorp, S.A.

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d. Restrictions on voting rights.

According to Article 21 of the Company's bylaws no shareholder can exercise votes in respect of more than 10 per cent of the total shares with voting rights outstanding at any time, irrespective of the number of shares they may own. This restriction on the maximum number of votes that each shareholder can cast refers solely to shares owned by the shareholder concerned and cast on their own behalf. It does not include additional votes cast on behalf of other shareholders who may have appointed them as proxy, who are themselves likewise restricted by the 10 per cent voting ceiling.

The 10 per cent limit described above also applies to the number of votes that can be cast either jointly or separately by two or more legal entity shareholders belonging to the same corporate group and to the number of votes that may be cast altogether by an individual or legal entity shareholder and any entity or entities that they directly or indirectly control and which are also shareholders.

e. Shareholder pacts

Telefónica, S.A. has received no communication notifying the existence of shareholder pacts that affect the exercise of voting rights at Shareholders' Meetings or that impose restrictions or conditions on the free transfer of Telefónica, S.A. shares.

f. Rules governing the appointment and replacement of Directors and the amendment of the Company's bylaws.

Appointment, reappointment and ratification.

Telefónica, S.A.'s bylaws state that the Board of Directors shall have between five and twenty Directors who are appointed by shareholders at the Shareholders' Meeting. The Board of Directors may, in accordance with the Spanish Corporation Law and the Company bylaws, provisionally co-opt Directors to fill any vacant seats.

The appointment of Directors to Telefónica, S.A. is as a general rule submitted for approval to the Shareholders' Meeting. Only in certain circumstances, when seats fall vacant after the conclusion of the General Meeting is it therefore necessary to co-opt Directors onto the board in accordance with the Spanish Corporation Law. Any such co-opted appointment is then ratified at the next Shareholders' Meeting.

Also, in all cases, proposals to appoint Directors must follow the procedures set out in the Company's Board of Directors' Rules and be preceded by the appropriate favorable report by the Appointments, Compensation and Good Governance Committee and in the case of independent Directors, by the corresponding proposal by the committee.

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Therefore, in exercise of the powers delegated to it, the Appointments, Compensation and Good Governance Committee must report, based on criteria of objectivity and the best interests of the company, on proposals to appoint, re-appoint or remove Company Directors, taking into account the skills, knowledge and experience required of candidates to fill the vacancies.

As a result, in accordance with its Rules, the Board of Directors, exercising the rights to co-opt and propose appointments to the Shareholders Meeting, shall ensure that external or non-executive Directors are in an ample majority over the executive Directors. Similarly, it shall ensure that independent Directors make up at least one third of the total Board members.

In all circumstances, where a Director is proposed to the Shareholders Meeting for reappointment or ratification, the report of the Appointments, Compensation and Good Governance Committee, or in the case of independent Directors the proposal of this committee, shall include an assessment of the Director's past work and diligence in discharge of their duties during their period in office.

Also, both the Board of Directors and the Appointments, Compensation and Good Governance Committee shall ensure, in fulfilling their respective duties, that all those proposed for appointment as Directors should be persons of acknowledged solvency, competence and experience who are willing to devote the time and effort necessary to the discharge of their functions, with particular attention paid to the selection of independent Directors.

Directors are appointed for a period of five years, renewable for one or more subsequent five-year periods.

As with appointments, proposals for the reappointment of Directors must be preceded by the corresponding report by the Appointments, Compensation and Good Governance Committee, and in the case of independent Directors by the corresponding proposal by the committee.

Termination of appointment or removal

Directors' appointments shall end at the expiry of the period for which they were appointed or when shareholders at the General Shareholders Meeting so decide in exercise of their powers under the law.

Also, in accordance with Article 12 of the Board Rules, Directors must submit their resignation to the Board of Directors and formalize their resignation in the following circumstances:

- i) If they leave the executive post by virtue of which they sat on the Board or when the reasons for which they were appointed cease to apply.

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- ii) If their circumstances become incompatible with their continued service on the Board or prohibit them from serving on the Board for one of the reasons specified under Spanish law.
- (iii) If they are severely reprimanded by the Appointments, Compensation and Good Governance Committee for failure to fulfill any of their duties as Director.
- iv) If their continued presence on the Board could affect the credit or reputation of the Company in the markets or otherwise threaten the Company's interests.

The Board of Directors shall not propose the termination of the appointment of any independent Director before the expiry of their statutory term, except in the event of just cause, recognized by the Board on the basis of a prior report submitted by the Appointments, Compensation and Good Governance Committee. Just cause shall be specifically understood to include cases where the Director has failed to fulfill their duties as Board member.

The Board may also propose the termination of the appointments of independent Directors in the case of takeover bids, mergers or other similar corporate transactions that represent a change in the structure of the Company's capital. Amendments to the Company bylaws.

The procedure for amending the bylaws is governed by Article 144 of the Spanish Corporation Law and requires any change to be approved by shareholders at the Shareholders' Meeting with the majorities stated in Article 103 of the same law. In accordance with the above, Article 14 of Telefónica, S.A.'s bylaws states that the power to amend Company's bylaws lies with shareholders acting at a General Shareholders' Meeting.

- g. Powers of Directors and, specifically, powers to issue or buy back shares.

Powers of Directors.

The Chairman of the Company, as Executive Chairman, is delegated all powers by the Board of Directors except where such delegation is prohibited by Law, by the Company bylaws or by the Regulations of the Board of Directors, whose Article 5.4 establishes the powers reserved to the Board of Directors. Specifically, the Board of Directors reserves the powers, inter alia, to: (i) approve the general policies and strategies of the Company; (ii) evaluate the performance of the Board of Directors, its committees and the Chairman; (iii) appoint senior executives, as well as the remuneration of directors and senior executives; and (iv) decide strategic investments.

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Meanwhile, the Chief Executive Officer has been delegated all the Board's powers to conduct the business and act as the senior executive for all areas of the Company's business, except where such delegation is prohibited by law, by the Company bylaws, or by the Regulations of the Board of Directors in its article 5.4.

In addition, the other executive Directors are delegated the usual powers of representation and administration appropriate to the nature and needs of their roles.

Powers to issue shares.

At the Ordinary Shareholders' Meeting of Telefónica, S.A. on June 21, 2006, the Board of Directors was authorized under Article 153.1.b) of the Spanish Corporation Law, to increase the Company's capital by up to 2,460 million euros, equivalent to half the Company's subscribed and paid share capital at that date, one or several times within a maximum of five years of that date. The Board of Directors has not exercised these delegated powers to date.

Also, at the General Shareholders' Meeting of Telefónica, S.A. on May 10, 2007, the Board of Directors was authorized under Articles 153.1.b) and 159.2 of the Spanish Corporation Law to issue bonds exchangeable for or convertible into shares in the Company, this power being exercisable one or several times within a maximum of five years of that date. The Board of Directors has not exercised this power to date.

Powers to buy back shares.

At the Ordinary Shareholders' Meeting of Telefónica, S.A. on May 10, 2007, the Board of Directors was authorized, in accordance with Articles 75 ff of the Spanish Corporation Law, to buy back its own shares either directly or via companies belonging to the Group. This authorization was granted for 18 months from that date and includes the specific limitation that at no point may the nominal value of treasury shares acquired, added to the those already held by Telefónica, S.A. and those held by any of the subsidiaries that it controls, exceed 5 per cent of the share capital at the time of acquisition.

- h. Significant agreements outstanding that would come into force, be amended or expire in the event of a change of control following a takeover.

The Company has no significant agreements outstanding that would come into force, be amended or expire in the event of a change of control following a takeover.

- i. Agreements between the Company and its directors, managers or employees that provide for compensation in the event of resignation or unfair dismissal or if the employment relationship should be terminated because of a takeover bid.

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In general, the contracts of executive directors and some managers of the steering committee include a clause giving them the right to receive the economic compensation indicated below in the event that their employment relationship is ended for reasons attributable to the Company and/or due to objective reasons such as a change of ownership. However, if the employment relationship is terminated for a breach attributable to the executive director and director, the director will not be entitled to any compensation whatsoever. That notwithstanding, in certain cases the termination benefit to be received by the executive director or director, according to their contract, does not meet these general criteria, but rather are based on other circumstances of a personal or professional nature or on when the contract was signed. The agreed economic compensation for the termination of the employment relationship, where applicable, consists of three years of salary plus another year based on length of service at the Company. The annual salary on which the indemnity is based is the director's last fixed salary and the average amount of the last two variable payments received by contract.

Meanwhile, contracts that tie employees to the Company under a common employment relationship due to include indemnity clauses for the termination of their employment. In these cases, the employee is entitled to any indemnity set forth in prevailing labor legislation. This notwithstanding, contracts of some Company employees, depending on their level and seniority, as well as their personal or professional circumstances or when they signed their contracts, establish their right to receive compensation in the same cases as in the preceding paragraph, generally consisting of a year and a half of salary. The annual salary on which the indemnity is based is the last fixed salary and the average amount of the last two variable payments received by contract.

The risks and uncertainty facing the company

In addition to the general risks affecting any type of business activity, Telefónica Group's business is also impacted by both internal factors, which are mainly related to its international presence, and external factors common to its business activity.

In this sense, the most significant risks which the Group faces and that could affect its business, financial situation and results would be the following:

Risks inherent to the business sector in which the Group operates.

The risks derived from the business activities' particular characteristics are because it operates in a highly competitive, highly regulated sector, in which the policies of many countries are designed to encourage new competition.

The risks involved in providing this service under licence or concession, which implies not only the need to comply with the terms and conditions of these licences, with the corresponding risk of review or revocation in the case of breach, but that these licenses and their terms and conditions is subject to review by the corresponding regulatory authorities.

The risks from constant technological change, experienced by companies in the telecommunication services sector, require continuous efforts by the Company to anticipate and adapt to these changes in sufficient time, in terms of the services provided and the networks used.

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The risks affecting other characteristics of the market in which the Group operates, such as a certain dependency on its network and equipment providers and the limitations which, specifically in the mobile telephone business, concern the limitation of the radio spectrum capacity.

Environmental issues and risks related to the possible impact of certain opinions which suggest that radio electric emissions could be hazardous to the health.

The risks specific to Telefónica Group.

Social-political risk (country risk) linked to the strong international presence of the Group, especially in Latin America, means the Company is affected by the risks typical of investment in economies in emerging countries, such as: the possibility that political changes may occur which can affect the economic or business conditions of the market in which they operate; the possible devaluation of local currency or the imposition of restrictions on capital movements; the effects of inflation and/or the possible devaluation of local currency; the possible state expropriation or nationalisation of assets; the possible imposition of excessive taxes or tax rates; the possible amendment of the terms under which the services in these markets are provided.

Risks of a financial nature, mainly related to exchange or interest rate risk management.

The risks involved in the investment models adopted in some countries, mainly in those carried out through joint ventures, in which Telefónica maintains a significant shareholding but not control. The risks inherent to business mergers and acquisitions, for example the acquisition in January 2006 of the British mobile telephone operator O2 and in April 2006 of Colombia Telecom).

The risks derived from a certain dependency on external financing sources, which in certain situations could limit the Company's capacity to access these funds or at least to obtain financing at acceptable interest rates.

The risks associated to litigation and other legal procedures.

Forecast business performance

Telefónica is an integrated telecommunications company with a presence in Spain, in most of Latin America, the United Kingdom, Germany, Czech Republic, Ireland, Slovak Republic and Morocco. We also have holdings in China Netcom and Telecom Italia which gives us the possibility of strategic agreements which we expect can only be positive for our shareholders as well as our customers.

In the past few years Telefónica has undergone a significant transformation, not only through its extensive geographical diversification and product mix but also by transforming its operational model to make it more efficient without losing sight of the customer and our ambitious growth plans. This operational model has centered on the integration of fixed and mobile business to have an integral business vision, of the processes and technology and it has been based on a regional focus which permits us to harness the synergies of scale without forgetting the importance of local management being the ones closest to the customer. We strive to lead the future of the sector by anticipating trends towards the new digital environment.

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In Spain, Telefónica is intensifying its commercial product range focusing on providing better quality services, and improving distribution channels and networks, enabling us to raise levels of customer satisfaction. Through market segmentation, we offer bundled services to the residential market, with voice, broadband and TV services tailored to suit customer needs. In the business and company sector we offer integral solutions including voice, broadband, network connections, equipment, support and maintenance, and different value added services such as web hosting and domains, with the aim of achieving the best global product range adapted to business needs. Furthermore, we will continue to defend our mobile leadership supported by our customer loyalty. The big challenge, in both the fixed and mobile businesses, continues to be improving the penetration growth of broadband and for this we will continue to transform our networks increasing UMTS coverage and taking the first steps in fiber optics in the case of fixed business.

In Latin America, our strategy is based on a regional model that harnesses the synergies of scale without losing sight of the local customer management. The growth in Latin America will come mainly from the mobile business, which is why we will continue to make significant investments to improve capacity and coverage through the technological advancements in our networks. The fixed networks are also being improved to drive the increase of quality broadband penetration with integrated voice and TV.

In Europe we will continue to improve customer satisfaction by strengthening our mobile offering in the United Kingdom and ADSL in Germany. We will continue to support the mobile data business and to offer the best and most innovative products to our customers. An example of this is the iPhone in the United Kingdom and the launch of the Fonic brand in Germany to satisfy a niche in the market we had previously left uncovered. We will also invest further in increasing and developing our own networks with the aim of substantially improving profitability through efficient cost management. In the Czech Republic we will continue to take advantage of the opportunities from a totally integrated operation, while maintaining our solid position in the mobile sector.

We are therefore confident that this company will continue to offer an unbeatable combination of growth and profitability, which permits us to keep our promises to the shareholders and at the same time offer the best solutions to our customers.

Events subsequent to year end

Significant events affecting Telefónica taking place from December 31, 2007 to the date of preparation of these financial statements included:

EIB financing

On January 15, 2008 Telefónica Finanzas, S.A. paid off at maturity the balance on the 200 million dollar loan taken out with the European Investment Bank (EIB) on January 9, 1998, guaranteed by Telefónica.

On January 17, 2008, Telefónica Finanzas, S.A. arranged a 75 million euro facility (Tranche B of the Telefónica Mobile Telephony II project) with a bank guarantee and counterguarantees by Telefónica maturing January 29, 2016.

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On January 30, 2008 Telefónica Finanzas, S.A. drew down the amounts of the facilities arranged with the EIB on December 3, 2007 and January 17, 2008 of 375 and 75 million euros, respectively, comprising Tranches A and B of the Telefónica Mobile Telephony II project.

Dividend received from Telefónica O2 Europe, Plc.

On February 14, 2008, Telefónica O2 Europe Plc paid the interim dividend charged against 2007 profit granted to Telefónica, S.A. for 2,000 million pounds sterling.

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AUDIT REPORT

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TELEFÓNICA, S.A. AND SUBSIDIARIES

**Consolidated Financial Statements and Consolidated Management Report
for the year ended
December 31, 2007**

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Translation of a report and financial statements originally issued in Spanish. In the event of a discrepancy, the Spanish-language version prevails (see Note 25)

AUDIT REPORT ON THE CONSOLIDATED FINANCIAL STATEMENTS

To the Shareholders of
Telefónica, S.A.

1. We have audited the consolidated financial statements of Telefónica, S.A. and subsidiaries, which comprise the consolidated balance sheet at December 31, 2007, the consolidated income statement, consolidated cash flow statement and consolidated statement of recognized income and expense and the notes thereto for the year then ended, the preparation of which is the responsibility of the Parent Company's Directors. Our responsibility is to express an opinion on the aforementioned consolidated financial statements taken as a whole, based upon work performed in accordance with auditing standards generally accepted in Spain, which require the examination, through the performance of selective tests, of the evidence supporting the consolidated financial statements, and the evaluation of their presentation, of the accounting principles applied, and of the estimates made.

2. In accordance with mercantile law, for comparative purposes the Parent Company's Directors have included for each of the captions included in the consolidated balance sheet, consolidated income statement, consolidated cash flow statement, consolidated statement of recognized income and expense and the notes thereto, in addition to the figures of 2007, those of 2006. Likewise for comparative purposes, the Parent Company's Directors have voluntarily included the 2005 figures of the consolidated income statement, consolidated cash flow statement, consolidated statement of recognized income and expense and the notes thereto. As explained in Note 2 of the notes to the accompanying consolidated financial statements, the 2005 figures were modified in 2006, and therefore differ from those included in the consolidated financial statements approved for the year 2005. Our opinion refers only to the consolidated financial statements for 2007. On March 1, 2007 and March 1, 2006, we issued our audit report on the 2006 and 2005 consolidated financial statements, respectively, in which we expressed an unqualified opinion.

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3. In our opinion, the accompanying 2007 consolidated financial statements give a true and fair view, in all material respects, of the consolidated equity and consolidated financial position of Telefónica, S.A. and subsidiaries at December 31, 2007 and the consolidated results of its operations, consolidated cash flows and consolidated recognized income and expense for the year then ended, and contain the required information necessary for their adequate interpretation and comprehension, in conformity with the international financial reporting standards adopted by the European Union, applied in the preparation of the two previous years' figures which are presented for purposes of comparison.

4. The accompanying consolidated management report for the year ended December 31, 2007 contains such explanations as the Parent Company's Directors consider appropriate concerning the situation of Telefónica, S.A. and subsidiaries, the evolution of their business and other matters, and is not an integral part of the consolidated financial statements. We have checked that the accounting information included in the consolidated management report mentioned above agrees with the 2007 consolidated financial statements. Our work as auditors is limited to verifying the consolidated 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 accounting records of the consolidated companies.

ERNST & YOUNG, S.L.

/s/ José Luis Perelli Alonso

José Luis Perelli Alonso

February 28, 2008

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**TELEFÓNICA, S.A. AND SUBSIDIARIES COMPOSING
THE TELEFÓNICA GROUP
CONSOLIDATED FINANCIAL STATEMENTS
(CONSOLIDATED ANNUAL ACCOUNTS) AND
CONSOLIDATED MANAGEMENT REPORT FOR 2007**

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TELEFÓNICA GROUP
CONSOLIDATED BALANCE SHEETS AS AT DECEMBER 31
(MILLIONS OF EUROS)

ASSETS	NOTE	2007	2006
A) NON-CURRENT ASSETS		87,395	91,269
Intangible assets	(Note 6)	18,320	20,758
Goodwill	(Note 7)	19,770	21,739
Property, plant and equipment	(Note 8)	32,460	33,887
Investment properties		9	1
Investments in associates	(Note 9)	3,188	959
Non-current financial assets	(Note 13)	5,819	5,224
Deferred tax assets	(Note 17)	7,829	8,701
B) CURRENT ASSETS		18,478	17,713
Inventories		987	1,012
Trade and other receivables	(Note 11)	9,662	9,666
Current financial assets	(Note 13)	1,622	1,680
Tax receivables	(Note 17)	1,010	1,554
Cash and cash equivalents	(Note 13)	5,065	3,792
Non-current assets held for sale		132	9
TOTAL ASSETS (A + B)		105,873	108,982
EQUITY AND LIABILITIES	NOTE	2007	2006
A) EQUITY	(Note 12)	22,855	20,001
Equity attributable to equity holders of the parent		20,125	17,178
Minority interests		2,730	2,823
B) NON-CURRENT LIABILITIES		58,044	62,645
Interest-bearing debt	(Note 13)	46,942	50,676
Trade and other payables	(Note 14)	1,015	982
Deferred tax liabilities	(Note 17)	3,926	4,700
Provisions	(Note 15)	6,161	6,287
C) CURRENT LIABILITIES		24,974	26,336

Interest-bearing debt	(Note 13)	6,986	8,381
Trade and other payables	(Note 14)	14,556	13,953
Current tax payables	(Note 17)	2,157	2,841
Provisions	(Note 15)	1,275	1,161

TOTAL EQUITY AND LIABILITIES (A+B+C)		105,873	108,982
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The accompanying Notes 1 to 25 and Appendices I to IV are an integral part of these consolidated financial statements.

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**TELEFÓNICA GROUP
CONSOLIDATED INCOME STATEMENTS
FOR THE YEARS ENDED DECEMBER 31
(MILLIONS OF EUROS)**

INCOME STATEMENT	NOTE	2007	2006	2005
Revenues from operations	(Note 19)	56,441	52,901	37,383
Other income	(Note 19)	4,264	1,571	1,416
Supplies		(17,907)	(16,629)	(9,999)
Personnel expenses	(Note 19)	(7,893)	(7,622)	(5,532)
Other expenses	(Note 19)	(12,081)	(11,095)	(8,212)
OPERATING INCOME BEFORE DEPRECIATION AND AMORTIZATION		22,824	19,126	15,056
Depreciation and amortization	(Note 19)	(9,436)	(9,704)	(6,693)
OPERATING INCOME		13,388	9,422	8,363
Share of profit (loss) of associates	(Note 9)	140	76	(128)
Finance income		703	1,082	630
Exchange gains		4,645	4,513	4,317
Finance expenses		(3,554)	(3,877)	(2,420)
Exchange losses		(4,638)	(4,452)	(4,155)
Net financial expense	(Note 16)	(2,844)	(2,734)	(1,628)
PROFIT BEFORE TAXES FROM CONTINUING OPERATIONS		10,684	6,764	6,607
Corporate income tax	(Note 17)	(1,565)	(1,781)	(1,904)
PROFIT FOR THE YEAR FROM CONTINUING OPERATIONS		9,119	4,983	4,703
Profit after taxes from discontinued operations	(Note 18)		1,596	124

PROFIT FOR THE YEAR		9,119	6,579	4,827
Minority interests	(Note 12)	(213)	(346)	(381)
PROFIT FOR THE YEAR ATTRIBUTABLE TO EQUITY HOLDERS OF THE PARENT		8,906	6,233	4,446
Basic and diluted earnings per share for continuing operations attributable to equity holders of the parent (euros)	(Note 19)	1,872	0,973	0,898
Basic and diluted earnings per share attributable to equity holders of the parent (euros)	(Note 19)	1,872	1,304	0,913

The accompanying Notes 1 to 25 and Appendices I to IV are an integral part of these consolidated financial statements.

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TELEFÓNICA GROUP
CONSOLIDATED CASH FLOW STATEMENTS
FOR THE YEARS ENDED DECEMBER 31
(MILLIONS OF EUROS)

	NOTE	2007	2006	2005
Cash flows from operating activities				
Cash received from customers		67,129	60,285	44,353
Cash paid to suppliers and employees		(47,024)	(41,475)	(30,532)
Dividends received		124	76	71
Net interest and other financial expenses paid		(3,221)	(2,372)	(1,520)
Taxes paid		(1,457)	(1,100)	(1,233)
Net cash from operating activities	(Note 23)	15,551	15,414	11,139
Cash flows from investing activities				
Proceeds on disposals of property, plant and equipment and intangible assets		198	129	113
Payments on investments in property, plant and equipment and intangible assets		(7,274)	(6,933)	(4,423)
Proceeds on disposals of companies, net of cash and cash equivalents disposed		5,346	2,294	502
Payments on investments in companies, net of cash and cash equivalents acquired		(2,798)	(23,757)	(6,571)
Proceeds on financial investments not included under cash equivalents		14	109	148
Payments made on financial investments not included under cash equivalents		(179)	(220)	(18)
Interest received		74	312	625
Capital grants received		27	14	32
Net cash flows used in investing activities	(Note 23)	(4,592)	(28,052)	(9,592)
Cash flows from financing activities				
Dividends paid	(Note 12)	(3,345)	(3,196)	(2,768)
Operations with equity holders		(2,152)	(2,346)	(2,055)
Proceeds on issue of debentures and bonds	(Note 13)	4,209	13,528	875
Proceeds on loans, credits and promissory notes		6,658	30,489	16,534
Cancellation of debentures and bonds	(Note 13)	(1,756)	(1,668)	(3,697)
Repayments of loans, credits and promissory notes		(13,039)	(22,235)	(9,324)
Net cash flow (used in) from financing activities	(Note 23)	(9,425)	14,572	(435)

Effect of foreign exchange rate changes on collections and payments		(261)	(372)	166
Effect of changes in consolidation methods and other non-monetary effects			28	10
Net increase in cash and cash equivalents during the year		1,273	1,590	1,288
CASH AND CASH EQUIVALENTS AT THE BEGINNING OF THE YEAR		3,792	2,202	914
CASH AND CASH EQUIVALENTS AT THE END OF THE YEAR	(Note 13)	5,065	3,792	2,202
RECONCILIATION OF CASH AND CASH EQUIVALENTS WITH THE BALANCE SHEET				
BALANCE AT THE BEGINNING OF THE YEAR		3,792	2,202	914
Cash on hand and at banks		2,375	1,555	855
Other cash equivalents		1,417	658	59
Bank overdrafts (1)			(11)	
BALANCE AT THE END OF THE YEAR	(Note 13)	5,065	3,792	2,202
Cash on hand and at banks		2,820	2,375	1,555
Other cash equivalents		2,245	1,417	658
Bank overdrafts (1)				(11)

(1) Included under Interest-bearing debt under current liabilities on the consolidated balance sheet.

The accompanying Notes 1 to 25 and Appendices I to IV are an integral part of these consolidated financial statements.

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TELEFÓNICA GROUP
CONSOLIDATED STATEMENTS OF RECOGNIZED INCOME AND EXPENSE
FOR THE YEARS ENDED DECEMBER 31
(MILLIONS OF EUROS)

	NOTE	2007	2006	2005
Gain (loss) on available-for-sale investments		32	584	(80)
Gain (loss) on hedges		892	10	(126)
Translation differences		(1,375)	(407)	2,577
Actuarial gains and losses and impact of limit on assets for defined benefit pension plans	(Note 15)	54	112	
Share of income (loss) directly recognized in equity of associates		(3)	(153)	(50)
Tax effects of items recognized directly in equity		(296)	(138)	73
Net (loss) income recognized directly in equity		(696)	8	2,394
Profit for the year		9,119	6,579	4,827
Total income and expense recognized in the year	(Note 12)	8,423	6,587	7,221
Attributable to:				
Equity holders of the parent	(Note 12)	8,158	6,346	6,397
Minority interests	(Note 12)	265	241	824
		8,423	6,587	7,221

The accompanying Notes 1 to 25 and Appendices I to IV are an integral part of these consolidated financial statements.

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TELEFÓNICA, S.A. AND SUBSIDIARIES COMPOSING THE TELEFÓNICA GROUP
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (CONSOLIDATED ANNUAL ACCOUNTS)
FOR THE YEAR ENDED DECEMBER 31, 2007

(1) INTRODUCTION AND GENERAL INFORMATION

Telefónica Group organizational structure

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

The parent company of this Group is Telefónica, S.A. (Telefónica), incorporated on April 19, 1924. Its registered office is at calle Gran Vía 28, Madrid (Spain).

Appendix IV lists the main subsidiaries, associates and investees in which the Telefónica Group has direct or indirect holdings, their lines of business, registered offices, equity and results at year end, gross carrying amounts, contribution to reserves of the Consolidated Group and the consolidation method used.

Corporate structure of the Group

Telefónica's basic corporate purpose, pursuant to Article 4 of its bylaws, is the provision of all manner of public or private telecommunications services, including ancillary or complementary telecommunications services or related services. All the business activities that constitute this stated corporate purpose may be performed either in Spain or abroad and wholly or partially by the Company, either through shareholdings or equity interests in other companies or legal entities with an identical or a similar corporate purpose.

The Telefónica Group follows a regional, integrated management model based on three business areas by geographical market and combining the wireline and wireless telephony businesses:

Telefónica Spain

Telefónica Latin America

Telefónica Europe

The business activities carried out by most of the Telefónica Group companies are regulated by broad ranging legislation, pursuant to which permits, concessions or licenses must be obtained in certain circumstances to provide the various services.

In addition, certain wireline and wireless telephony services are provided under regulated rate and price systems.

A more detailed presentation of the activities by segments carried out by the Group is provided in Note 4.

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(2) BASIS OF PRESENTATION OF THE CONSOLIDATED FINANCIAL STATEMENTS

The accompanying consolidated financial statements were prepared from the accounting records of Telefónica, S.A. and of each of the companies composing the Telefónica Group, which were prepared in accordance with the International Financial Reporting Standards (IFRS) adopted by the European Union, which for the purposes of the Telefónica Group are not different from those issued by the International Accounting Standards Board (IASB), to give a true and fair view of the equity, financial position, results of operations and cash flow generated and used and recognized income and expense in 2007. The figures in these consolidated financial statements are expressed in millions of euros unless indicated otherwise. The euro is the Group's functional currency.

The accompanying consolidated financial statements for the year ended December 31, 2007 were prepared by the Company's Board of Directors at its meeting on February 27, 2008 and will be submitted for approval at the General Shareholders' Meeting. The Board expects them to be approved without any modification.

Note 3 contains a detailed description of the most significant accounting policies used to prepare these consolidated financial statements.

For comparative purposes, the accompanying financial statements for 2007 include in the consolidated income statement, the consolidated cash flow statement, the consolidated statement of recognized income and expense and the related notes thereto for the year then ended, the figures for 2006 and, voluntarily, those of 2005.

Comparative information and changes in the consolidation scope

The main changes in the consolidation scope affecting comparability of the consolidated information for 2007 and 2006 (see Appendix I for a more detailed explanation of the changes in consolidation scope in both years and the main transactions in 2005) are as follows:

a) Sale of shareholding in Airwave O2, Ltd.

In April 2007, Telefónica O2 Europe, Plc, a wholly owned subsidiary of Telefónica, S.A., sold, through its subsidiary O2 Holdings, Ltd, 100% of the share capital of the UK company, Airwave O2, Ltd, for 1,932 million pounds sterling (equivalent to 2,841 million euros at the transaction date). The sale produced a gain of 1,296 million euros, recognized under "Other income" in the accompanying consolidated income statement (see Note 19).

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b) Sale of shareholding in Endemol Investment Holding, B.V.

In May 2007, Telefónica, S.A. signed an agreement to sell its 99.7% stake in Dutch company Endemol Investment Holding, B.V. to a consortium owned by Mediainco Cartera, S.L., Cyrte Fond II, B.V. and G.S. Capital Partners VI Fund, L.P, for 2,629 million euros. The transaction was carried out on July 3, producing a gain of 1,368 million euros, recognized under Other income in the accompanying consolidated income statement (see Note 19).

c) Acquisition of indirect shareholding in Telecom Italia

On April 28, 2007, Telefónica, S.A., together with its partners Assicurazioni Generali, S.p.A., Intesa Sanpaolo, S.p.A., Mediobanca, S.p.A. and Sintonía, S.A. (Benetton), entered into a Co-Investment Agreement and Shareholders Agreement which established the terms and conditions of their acquisition of an indirect shareholding in Telecom Italia, S.p.A. through an Italian company, called Telco, S.p.A., in which Telefónica has a 42.3% interest. Both agreements were modified on October 25, 2007 to include the Assicurazioni Generali Group companies and the Shareholders Agreement was further amended on November 19, 2007.

On October 25, 2007 Telco, S.p.A. acquired 100% of Olimpia, S.p.A., which held 17.99% of the voting shares of Telecom Italia, S.p.A. Also on that date, Assicurazioni Generali S.p.A. (together with its group companies Alleanza Assicurazioni S.p.A., INA Assitalia S.p.A., Volksfürsorge Deutsche Lebensversicherung A.G. and Generali Vie S.A.) and Mediobanca S.p.A. contributed a total share of 5.6% of Telecom Italia S.p.A.'s voting shares (4.06% and 1.54%, respectively) to Telco S.p.A.

The Telefónica Group accounts for its investment in Telco, S.p.A. using the equity method.

On December 10, 2007, an agreement was reached to takeover and merge Olimpia S.p.A. into Telco S.p.A., making Telco S.p.A.'s entire stake in the voting shares of the Italian operator (23.6%) direct and leaving Telefónica with an indirect holding in the voting shares of Telecom Italia S.p.A. of 9.98% (6.88% of the dividend rights) for 2,314 million euros.

The Shareholders Agreement signed on April 28, 2007 contained a general clause whereby both Telefónica, at the shareholders meetings of Telco S.p.A. and Telecom Italia S.p.A., and the Telefónica directors appointed to the companies' respective boards, would abstain from participating in and voting at the meetings dealing with issues regarding the operations of telecommunications services by companies controlled by Telecom Italia S.p.A., in countries where there are legal or regulatory restrictions on the exercise of voting rights by Telefónica.

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Therefore, as indicated above, on November 19, 2007 the partners expanded on and detailed the Shareholders Agreement, as well as the bylaws of Telco S.p.A., to include the specific limitations imposed by the Brazilian telecommunications regulator (Agência Nacional de Telecomunicações, ANATEL), as initially posted on its website on October 23, 2007 and subsequently published on November 5, 2007 as ANATEL's Atto no. 68,276 dated October 31, 2007.

Pursuant to clause 8.5(a) of the Shareholders Agreement, on November 6, 2007 Telco, S.p.A. and Telefónica entered into a Call Option Agreement giving Telefónica the option to buy shares of Telecom Italia, S.p.A. in the event Telco S.p.A. adopted a resolution to sell or pledge shares of Telecom Italia, S.p.A. (or rights related to its shares, such as voting rights) by simple majority and Telefónica were the dissenting party, under the terms of the Shareholders Agreement.

d) Acquisition of O2

On January 23, 2006, Telefónica, S.A. stated that it had complied with all the requirements of the full takeover offer for O2 plc made on November 21, 2005, finalizing the acquisition of 100% of the company's shares.

The acquisition of the O2 Group cost 26,135 million euros (17,887 million pounds sterling) (see Note 5). The Telefónica Group includes the O2 Group in the consolidation scope using the full consolidation method from January 31, 2006.

e) Merger with Telefónica Móviles, S.A.

On July 29, 2006, Telefónica, S.A. took over and merged Telefónica Móviles, S.A., with the dissolution of Telefónica Móviles, S.A. and the block transfer of all its equity to Telefónica, S.A. To cover the share exchange, Telefónica delivered 244,344,012 of its treasury shares to the shareholders of Telefónica Móviles, S.A., representing approximately 7.08% of its share capital at that date (see Note 5).

f) Colombia de Telecomunicaciones, S.A. (Coltel)

In April 2006, Telefónica Internacional, S.A. acquired 50% plus one share in Colombian company Colombia Telecom, S.A. ESP in public tender for 289 million euros (see Note 5). The Telefónica Group consolidates this company using the full consolidation method.

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g) Sale of Telefónica Publicidad e Información, S.A. (TPI)

In July 2006, Telefónica, S.A. accepted the public takeover bid launched by Yell Group Plc for 100% of the shares of Telefónica Publicidad e Información, S.A. (TPI). It therefore accepted Yell's bid for the 216,269,764 shares Telefónica owned in TPI, representing 59.905% of the share capital, for a total amount of 1,838 million euros (see Note 18). The gain on the disposal, which amounted to 1,563 million euros, and the results contributed by the TPI Group through June 30, 2006 are recognized under Profit after taxes from discontinued operations in the Telefónica Group's consolidated income statement. In addition, to make the historical information comparable, the Telefónica Group's 2005 financial statements were restated to present the results of the TPI Group under the same heading (see Note 18).

Comparability of information due to changes in the definition of segments in 2006

As agreed at the Board of Directors Meeting held July 26, 2006, the Telefónica Group has modified the segment reporting with respect to the 2005 annual accounts, adapting it to the new regional management model (see Note 4).

(3) VALUATION CRITERIA

The main valuation methods used in preparing the accompanying consolidated financial statements are as follows:

a) Translation methodology

The financial statements of the Group's foreign subsidiaries were translated to euros at the year-end exchange rates, except for:

1. Capital and reserves, which were translated at historical exchange rates.
2. Income statements, which were translated at the average exchange rates for the year.
3. Cash flow statements, which were translated at the average exchange rate for the year.

Goodwill and balance sheet items remeasured to fair value when a stake is acquired in a foreign operation are recognized as assets and liabilities of the company acquired and therefore translated at the year-end exchange rate.

The exchange rate differences arising from the application of this method are included in Translation differences under Equity attributable to equity holders of the parent in the accompanying consolidated balance sheets, net of the portion of said differences attributable to minority interests, which is shown under Equity Minority interests. When a foreign operation is sold, totally or partially, or contributions are reimbursed, cumulative translation differences since January 1, 2004 -the IFRS transition date- recognized in equity are taken proportionally to the income statement as a gain or loss on the disposal.

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b) Foreign currency transactions

Monetary transactions denominated in foreign currencies are translated to euros at the exchange rates prevailing on the transaction date, and are adjusted at year end to the exchange rates then prevailing.

All realized and unrealized exchange gains or losses are included in the income statement for the year, with the exception of gains or losses arising from specific-purpose financing of foreign currency investments in investees designated as hedges of foreign currency risk to which these investments are exposed (see Note 3 i), and exchange gains or losses on intra-group loans considered part of investment in the foreign operation, which are recorded under Translation differences in the consolidated balance sheet.

c) Goodwill

For acquisitions occurring after January 1, 2004, the IFRS transition date, goodwill represents the excess of the acquisition cost over the acquirer's interest, at the acquisition date, in the fair values of identifiable assets, liabilities and contingent liabilities acquired from a subsidiary, associate or joint venture. After the initial measurement, goodwill is carried at cost, less any accumulated impairment losses.

In the transition to IFRS, Telefónica availed itself of the exemption allowing it not to restate business combinations taking place before January 1, 2004. As a result, the accompanying consolidated balance sheets include goodwill, net of amortization deducted until December 31, 2003, arising before the IFRS transition date, from the positive consolidation difference between the amounts paid to acquire shares of consolidated subsidiaries, and their carrying amounts plus increases in the fair value of assets and liabilities acquired.

In all cases, goodwill is recognized as an asset denominated in the currency of the company acquired.

Goodwill is tested for impairment annually or more frequently if there are certain events or changes indicating the possibility that the carrying amount may not be fully recoverable.

The potential impairment loss is determined based on the recoverable amount of the cash-generating unit (or group of cash generating units) to which the goodwill is allocated when it arises. If this recoverable amount is less than the carrying amount, an irreversible impairment loss is recognized in income (see Note 3 f).

d) Intangible assets

Intangible assets are stated at acquisition or production cost, less any accumulated amortization or any accumulated impairment losses.

The useful lives of intangible assets are assessed on a case-by-case basis to be either finite or indefinite. Intangible assets with finite lives are amortized systematically over the useful economic life and assessed for impairment whenever there is an indication that the carrying amount may not be recoverable. Intangible assets with indefinite useful lives are not amortized, but are tested for impairment annually, or more frequently in the event of indications that their carrying amount may not be recoverable (see Note 3 f).

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The Company's management reassesses the indefinite useful life classification of these assets each year.

Amortization methods and schedules are revised annually at year end and, where appropriate, adjusted prospectively.

Research and development expenses

Research costs are expensed as incurred. Costs incurred in developing new products to be marketed or used for the Group's own network, and whose future economic viability is reasonably certain, are capitalized and amortized on a straight-line basis over the period during which the related project is expected to generate economic benefits, starting upon its completion.

Recoverability is considered to be reasonably assured when the Group can demonstrate the technical feasibility of completing the intangible asset, whether it will be available for internal use or sale, its intention to complete and its ability to use or sell the asset and how the asset will generate future economic benefits.

As long as intangible assets developed internally are not in use, the associated capitalized development costs are tested for impairment annually, and more frequently if there are indications that carrying amount may not be fully recoverable. Costs incurred in connection with projects that are not economically viable are charged to the consolidated income statement for the year in which this circumstance becomes known.

Administrative concessions

These relate to the acquisition cost of the licenses granted to the Telefónica Group by various public authorities to provide telecommunications services and to the value assigned to licenses held by certain companies at the time they were included in the Telefónica Group.

These concessions are amortized on a straight-line basis over the duration of related licenses from the moment commercial exploitation commences.

Customer base

This represents the allocation of acquisition costs attributable to customers acquired in business combinations. Amortization is recognized on a straight-line basis over the estimated period of the customer relationship.

Industrial property and software

These items are stated at cost and are amortized on a straight-line basis over their useful life, generally estimated at three years.

e) Property, plant and equipment

Property, plant and equipment is stated at cost less any accumulated depreciation and any accumulated impairment in value. Land is not depreciated.

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Cost includes external and 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 revenues under Internal expenditures capitalized and Other income. Cost includes, where appropriate, the estimate of decommissioning, withdrawal and site reconditioning costs when they correspond to obligations arising as a result of the use of the related assets

Interest and other financial expenses incurred and directly attributable to the acquisition or construction of qualifying assets are capitalized. Qualifying assets at the Telefónica Group are those assets that require preparation of at least 18 months for their intended use or sale.

The costs of expansion, modernization or improvement leading to increased productivity, capacity or efficiency or to a lengthening of the useful lives of assets are capitalized when recognition requirements are met.

Upkeep and maintenance expenses are expensed as incurred.

The Telefónica Group assesses the need to write down, if appropriate, the carrying amount of each item of property, plant and equipment to its recoverable amount at each year end, whenever there are indications that the assets' carrying amount may not be fully recoverable through the generation of sufficient revenues to cover all the costs and expenses. The impairment provision is not maintained if the factors giving rise to the impairment disappear (see Note 3 f).

The Group's subsidiaries depreciate their property, plant and equipment once they are in full working condition using the straight-line method based on the assets' estimated useful lives, calculated in accordance with technical studies which are revised periodically based on technological advances and the rate of dismantling, as follows:

	Years of estimated useful life
Buildings	25 40
Plant and machinery	10 15
Telephone installations, networks and subscriber equipment	5 20
Furniture, tools and other items	2 10

Assets' estimated residual values and methods and depreciation periods are reviewed, and adjusted prospectively at each financial year end, if necessary.

Table of Contents***f) Impairment of non-current assets***

Non-current assets, including goodwill and intangible assets are evaluated at each balance sheet date for indications of impairment losses. Wherever such indications exist, or for assets requiring annual impairment testing, the Company estimates the asset's recoverable value as the higher of fair value less costs to sell or value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects the time value of money and the risks specific to the asset. An asset is considered to be impaired when its recoverable amount is less than its carrying amount. In this case, the carrying amount is written down to the recoverable amount and the resulting loss is taken to the income statement. Future depreciation charges are adjusted for the new carrying amount for the asset's remaining useful life. The Company carries out asset impairment tests on an individual asset basis, except when the cash flows generated by the assets are not independent of those from other assets (cash-generating units).

The Company bases the calculation of impairment on the business plans of the various cash-generating units to which the assets are allocated. These business plans generally cover five years. For longer periods, an expected constant or decreasing growth rate is applied to the projections based on these plans from the fifth year.

Pre-tax discount rates adjusted for country and business risks are applied. The Company used the following rates in 2007 and 2006:

Rates	2007	2006
Businesses in Spain	7.0%-11.3%	7.0%-10.6%
Businesses in Latin America	8.1%-18.6%	7.7%-17.6%
Businesses in Europe	7.7%-8.1%	7.2%-9.1%

When there are new events or changes in circumstances that indicate that a previously recognized impairment loss no longer exists or has been decreased, a new estimate of recoverable amount is made. A previously recognized impairment loss is only reversed if there has been a change in the estimates used to determine the asset's recoverable amount since the last impairment loss was recognized. If that is the case, the carrying amount of the asset is increased to its recoverable amount. This revised amount cannot exceed the carrying amount that would have been determined, net of depreciation, had no impairment loss been recognized for the asset in prior years. Such reversal is recognized in profit or loss and the depreciation charge is adjusted in future periods to allocate the asset's revised carrying amount. Impairment losses relating to goodwill cannot be reversed in future periods.

g) Leases

The determination of whether an arrangement is, or contains a lease is based on the substance of the agreement and requires an assessment of whether the fulfillment of the arrangement is dependent on the use of a specific asset and the agreement conveys a right to the Telefónica Group to use the asset.

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Leases where the lessor retains substantially all the risks and benefits of ownership of the asset are classified as operating leases. Operating lease payments are recognized as an expense in the income statement on a straight-line basis over the life of the lease.

Leases are classified as finance leases when the terms of the lease transfer substantially all the risks and rewards incidental to ownership of the leased item to the Group. These are classified at the inception of the lease, in accordance with its nature and the associated liability, at the lower of the present value of the minimum lease payments or the fair value of the leased property. Lease payments are apportioned between the finance charges and reduction of the lease liability so as to achieve a constant rate of interest on the remaining balance of the liability. Finance charges are charged directly against income over the lease term.

h) Investments in associates

The Telefónica Group's investments in companies in which it has significant influence (either through a presence on the Board of Directors or through agreements with shareholders), but which are neither a subsidiary nor a joint venture, are accounted for using the equity method. The carrying amount of investments in associates includes related goodwill and the consolidated income statement reflects the share of profit or loss from operations of the associate. If the associate recognizes any gains or losses directly in equity, the Group also recognizes the corresponding portion of these gains or losses directly in its equity.

i) Financial assets and liabilities

Financial assets

All typical way purchases and sales of financial assets are recognized on the balance sheet on the trade date, which is the date that the Group commits to purchase or sell the asset. The Telefónica Group classifies its financial instruments into four categories for initial recognition purposes: financial assets at fair value through profit or loss, loans and receivables, held-to-maturity investments and available-for-sale financial assets. Where appropriate, the Group re-evaluates the designation at each financial year end.

Financial assets held for trading, i.e., investments made with the aim of realizing short-term returns as a result of price changes, are included in the category financial assets at fair value through profit or loss and presented as current assets. All derivatives fall under this category, unless they are designated as effective hedging instruments. The Group also classifies certain financial instruments under this category when doing so eliminates or mitigates measurement or recognition inconsistencies that could arise from the application of other criteria for measuring assets and liabilities or for recognizing gains and losses on different bases. Also in this category are financial assets for which an investment and disposal strategy have been designed based on their fair value. Financial instruments included in this category are recorded at fair value and are remeasured at subsequent reporting dates at fair value, with any realized or unrealized gains or losses taken to the income statement.

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Financial assets with a fixed maturity that the Company has the positive intention and ability (legal and financial) to hold until then are classified as held-to-maturity and presented as Current assets or Non-current assets, depending on the time left until settlement. Financial assets falling into this category are carried at amortized cost using the effective interest rate method, with gains and losses recognized in the income statement at settlement or upon impairment, as well as due to scheduled amortization.

Financial assets which the Company intends to hold for an unspecified period of time and could be sold at any time to meet specific liquidity requirements or in response to interest-rate movements are classified as available-for-sale. These instruments are recorded as Non-current assets unless it is probable and feasible that they will be sold within 12 months. Available-for-sale investments are measured at fair value. Gains or losses arising from changes in fair value are recognized in equity until the asset is derecognized or is determined to be impaired, at which time the cumulative gain or loss previously reported in equity is taken to the income statement. Dividends from available-for-sale shareholdings are taken to the income statement once the Company has the right to receive the dividend. Fair value is determined in accordance with the following criteria:

1. Listed securities on active markets:

Fair value is considered to be the market value on the closing date.

2. Unlisted securities:

Fair value is determined using valuation techniques such as discounted cash flow analysis, option valuation models, or by referring to comparable transactions. When fair value cannot be determined reliably, these investments are carried at cost.

Loans and receivables include financial assets that are not traded on organized markets and do not fall into any of the previous categories. These assets are carried at amortized cost using the effective interest rate method. Gains and losses are taken to the income statement when the assets are derecognized or determined to be impaired, as well as due to scheduled amortization.

Trade receivables are recognized at original invoice amount less an allowance for uncollectible amounts. A provision is made when there is objective evidence that the Group will not be able to collect the debts. The provision is calculated as the difference between the carrying amount of the doubtful trade receivables and their recoverable amount. As a general rule, short-term commercial bills are not discounted.

Financial instruments are subject to impairment testing at each balance sheet date. If there is objective evidence that an impairment loss on a financial asset carried at amortized cost has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future losses that have not been incurred), discounted at the financial asset's original effective interest rate. If there is objective evidence that an available-for-sale financial instrument is impaired, an amount comprising the difference between its cost (net of any principal payments and amortization) and its current fair value, less any impairment loss previously recognized in profit or loss, is transferred from equity to the income statement.

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Financial assets are only fully or partially derecognized where:

1. The rights to receive cash flows from the asset have expired;
2. The Company has assumed an obligation to pay the cash flows received from the asset to a third party;
or
3. The Company has transferred its rights to receive cash flows from the asset to a third party, transferring substantially all the risks and rewards of the asset.

Cash and cash equivalents

Cash and cash equivalents comprise cash on hand and at banks, demand deposits and other highly liquid investments with an original maturity of three months or less. These items are stated at historical cost, which does not differ significantly from realizable value.

For the purpose of the consolidated cash flow statement, cash and cash equivalents are shown net of any outstanding bank overdrafts.

Preferred stock

Preferred shares are classified as a liability or equity instrument depending on the issuance terms. A preferred share issue is considered equity only when the issuer is not obliged to give cash or another financial instrument in the form of either principal repayment or dividend payment, whereas it is recorded as a financial liability on the balance sheet whenever the Telefónica Group does not have the right to avoid cash payments.

Interest-bearing debt

These debts are recognized initially at the fair value of the consideration received less directly attributable transaction costs. After initial recognition, interest-bearing debt is subsequently measured at amortized cost using the effective interest rate method. Any difference between the cash received (net of transaction costs) and the repayment value is recognized in the income statement over the life of the debt. Interest-bearing debt is considered non-current when its maturity is over 12 months or the Telefónica Group has full discretion to defer settlement for at least another 12 months from the balance sheet date.

Financial liabilities are derecognized when the obligation under the liability is discharged, cancelled or expires. Where an existing financial liability is replaced by another from the same lender under substantially different terms, such an exchange is treated as a derecognition of the original liability and the recognition of a new liability, and the difference between the respective carrying amounts is recognized in profit or loss.

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Derivative financial instruments and hedge accounting

Derivative financial instruments are initially recognized at fair value, normally equivalent to cost. Their carrying amounts are subsequently remeasured at fair value. Derivatives are recorded as assets when the fair value is positive and as liabilities when the fair value is negative. They are classified as current or non-current depending on whether they fall due within less than or after one year, respectively. Derivatives that meet all the criteria for consideration as instruments hedging long-term items are recorded as non-current assets when fair value is positive and liabilities when fair value is negative.

The accounting treatment of any gain or loss resulting from changes in the fair value of a derivative depends on whether the derivative in question meets all the criteria for hedge accounting and, if appropriate, on the nature of the hedge.

The Group designates certain derivatives as:

1. Fair value hedges, when hedging the exposure of changes in the fair value of a recognized asset or liability;
2. Cash flow hedges, when hedging exposure to variability in cash flows that is either attributable to a particular risk associated with a recognized asset or liability or a highly probable forecast transaction; or
3. Hedges of net investment in a foreign operation.

A hedge of a foreign currency risk of a firm commitment is accounted for as either a fair value or a cash flow hedge.

Changes in fair value of derivatives that qualify as fair value hedges are recognized in the income statement, together with changes in the fair value of the hedged asset or liability attributable to the risk being hedged.

Changes in fair value of derivatives that qualify and have been assigned to hedge cash flows, which are highly effective, are recognized in equity. The portion considered ineffective is recognized immediately in income. Fair value changes from hedges that relate to firm commitments or forecast transactions that result in the recognition of non-financial assets or liabilities are included in the initial measurement of those assets or liabilities. Otherwise, changes in fair value previously recognized in equity are recognized in the income statement in the period in which the hedged transaction affects profit or loss.

An instrument designed to hedge foreign currency exposure from a net investment in a foreign operation is accounted for in a way similar to cash flow hedges.

The application of the Company's corporate risk-management policies could result in financial risk-hedging transactions that make economic sense, yet are not strictly IFRS compliant for hedge accounting. Alternatively, the Group may opt not to apply hedge accounting criteria in certain instances. In these cases, following the general rule, gains or losses resulting from changes in the fair value of derivatives are recognized directly in to the income statement. Transactions used to reduce the exchange rate risk relating to the income contributed by foreign subsidiaries are not treated as hedging transactions.

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From inception, the Group formally documents the hedging relationship between the derivative and the hedged item, as well as the associated risk management objectives and strategies. This documentation includes identification of the hedge instrument, the hedged asset, liability or transaction and the nature of the risk hedged. In addition, it states the manner in which hedge effectiveness, i.e. the extent to which the hedge instrument offsets any changes in the underlying hedged item's fair value or cash flows that can be attributed to the risk hedged, is measured. Its effectiveness is measured, prospectively and retroactively, both at the inception of the hedge relationship and on a systematic basis throughout the life of the hedge.

Hedge accounting is discontinued whenever the hedging instrument expires or is sold, terminated or settled, the hedge no longer meets the criteria for hedge accounting or the Group revokes the designation. In these instances, gains or losses accumulated in equity are not taken to the income statement until the forecast transaction or commitment affects profit or loss. However, if the hedged transaction is no longer expected to occur, the cumulative gains or losses recognized directly in equity are taken immediately to profit and loss.

The fair value of the derivative portfolio includes estimates based on calculations using observable market data, as well as specific pricing and risk-management tools commonly used by financial entities.

j) Inventories

Materials stored for use in investment projects and inventories for consumption and replacement are valued at the lower of weighted average cost and net realizable value.

When the cash flows associated with the purchase of inventory are effectively hedged, the corresponding gains and losses accumulated in equity become part of the cost of the inventories acquired.

Obsolete, defective or slow-moving inventories have been written down to estimated net realizable value. The recoverable amount of inventory is calculated based on the inventory's age and turnover.

k) Treasury shares

Treasury shares are stated at cost and as a reduction to equity. Any gain or loss obtained on the purchase, sale, issue or cancellation of treasury shares is recognized directly in equity.

l) Provisions

Pensions and other employee obligations

Provisions required to cover the accrued liability for defined benefit pensions are determined using the projected unit credit actuarial valuation method. The calculation is based on demographic and financial assumptions for each country considering the macroeconomic environment. The discount rates are determined based on market yield curves. Plan assets are measured at fair value. Actuarial gains and losses are recognized immediately in equity.

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For defined-contribution pension plans, the obligations are limited to the payment of the contributions, which are taken to the income statement as accrued.

Provisions for post-employment benefits (e.g. early retirement or other) are calculated individually based on the terms agreed with the employees. In some cases, these may require actuarial valuations based on both demographic and financial assumptions.

Other provisions

Provisions are recognized when the Group has a present obligation (legal or constructive), as a result of a past event, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation. When the Group expects some or all of a provision to be reimbursed, for example under an insurance contract, the reimbursement is recognized as a separate asset, but only when the reimbursement is virtually certain. The expense relating to any provision is presented in the income statement net of any reimbursement. If the effect of the time value of money is material, provisions are discounted, and the corresponding increase in the provision due to the passage of time is recorded as an interest expense.

m) Share-based payments

The Group has compensation systems linked to the market value of its shares, providing employees share options. Certain compensation plans are settled in cash or shares, at the option of the beneficiary, while others are settled via the delivery of shares.

In accordance with the transition to IFRS, share-based payment schemes granted prior to November 7, 2002 are measured in accordance with the criteria applied before the application of IFRS 2, consisting of recording a provision evenly throughout the duration of the plan based on the best estimate of the net future expenditure required to settle the obligation in accordance with its terms and conditions.

The following criteria are applied to share-based payment schemes granted after November 7, 2002:

Option plans that can be cash-settled or equity-settled at the option of the employee are recognized at the fair value on the grant date and divided into the liability and equity components of the compound instrument granted. Considering the terms and conditions of the share option plan, the fair value of each component is the same and, accordingly, the accounting treatment of plans of this nature is that established for cash-settled transactions. In these, the total cost of the rights granted is expensed over the vesting period with recognition of a corresponding liability. The total cost of cash-settled transactions is measured initially at fair value at the grant date using the Black-Scholes formula, taking into account the terms and conditions established in each share option plan. At each subsequent reporting date, the Company reviews its estimate of fair value and the number of options it expects to be exercised, remeasuring the liability, with any changes in fair value recognized in profit or loss.

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For equity-settled share option plans, fair value at the grant date is measured using a binomial model or benchmark securities. The cost is recognized, together with a corresponding increase in equity, over the vesting period. At each subsequent reporting date, the Company reviews its estimate of the number of options it expects to be exercised, with a corresponding adjustment to equity.

n) Corporate income tax

This heading in the accompanying consolidated income statement includes all the expenses and credits arising from the corporate income tax levied on the Spanish Group companies and similar taxes applicable to the Group's foreign operations.

The income tax expense of each year includes both current and deferred taxes, if any.

Current tax assets and liabilities for the current and prior periods are measured at the amount expected to be recovered from or paid to the taxation authorities. The tax rates and tax laws used to compute the amount are those that are enacted at the balance sheet date.

Deferred taxes are calculated based on balance sheet analysis of the temporary differences generated as a result of the difference between the tax bases of the assets and liabilities and their respective carrying amounts.

The main temporary differences arise due to differences between the tax basis and carrying amounts of plant, property and equipment, intangible assets, and non-deductible provisions, as well as differences in the fair value and tax bases of net assets acquired from a subsidiary, associate or joint venture.

Furthermore, deferred taxes arise from unused tax credits and tax loss carryforwards.

The Group determines deferred tax assets and liabilities by applying the tax rates that will be effective when the corresponding asset is received or the liability settled, based on tax rates and tax laws that are enacted (or substantively enacted) at the balance sheet date.

Deferred income tax assets and liabilities are not discounted to present value and are classified as non-current, irrespective of the date of their reversal.

The carrying amount of deferred income tax assets is reviewed at each balance sheet date and the necessary adjustments are made if there is uncertainty as to their recoverability. In addition, at each balance sheet date deferred tax assets not previously recognized are reviewed to determine whether they should be recognized to the extent that future taxable profit will allow the deferred tax asset to be recovered.

Deferred tax liabilities on investments in subsidiaries, branches, associates and joint ventures are not recognized if the parent company is in a position to control the timing of the reversal and if the reversal is unlikely to take place in the foreseeable future.

Income tax relating to items recognized in equity is recognized in equity. Deferred tax assets and liabilities resulting from business combinations are added to or deducted from goodwill.

Deferred tax assets and liabilities are offset only if a legally enforceable right exists to set off current tax assets against current tax liabilities and the deferred taxes relate to the same taxable entity and the same taxation authority.

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o) Revenue and expenses

Revenue and expenses are recognized on the income statement based on an accruals basis; i.e. at the moment the delivery of goods or services represented by them has occurred, regardless of when actual payment or collection occurs.

The Telefónica Group principally obtains revenues from providing the following telecommunications services: traffic, connection fees, regular (normally monthly) network usage fees, interconnection, network and equipment leasing, handset sales and other services, value-added services (e.g. text messaging) and maintenance. Products and services may be sold separately or in promotional packages (bundled).

Revenues from calls carried on Telefónica's networks (traffic) include an initial call establishment fee plus a rate per call, which varies depending on call length, distance and type of service. Both wireline and wireless traffic are recognized as revenue as service is provided. For prepaid calls, the amount of unused traffic generates a deferred revenue recognized in Trade and other payables on the liability side of the balance sheet. Prepaid cards generally expire within 12 months and any deferred revenue from prepaid traffic is taken directly to the income statement when the card expires as the Group has no obligation to provide service after this date.

Revenue from traffic sales and services at a fixed rate over a specified period of time (flat rate) are recognized on a straight-line basis over the period of time covered by the rate paid by the customer.

Connection fees arising when customers connect to the Group's network are deferred and taken to the income statement throughout the average estimated customer relationship period, which varies by type of service. All related costs, except those related to network enlargement expenses, administrative expenses and overhead, are recognized in the income statement as incurred.

Regular fees are taken to the income statement on a straight-line basis over the related period. Equipment leases and other services are taken to profit or loss as they are rendered.

Interconnection fees from wireline-wireless and wireless-wireline calls and other customer services are recognized in the period in which the calls are made.

Revenues from handset and equipment sales are recognized once the sale is considered complete, i.e., generally when delivered to the end customer.

In the wireless telephony business there are loyalty campaigns whereby customers obtain points for the telephone traffic they generate. The amount assigned to points awarded is deducted from revenue until the points are exchanged and recognized as net sales or services based on the product or service chosen by the customer. This exchange can be for discounts on the purchase of handsets, traffic or other types of services based on the number of points earned and the type of contract involved. The accompanying consolidated balance sheets include the related provision, based on an estimate of the value of the points accumulated at year end, under Trade and other payables.

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Bundle packages, which include different elements, are sold in the wireline, wireless and internet businesses. They are assessed to determine whether it is necessary to separate the different identifiable components and apply the corresponding revenue recognition policy to each component. Total package revenue is split among the identified components based on their respective fair values (i.e. the fair value of each component relative to the total fair value of the package).

As the non refundable connection fees may not be separated as identified components of this type of package, any amount received from the customer for this concept is assigned to the other components delivered. However, amounts that are contingent upon delivery of other components that have not been delivered may not be assigned to the other components delivered.

All expenses related to bundled promotional packages are taken to the income statement as incurred.

p) Use of estimates

The main assumptions concerning the future and other key sources of estimation uncertainty at the balance sheet date, that have a significant risk of causing a material adjustment on the carrying amounts of assets and liabilities within the the next financial year are discussed below.

A significant change in the facts and circumstances on which these estimates are based could have a material impact on the Group's results and financial position.

Property, plant and equipment, intangible assets and goodwill

The accounting treatment of property, plant and equipment and intangible assets entails the use of estimates to determine the useful life for depreciation and amortization purposes and to assess fair value at their acquisition dates for assets acquired in business combinations.

Determining useful life requires making estimates in connection with future technological developments and alternative uses for assets. There is a significant element of judgment involved in making technological development assumptions, since the timing and scope of future technological advances are difficult to predict.

When an item of property, plant and equipment or an intangible asset is considered to be impaired, the corresponding loss is taken to the income statement for the period. The decision to recognize an impairment loss involves estimates of the timing and amount of the impairment, as well as the reasons for the potential loss. Furthermore, additional factors, such as technological obsolescence, the suspension of certain services and other circumstantial changes are taken into account.

The Telefónica Group evaluates its cash-generating units' performance regularly to identify potential goodwill impairments. Determining the recoverable amount of the cash-generating units to which goodwill is allocated also entails the use of assumptions and estimates and requires a significant element of judgment.

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Deferred income tax

The Group assesses the recoverability of deferred tax assets based on estimates of future earnings. The ability to recover these taxes depends ultimately on the Group's ability to generate taxable earnings over the period for which the deferred tax assets remain deductible. This analysis is based on the estimated schedule for reversing deferred taxes, as well as estimates of taxable earnings, which are sourced from internal projections and are continuously updated to reflect the latest trends.

The appropriate classification of tax assets and liabilities depends on a series of factors, including estimates as to the timing and realization of deferred tax assets and the projected tax payment schedule. Actual Group company income tax receipts and payments could differ from the estimates made by the Group as a result of changes in tax legislation or unforeseen transactions that could affect tax balances.

Provisions

Provisions are recognized when the Group has a present obligation as a result of a past event, it is probable that an outflow of resources will be required and the amount of the liability can be measured reliably. This obligation may be legal or constructive, deriving from *inter alia* regulations, contracts, normal practices or public commitments that lead third parties to reasonably expect that the Group will assume certain responsibilities. The amount of the provision is determined based on the best estimate of the outflow of resources required to settle the obligation, bearing in mind all available information at the balance sheet date, including the opinions of independent experts such as legal counsel or consultants.

Given the uncertainties inherent in the estimates used to determine the amount of provisions, actual outflows of resources may differ from the amounts recognized originally on the basis of the estimates.

Revenue recognition

Connection fees

Connection fees, generated when customers connect to the Group's network, are deferred and recognized as revenue over the average estimated customer relationship period.

The estimate of the average estimated customer relationship period is based on the recent history of customer churn. Potential changes in estimates could lead to changes in both the amount and timing of the future recognition of revenues.

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Bundled offers

Bundled offers that combine different elements are assessed to determine whether it is necessary to separate the different identifiable components and apply the corresponding revenue recognition policy to each element. Total package revenue is split among the identified components based on their respective fair values.

Determining fair values for each identified component requires estimates that are complex due to the nature of the business.

A change in estimates of fair values could affect the apportionment of revenue among the components and income in future years.

q) Consolidation methods

The consolidation methods applied are as follows:

Full consolidation for companies over which the Company has control, either by exercising effective control or by virtue of agreements with the other shareholders.

Proportionate consolidation for companies which are jointly controlled with third parties (joint ventures). Similar items are grouped together such that the corresponding proportion of these companies overall assets, liabilities, expenses and revenues and cash flows are integrated line by line into the consolidated financial statements.

Equity consolidation for companies in which there is significant influence, but not control or joint control with third parties.

In certain circumstances, some of the Group's investees may require a qualified majority to adopt certain resolutions. This, together with other factors, is taken into account when selecting the consolidation method.

All material accounts and transactions between the consolidated companies were eliminated on consolidation. The returns generated on transactions involving capitalizable goods or services by subsidiaries with other Telefónica Group companies were eliminated on consolidation.

The financial statements of the consolidated companies have the same financial year end as the parent company's individual financial statements and are prepared using the same accounting policies. In the case of Group companies whose accounting and valuation methods differed from those of Telefónica, adjustments are made on consolidation in order to present the consolidated financial statements on a uniform basis.

The consolidated income statement and consolidated cash flow statement include the revenues and expenses and cash flows of companies that are no longer in the Group up to the date on which the related holding is sold or the company is liquidated, and those of the new companies included in the Group from the date on which the holding was acquired or the company was incorporated through year end.

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Revenues and expenses associated with discontinued operations are presented in a separate line on the consolidated income statement. Discontinued operations are those with identifiable operations and cash flows (for both operating and management purposes) and that represent a line of business or geographic unit which has been disposed of or is available for sale.

The value of the share of minority interests in the equity and results of the fully consolidated subsidiaries is presented under *Minority interests* on the consolidated balance sheet and income statement, respectively.

r) Acquisitions and disposals of minority interests

Acquisitions of minority interests

The Telefónica Group treats increases equity investments in companies already controlled by the Group via purchases from minority shareholders by recognizing any difference between the acquisition price and the carrying amount of the minority interest's participation as goodwill.

Disposals of investments in subsidiaries without relinquishing control

In transactions involving the sale of investments in subsidiaries in which the Group retains control, the Telefónica Group applies a consistent treatment to that described for acquisitions of investments from minority interests. This consists of derecognizing the carrying amount of the shareholding sold, including any related goodwill. The difference between this amount and the sale price is recognized as a gain or loss in the income statement.

Commitments to acquire minority interests (put options)

Put options granted to minority shareholders of subsidiaries are measured at the exercise price and classified as a financial liability, with a deduction from minority interests on the balance sheet. Where the exercise price exceeds the balance of minority interests, the difference is recognized as an increase in the goodwill of the subsidiary. At each balance sheet date, the difference is adjusted based on the exercise price of the options and the carrying amount of the minority interests.

Table of Contentss) ***New IFRS and interpretations of the International Financial Reporting Interpretations Committee (IFRIC)***

The following IFRS and IFRIC interpretations published have been adopted, with effective dates for the year ended December 31, 2007:

Standards and amendments	Mandatory application: annual periods beginning on or after
IFRS 7 <i>Financial Instruments: Disclosures</i>	January 1, 2007
IFRS 8 <i>Operating Segments</i>	January 1, 2009
Amendment to IAS 1 <i>Presentation of Financial Statements</i> <i>Capital Disclosures</i>	January 1, 2007
<i>Guidance for amended IFRS 4</i>	January 1, 2007
Interpretations	Mandatory application: annual periods beginning on or after
IFRIC 7 <i>Applying the Restatement Approach under IAS 29 Financial Reporting in Hyperinflationary Economies</i>	March 1, 2006
IFRIC 8 <i>Scope of IFRS 2 Share based payment</i>	May 1, 2006
IFRIC 9 <i>Reassessment of Embedded Derivatives</i>	June 1, 2006
IFRIC 10 <i>Interim Financial Reporting and Impairment</i>	November 1, 2006
The Company has opted for the early adoption of IFRS 8 <i>Operating Segments</i> . The adoption of these standards, amendments and interpretations has not had a significant impact on the Company's financial position or its consolidated results in the initial period of application, although it has entailed new disclosures in the accompanying consolidated financial statements.	

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At the date of preparation of the consolidated financial statements, the following IFRS and IFRIC interpretations have been published, but their application is not mandatory:

Standards and amendments		Mandatory application: annual periods beginning on or after
Amendment to IAS 23	<i>Borrowing Costs</i>	January 1, 2009 (*)
Amendment to IAS 1	<i>Revised Presentation of Financial Statements</i>	January 1, 2009
Amendments to IAS 32 and IAS 1	<i>Puttable instruments and Obligations Arising on Liquidation</i>	January 1, 2009
Revised IFRS 3	<i>Business Combinations</i>	July 1, 2009
Amendment to IAS 27	<i>Consolidated and Separate Financial Statements</i>	July 1, 2009
Amendment to IFRS 2	<i>Share-based Payment Vesting Conditions and Cancellations.</i>	January 1, 2009
Interpretations		Mandatory application: annual periods beginning on or after
IFRIC 11	<i>Group and Treasury Share Transactions</i>	March 1, 2007
IFRIC 12	<i>Service Concession Arrangements</i>	January 1, 2008
IFRIC 13	<i>Customer Loyalty Programs</i>	July 1, 2008
IFRIC 14	<i>IAS 19 The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction</i>	January 1, 2008

(*) Borrowing costs related to qualifying assets as of January 1, 2009.

The Group estimates that the application of the aforementioned standards, amendments and interpretations will not have a significant impact on its consolidated financial statements.

(4) SEGMENTED REPORTING

At its meeting of July 26, 2006, the Board of Directors of Telefónica agreed to restructure the Company's management to adapt to a new regional, integrated management model.

Combining the wireline and wireless telephony services underscores the need to manage the business by region in order to offer customers the best integrated solutions and support wireless-wireline convergence.

This vision prompted the Group to create three large business areas: Telefónica Spain, Telefónica Europe and Telefónica Latin America, with each overseeing the integrated business. This forms the basis of the segment reporting in these consolidated financial statements.

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Telefónica Spain oversees the wireline and wireless telephony, broadband, internet, data, broadband TV, value added services activities and their development in Spain.

Telefónica Latin America oversees the same businesses in Latin America.

Telefónica Europe oversees the wireline, wireless, broadband, value added services and data businesses in the UK, Germany, the Isle of Man, Ireland, the Czech Republic and the Republic of Slovakia.

The Telefónica Group is also involved in media and contact center businesses through investments in Telefónica de Contenidos and Atento, included under Other and inter-group eliminations together with the consolidation adjustments.

The segment reporting takes into account the impact of the purchase price allocation (PPA) to assets acquired and the liabilities assumed from the companies included in each segment. The assets and liabilities presented in each segment are those managed by the heads of each segment.

The Telefónica Group manages its borrowing activities and tax implications centrally. Therefore, it does not disclose the related assets, liabilities, revenue and expenses breakdown by reportable segments.

Inter-segment transactions are carried out at arm's length prices.

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Key information for these segments is as follows:

Millions of euros	Telefónica Spain	2007 Telefónica Latin America	Telefónica Europe	Other & inter-group eliminations	Total
External sales	20,423	19,901	14,417	1,700	56,441
Inter-segment sales	260	177	41	(478)	
Other operating income and expenses	(11,235)	(12,957)	(9,481)	(**) 56	(33,617)
OIBDA (*)	9,448	7,121	4,977	1,278	22,824
Depreciation and amortization	(2,381)	(3,559)	(3,386)	(110)	(9,436)
OPERATING INCOME	7,067	3,562	1,591	1,168	13,388
INVESTMENT IN PP&E	2,381	3,343	2,125	178	8,027
INVESTMENT IN ASSOCIATES	95	70		3,023	3,188
NON-CURRENT ASSETS	14,451	23,215	31,658	1,226	70,550
TOTAL ALLOCATED ASSETS	34,423	37,618	39,144	(5,312)	105,873
TOTAL ALLOCATED LIABILITIES	22,014	22,205	10,215	28,584	83,018

(*) For the presentation of the segment reporting, revenue and expenses arising from the use of the trademark and that do not affect the Group's consolidated results have been eliminated from the operating results of each Group segment.

(**) Other operating income and expenses for the Other & inter-group eliminations segment includes the 1,368 million euro gain on the sale of Endemol (see Note 2).

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	2006				
Millions of euros	Telefónica Spain	Telefónica Latin America	Telefónica Europe	Other & inter-group eliminations	Total
External sales	19,565	17,932	13,124	2,280	52,901
Inter-segment sales	186	156	35	(377)	
Other operating income and expenses	(11,104)	(11,517)	(9,451)	(1,703)	(33,775)
OIBDA (*)	8,647	6,571	3,708	200	19,126
Depreciation and amortization	(2,533)	(3,671)	(3,399)	(101)	(9,704)
OPERATING INCOME	6,114	2,900	309	99	9,422
INVESTMENT IN PP&E	2,304	2,811	2,552	343	8,010
INVESTMENT IN ASSOCIATES	57	20		882	959
NON-CURRENT ASSETS	14,664	23,373	35,889	2,459	76,384
TOTAL ALLOCATED ASSETS	30,790	37,705	41,651	(1,164)	108,982
TOTAL ALLOCATED LIABILITIES	20,855	23,674	10,021	34,431	88,981

(*) For the presentation of the segment reporting, revenue and expenses arising from the use of the trademark and that do not affect the Group's consolidated results have been eliminated from the operating results of each Group segment.

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	2005				
Millions of euros	Telefónica	Telefónica Latin America	Telefónica Europe	Other & inter-group eliminations	Total
External sales	Spain 18,936	15,256	1,308	1,883	37,383
Inter-segment sales	169	133	8	(310)	
Other operating income and expenses	(10,235)	(9,876)	(819)	(1,397)	(22,327)
OIBDA (*)	8,870	5,513	497	176	15,056
Depreciation and amortization	(2,804)	(3,461)	(364)	(64)	(6,693)
OPERATING INCOME	6,066	2,052	133	112	8,363
INVESTMENT IN PP&E	2,134	2,664	145	525	5,468
INVESTMENT IN ASSOCIATES	48	26		1,590	1,664
NON-CURRENT ASSETS	11,771	24,333	6,439	2,236	44,780
TOTAL ALLOCATED ASSETS	28,969	37,714	6,993	(502)	73,174
TOTAL ALLOCATED LIABILITIES	22,337	23,088	1,511	10,080	57,016

(*) For the presentation of the segment reporting, revenue and expenses arising from the use of the trademark and that do not affect the Group's consolidated results have been eliminated from the operating results of each Group

segment.

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The breakdown of external sales by the main countries in which the Group operates is as follows:

Country	Millions of euros		
	2007	2006	2005
Telefónica Spain	20,423	19,565	18,936
Brazil	7,855	7,412	6,691
Argentina	2,249	2,149	1,843
Venezuela	2,391	2,040	1,439
Chile	1,799	1,711	1,528
Peru	1,496	1,414	1,287
Colombia	1,564	1,178	769
Mexico	1,439	999	801
Remainder of Telefónica Latin America segment	1,108	1,029	898
Telefónica Latin America	19,901	17,932	15,256
UK	7,665	6,720	
Germany	3,509	3,310	
Ireland	966	870	
Czech Republic	2,233	2,130	1,308
Remainder of Telefónica Europe segment	44	94	
Telefónica Europe	14,417	13,124	1,308
Other & inter-group eliminations	1,700	2,280	1,883
Total external sales	56,441	52,901	37,383

The breakdown of services rendered by the main countries where the Group operates is as follows:

	2007		2006		2005	
	Wireline	Wireless	Wireline	Wireless	Wireline	Wireless
Millions of euros						
SPAIN	10,908	8,755	10,603	8,276	10,500	7,857
BRAZIL	5,537	2,079	5,490	1,710	4,902	1,600
ARGENTINA	906	1,341	895	1,252	837	1,005
VENEZUELA		2,390		2,040		1,438
CHILE	930	860	964	717	919	580
PERU	964	529	1,046	364	1,016	268
COLOMBIA	704	858	400	775	19	749
MÉXICO		1,421		980		771

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UK		7,665		6,721		
GERMANY		3,509		3,310		273
CZECH REPUBLIC	1,082	1,194	1,072	1,090	540	495
IRELAND		966		870		

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(5) BUSINESS COMBINATIONS AND ACQUISITIONS OF MINORITY INTERESTS

Business combinations:

No significant acquisitions were carried out in 2007. Changes to the consolidation scope in the year are included in Appendix I.

The main business combinations carried out in 2006 were the following:

a) Acquisition of O2

As indicated in Note 2, from February 1, 2006, the Telefónica Group has included the financial statements of O2 plc following the acquisition which began in 2005 and was completed on January 23, 2006. O2 plc mainly engages in the provision of wireless telephony services in the UK, Germany and Ireland.

In 2006, the purchase price was allocated to the assets acquired and the liabilities and contingent liabilities assumed. These amounts were determined using generally accepted measurement methods for each type of asset and/or liability based on the best information available.

The methods and assumptions used to determine the fair values were the following:

Licenses

The fair value was determined using the Greenfield method, which consists of measuring an asset based on the valuation of a hypothetical newly created company that starts its business with no assets except the asset being measured. Since the hypothetical company has no other assets, the value of the license must equal enterprise value.

A combined business plan is drawn up considering the licenses available, as the net cash flows from each of its businesses cannot be determined individually for each license.

This conclusion is based on the following assumptions, on the customer's indiscriminate use of the various networks without receiving itemized bills for the use of each, no differentiation is made between voice revenues, innovations gradually reduce the technological separation between the different licenses and the same infrastructure is used and a managed and evaluated operation is considered an integrated operation.

Customer base

The customer base was measured using the MEEM (Multiple Excess Earnings Method), which is based on calculating the present value of future cash flows of the future economic benefits attributable to the customer base. To estimate the remaining useful life of the customer base, the life of the customer relationship was analyzed using a churn method based on actuarial techniques.

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The aim of the analysis of lives was to estimate a survival curve that predicted future churn rates related to the current customer base. A typical analysis begins with determining a partial trend curve based on a historical study of customer retention data. These curves were compared to studies of standard complete survival curves obtained from in-depth studies of trends. The comparison allows us to determine which of the standard trends more closely resembles our customer base and then to assign it a remaining useful life.

Trademark

The fair value of the trademark was measured according to the relief-from-royalty method. This method measures the value of the asset by capitalizing the royalties saved by owning intellectual property. In this respect, the owner of the trademark obtains a benefit for owning the intangible asset, rather than having to pay royalties for its use. The royalties saved are determined by applying a market royalty rate (expressed as a percentage of income) to the future expected revenues from the sale of the product or service related to the intangible asset. The market royalty rate, normally expressed as a percentage of net income, is the rate a knowledgeable, willing owner would charge a knowledgeable, willing user for use of the asset in an arm's length transaction.

Property, plant and equipment

These assets were measured using the depreciated replacement cost method, which measures the asset by the sum of the costs necessary to replace the asset. The estimate of the replacement cost is based on the price of the asset, including its installation.

This process led to the identification of the fair values of the acquired companies' assets and liabilities.

The carrying amounts, fair values, goodwill and acquisition prices of the assets and liabilities acquired in this process at the acquisition date were the following:

	O2 plc Group	
Millions of euros	Carrying amount	Fair value
Intangible assets	6,320	14,463
Goodwill	4,691	N/A
Property, plant and equipment	6,003	5,743
Other non-current assets	1	825
Other current assets	3,615	3,615
Financial liabilities	(2,101)	(2,170)
Deferred tax liabilities	(29)	(2,466)
Other liabilities and current liabilities	(3,191)	(3,191)
Net asset value	15,309	16,819
Acquisition cost		26,135
Goodwill (Note 7)		9,316

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The impact of this acquisition on cash and cash equivalents in 2006 was the following:

Millions of euros	O2 plc Group
Cash and cash equivalents of the companies acquired	1,316
Cash paid in the acquisition plus related costs	26,135
Total net cash outflow	24,819
24,869 million euros of the acquisition cost of the O2 Group were paid in 2006 and the remainder had been paid in 2005.	

b) Acquisition of Colombia de Telecomunicaciones, S.A., ESP

In addition, the Company acquired 50% plus one share of Colombian wireline operator Colombia de Telecomunicaciones, S.A. in April 2006 and signed a commitment to acquire the remaining shares, carrying out the purchase price allocation.

	Colombia de Telecomunicaciones, S.A., ESP	
Millions of euros	Carrying amount	Fair value
Intangible assets	155	160
Property, plant and equipment	880	880
Other non-current assets	485	485
Other current assets	588	588
Financial liabilities	(1,881)	(1,881)
Deferred tax liabilities	343	343
Other liabilities and current liabilities	(757)	(757)
Net asset value	(187)	(182)
Commitment to acquire minority interests (see Note 21)		(289)
Acquisition cost		289
Goodwill (Note 7)		760

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The impact of this acquisition on cash and cash equivalents in 2006 was the following:

	Colombia de Telecomunicaciones, S.A., ESP
Millions of euros	
Cash and cash equivalents of the companies acquired	328
Cash paid in the acquisition plus related costs	289
Total net cash outflow	(39)

The contributions to operating income by the O2 plc Group and Colombia de Telecomunicaciones, S.A., ESP in 2006 from the date of acquisition were 73 and 100 million euros, respectively.

Pro-forma data for 2006 assuming these acquisitions had taken place at the beginning of the year is as follows:

Unaudited	Millions of euros
Revenue	53,819
Profit for the year	6,346
Basic earnings per share	1.33

The unallocated portion after the purchase price allocations in the transactions described above was recognized as goodwill in the accompanying consolidated balance sheet and relates to the economic benefits the acquired company is expected to generate in the future, in addition to other non-identifiable elements, such as workforce, geographic expansion and potential synergies arising from the merger of its operations with those of the Group.

Acquisitions of minority interests:

In 2007, the put option held by companies of the Banco Bilbao Vizcaya Argentaria, S.A. group (BBVA) on 8.65% of Atento, N.V. was exercised. The value of the stake was determined to be 70 million euros. Following this acquisition, Telefónica owns 100% of Atento N.V.

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In addition, pursuant to the terms of this contract, the price may be adjusted if prior to April 1, 2008:

- (a) the shares of Atento N.V. were admitted to trading, in which case the share price of Atento N.V. would be adjusted (i) to the price per share of Atento N.V. for institutional investors in the public offering and/or subscription for the admission to trading, or (ii) the value allocated to the shares for their admission to trading in the securities markets,
- (b) there is a filing of a significant event, prior communication or prospectus of public offering or subscription in relating to the admission to trading of the shares on the securities markets, in which case the price will be adjusted to the prices, once set, referred to in (a) above, or,
- (c) the shares are transferred to a third party, in which case the price of the purchase-sale agreement will be adjusted to price per share of this transfer.

The amount resulting from the price adjustment will be paid to Telefónica or BBVA as appropriate.

The merger between Telefónica, S.A. and Telefónica Móviles, S.A. was completed in July 2006. The transaction resulted in the acquisition of 7.08% of Telefónica Móviles, SA. held by minority interests (see Note 2).

The difference between the company's equity and the market value used to determine the exchange ratio was 2,998 million euros and was recognized in Goodwill in the accompanying consolidated balance sheet (Note 7).

Table of Contents**(6) INTANGIBLE ASSETS**

The breakdown and movements in Intangible assets in 2007 and 2006 is the following:

Millions of euros								
	Balance at 12/31/06	Additions	Disposals	Transfers	Translation differences	Inclusion of companies	Exclusion of companies	Balance at 12/31/07
Cost:								
Development costs	1,430	117		(23)	(3)			1,521
Administrative concessions	12,733	112	(3)	8	(281)	134		12,703
Industrial property and software	7,333	856	(89)	70	40	3	(1)	8,212
Customer base	6,195			232	(202)	34	(639)	5,620
Other intangible assets	2,734	250	(10)	(233)	(124)		(38)	2,579
Total gross intangible assets	30,425	1,335	(102)	54	(570)	171	(678)	30,635
Accumulated amortization:								
Development costs	1,330	74		(60)				1,344
Administrative concessions	2,285	776		17	(45)			3,033
Industrial property and software	4,621	1,204	(78)	(36)	37		(1)	5,747
Customer base	973	644		(29)	(59)		(62)	1,467
Other intangible assets	455	241	(8)	79	(26)		(21)	720
Total accumulated amortization	9,664	2,939	(86)	(29)	(93)		(84)	12,311
Provisions for impairment	3			1				4
Net intangible assets	20,758	(1,604)	(16)	82	(477)	171	(594)	18,320

Millions of euros								
	Balance at 12/31/05	Additions	Disposals	Transfers	Translation differences	Inclusion of companies	Exclusion of companies	Balance at 12/31/06
Cost:								
Development costs	1,338	96		(1)	(3)			1,430

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Administrative concessions	6,027	18	(82)	90	(236)	6,919	(3)	12,733
Industrial property and software	5,620	846	(168)	421	(104)	828	(110)	7,333
Customer base	1,533				71	4,591		6,195
Other intangible assets	399	272	(39)	(333)	100	2,340	(5)	2,734
Total gross intangible assets	14,917	1,232	(289)	177	(172)	14,678	(118)	30,425
Accumulated amortization:								
Development costs	1,257	73						1,330
Administrative concessions	1,686	731	(80)	(4)	(45)		(3)	2,285
Industrial property and software	3,742	1,186	(158)	3	(78)		(74)	4,621
Customer base	307	695			(29)			973
Other intangible assets	43	393	(38)	(4)	66		(5)	455
Total accumulated amortization	7,035	3,078	(276)	(5)	(86)		(82)	9,664
Provisions for impairment	5		(2)					3
Net intangible assets	7,877	(1,846)	(11)	182	(86)	14,678	(36)	20,758

In Additions, the main additions in both 2007 and 2006 relate to investments in software.

Exclusion of companies in 2007 consists of the disposal of Airwave and Endemol, for net amounts of 577 million euros and 17 million euros, respectively.

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The principal changes in 2006 correspond to the inclusions of the O2 Group and Colombia de Telecomunicaciones, S.A., ESP in the consolidation scope, which led to increases in the cost of the assets of 14,463 million and 160 million euros, respectively (see Note 5).

Exclusions of companies in 2006 includes the disposal of the TPI Group for 118 million euros of intangible assets and 82 million euros of accumulated amortization.

At December 31, 2007 and 2006, the Company carried intangible assets with indefinite useful lives of 242 and 125 million euros, respectively, related primarily to licenses to operate wireless telecommunications services in Argentina, and of 108 and 134 million euros, respectively, for licenses to use MMDS technology in Brazil.

Intangible assets are also subject to impairment tests whenever there are indications of a potential loss in value and, in any event, at the end of each year. There was no impairment recognized in the consolidated financial statements for 2007 or 2006 as a result of these impairment tests.

Intangible assets with finite lives are amortized on a straight-line basis over their estimated useful lives. Amortization charges in 2007 and 2006 amounted to 2,939 million and 3,078 million euros, respectively, of which 10 million euros in 2006 correspond to discontinued operations.

Other intangible assets includes the amounts allocated to trademarks acquired in business combinations, of 1,645 and 1,739 million euros at December 31, 2007 and 2006 (1,330 and 1,579 million euros net of the related accumulated amortization).

(7) GOODWILL

The movement in this heading assigned to each Group segment was the following:

Millions of euros					
	Balance at 12/31/06	Acquisitions	Disposals	Translation differences and other	Balance at 12/31/07
2007					
Telefónica Spain	3,234		(2)	1	3,233
Telefónica Latin America	5,618	196		(290)	5,524
Telefónica Europe	11,469		(136)	(503)	10,830
Other	1,418		(1,250)	15	183
Total	21,739	196	(1,388)	(777)	19,770

Millions of euros					
	Balance at 12/31/05	Acquisitions	Disposals	Translation differences and other	Balance at 12/31/06
2006					
Telefónica Spain	215	3,019			3,234
Telefónica Latin America	5,525	779	(2)	(684)	5,618
Telefónica Europe	1,836	9,430		203	11,469
Other	1,334	143	(67)	8	1,418
Total	8,910	13,371	(69)	(473)	21,739

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Goodwill generated in the acquisition of foreign companies is treated as an asset denominated in the currency of the company acquired, and is therefore subject to exchange rate differences, which are included under Translation differences.

Impairment tests carried out by the Directors in 2007 and 2006 did not uncover the need to make any material write-downs to goodwill as recoverable value was higher than carrying amount in all cases at year end.

2007

The main disposals of goodwill relate to the disposals of holdings during the year in Airwave O2, Ltd. and Endemol Investment Holding, B.V. (see Note 2), for 129 million and 1,244 million euros, respectively. Increases in the year mainly related to the acquisition of Brazilian company Navy Tree Participações, S.A., which gave rise to 182 million euros of goodwill (see Appendix I).

2006

In 2006, the additions to goodwill related to the acquisition of the following companies:

	Millions of euros
O2 plc Group (Note 5)	9,316
Telefónica Móviles Group (Note 5)	2,998
Colombia de Telecomunicaciones, S.A. (Note 5)	760
Other	297
Total	13,371

Table of Contents**(8) PROPERTY, PLANT AND EQUIPMENT**

The breakdown and movement in Property, plant and equipment and accumulated depreciation in 2007 and 2006 was the following:

	Millions of euros							Balance at 12/31/07
	Balance at 12/31/06	Additions	Disposals	Inclusion of companies	Exclusion of companies	Translation differences	Transfers	
Cost:								
Land and buildings	10,961	183	(235)		(42)	(29)	551	11,389
Plant and machinery	73,251	2,483	(3,045)	66	(1,119)	(66)	2,514	74,084
Furniture, tools and other	4,345	470	(139)	1	(65)	(76)	241	4,777
Total PP&E in service	88,557	3,136	(3,419)	67	(1,226)	(171)	3,306	90,250
Construction in progress	2,517	3,245	(13)	6	(348)	(94)	(3,038)	2,275
Advance payments on PP&E	15	18				(2)	(16)	15
Installation materials	345	293	(16)			(13)	(235)	374
Gross PP&E	91,434	6,692	(3,448)	73	(1,574)	(280)	17	92,914
Accumulated depreciation:								
Buildings	3,635	557	(134)		(22)	(5)	47	4,078
Plant and machinery	51,171	5,264	(2,945)		(409)	134	(29)	53,186
Furniture, tools and other	2,581	676	(120)		(46)	(37)	(55)	2,999
Total accumulated depreciation	57,387	6,497	(3,199)		(477)	92	(37)	60,263
Provisions for impairment	160	18	(27)	2		3	35	191
Net PP&E	33,887	177	(222)	71	(1,097)	(375)	19	32,460

	Millions of euros							Balance at 12/31/06
	Balance at 12/31/05	Additions	Disposals	Inclusion of companies	Exclusion of companies	Translation differences	Transfers	

Cost:

Land and buildings	9,392	153	(39)	395	(35)	(132)	1,227	10,961
Plant and machinery	67,284	2,506	(1,431)	5,208	(1)	(2,064)	1,749	73,251
Furniture, tools and other	3,564	593	(179)	422	(56)	(173)	174	4,345

Total PP&E in service

	80,240	3,252	(1,649)	6,025	(92)	(2,369)	3,150	88,557
Construction in progress	1,676	3,208	(16)	750		(80)	(3,021)	2,517
Advance payments on PP&E	18	7					(10)	15
Installation materials	310	311	(27)			(11)	(238)	345
Gross PP&E	82,244	6,778	(1,692)	6,775	(92)	(2,460)	(119)	91,434

Accumulated depreciation:

Buildings	2,928	527	(16)		(17)	(96)	309	3,635
Plant and machinery	48,793	5,537	(1,342)		(1)	(1,472)	(344)	51,171
Furniture, tools and other	2,419	575	(159)		(42)	(137)	(75)	2,581

Total accumulated depreciation

	54,140	6,639	(1,517)		(60)	(1,705)	(110)	57,387
Provisions for impairment	111	83	(32)			(3)	1	160
Net PP&E	27,993	56	(143)	6,775	(32)	(752)	(10)	33,887

Exclusion of companies in 2007 mainly consists of the disposals of Airwave O2, Plc and the Endemol Group for gross amounts of 1,432 and 141 million euros, respectively (1,047 and 50 million euros, respectively, of assets net of depreciation).

Inclusion of companies in 2006 mainly consists of the acquisitions of the O2, Plc Group and Colombia de Telecomunicaciones, S.A., ESP in the consolidation scope for 5,743 million and 880 million euros, respectively (see Note 5).

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Exclusion of companies in 2006 consists of the disposals of the TPI Group, for a gross amount of 92 million euros, and the accumulated depreciation of 60 million euros at the disposal date.

Among the main investments in 2007 and 2006 were additions by Telefónica de España of 2,381 and 2,304 million euros, respectively. The investments were mostly to develop ADSL, enabling Telefónica de España to post a 22.1% increase in gross ADSL adds, ending the year with 4.5 million end users (compared to 3.7 million at the end of 2006) offering also to users in 2007 an increase in user speeds from 1 Mbps to 3 Mbps. Also worth highlighting in 2007 was Telefónica de España's continued work on its network transformation to adapt existing loops to FTTx (fiber optic) technology in order to enhance coverage of new services. Now, more than 12% of its loops can handle speeds of over 25 Mbps. Meanwhile, Telefónica Móviles España invested heavily in its UMTS network, raising its 3G coverage rate to 72% of the population by the end of the year.

Other additions in 2007 and 2006 include large investments in Latin America (3,343 and 2,811 million euros, respectively). In the wireless business, highlights include investment to improve and roll out the GSM networks, mainly in Brazil, Venezuela and Mexico. Investments in the wireline business went mainly to television in Brazil and, above all, Chile, as well as to network transformation to offer higher broadband in Brazil and Colombia.

Translation differences reflect the impact of exchange rate movements on opening balances. The effect of exchange rates on movements in the year is included in the appropriate column for each movement.

Depreciation in 2007 and 2006 based on the estimated useful lives of the assets (see Note 3.e) totaled 6,497 and 6,639 million euros, respectively, of which 3 million euros in 2006 corresponded to assets related to discontinued operations.

Telefónica Group companies have purchased insurance policies to reasonably cover the possible risks to which their property, plant and equipment used in operations are subject, with suitable limits and coverage.

Property, plant and equipment deriving from lease transactions at December 31, 2007 amounted to 1,208 million euros (1,205 million euros at December 31, 2006) (see Note 22).

The net amounts of Plant, property and equipment temporarily out of service at December 31, 2007 and 2006 were not significant.

Table of Contents**(9) ASSOCIATES AND JOINT VENTURES****Associates**

The breakdown of amounts recognized in the consolidated balance sheet related to transactions with associates is as follows:

Description	Millions of euros	
	12/31/07	12/31/06
Investments in associates	3,188	959
Long-term loans to associates	75	73
Short-term loans to associates	45	88
Current payables to associates	84	80
Revenue from operations with associates	148	221
Expenses from operations with associates	27	11
The detail of associates and key financial highlights are:		

December 31, 2007

Millions of euros

	%	Total	Total	Current	Profit	Carrying	Fair
COMPANY	Holding	assets	liabilities	revenues	(loss)	amount	value
Portugal Telecom, S.G.P.S., S.A. (Portugal)							
(1)	9.16%	13,578	11,249	4,531	1,010	606	839
Lycos Europe, N.V. (Netherlands)	32.10%	209	36	58	38	54	49
Médi Telecom, S.A. (Morocco)	32.18%	1,275	1,023	447	24	91	N/A
Hispasat, S.A. (Spain)	13.23%	645	308	117	25	45	N/A
Telefónica Factoring Establecimiento Financiero de Crédito, S.A. (Spain)	50.00%	91	81	7	3	4	N/A
Mobipay España, S.A. (Spain)	13.36%	6	4	2	(2)		N/A
Telco, S.p.A. (*) (Italy)	42.30%	8,769	3,645	(1)	(36)	2,314	N/A
Other	N/A	N/A	N/A	N/A	N/A	74	N/A
TOTAL		24,573	16,346	5,161	1,062	3,188	888

(*) Through this
company,

Telefónica
effectively has
an indirect stake
in Telecom
Italia, S.p.A. s
voting shares of
approximately
9.98%,
representing
6.88% of the
dividend rights.

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December 31, 2006

Millions of euros

	%	Total	Total	Current	Profit (loss) for	Carrying	Fair
COMPANY	Holding	assets	liabilities	revenues	the year	amount	value
Portugal Telecom, S.G.P.S., S.A. (Portugal)							
(1)	9.84%	13,788	11,035	4,708	862	761	1,106
Lycos Europe, N.V. (Netherlands)	32.10%	168	35	59	3	42	91
Médi Telecom, S.A. (Morocco)	32.18%	1,288	1,106	423	22	59	N/A
Hispasat, S.A. (Spain)	13.23%	585	270	120	25	42	N/A
Sistemas Técnicos de Loterías del Estado, S.A. (Spain)	31.75%	89	12	55	5	24	N/A
Telefónica Factoring Establecimiento Financiero de Crédito, S.A. (Spain)	50.00%	97	87	7	3	5	N/A
Mobipay España, S.A. (Spain)	13.36%	16	5	3	(3)	1	N/A
Ipsa 2000, S.p.A. (Italy)	49.67%	41	634		(23)		N/A
Other	N/A	N/A	N/A	N/A	N/A	25	N/A
TOTAL		16,072	13,184	5,375	894	959	1,197

(1) Figures for the
12-month period
ended
September 30.

Fair value was calculated based on the trading price of listed companies.

The movement in Investments in associates in 2007 and 2006 was the following:

Investments in associates	Millions of euros
Balance at 12/31/05	1,664
Acquisitions	1
Disposals	(188)
Inclusion of companies	7
Translation differences	(5)
Income (loss)	76
Dividends	(43)
Transfers	(553)
Balance at 12/31/06	959

Acquisitions	2,369
Disposals	(148)
Exclusion of companies	(9)
Translation differences	(3)
Income (loss)	140
Dividends	(218)
Transfers	98
Balance at 12/31/07	3,188

Additions at December 31, 2007 and 2006 reflect the amounts from transactions detailed in the changes to the consolidation scope (see Appendix I and Note 2). The figure for 2007 includes the acquisition of an indirect holding in Telecom Italia through the investment in Telco, S.p.A. for 2,314 million euros.

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Disposals in 2007 include the disposal of a 1.809% stake in Portugal Telecom, S.G.P.S., S.A. Telefónica's stake in this company following the disposal and the capital decrease carried out by Portugal Telecom in 2007 is 9.16%.

Among dividends in 2007 were those paid by Portugal Telecom, S.G.P.S., S.A., consisting of a cash and non-cash dividend via the distribution of 0.176067 shares of Portugal Telecom Multimedia S.G.P.S., S.A. per share of Portugal Telecom S.G.P.S., S.A. held. Therefore, Telefónica received a total of 16,879,406 shares of this company, representing 5.46% of its share capital. These shares were classified as available-for-sale financial assets at the end of 2007 (see Note 13). These shares had a total market value at the date of distribution of 155 million euros.

In 2006, Telefónica tendered shares in the takeover bid for Sogecable, reducing its equity ownership interest in the company from 23.83% to 17.26%. This transaction is included under Disposals for an amount of 188 million euros. The gain totaled 142 million euros (Note 19).

Subsequently, Sogecable held a capital increase suspending the pre-emptive subscription rights to allow the Warner-Dalbergia Group to become a shareholder. This diluted Telefónica's stake to 16.84%, while another capital increase held to cover its share option plans for company directors further diluted its stake to 16.75%, which Telefónica held as of December 31, 2007 and 2006 (see Appendix I).

Since these transactions took the equity interest to below 20%, Telefónica ceased consolidating Sogecable using the equity method, recognizing it as Available-for-sale investments. Transfers in 2006 include the impact of this change in the consolidation scope, for an amount of 502 million euros (see Note 13).

Non-current financial assets includes a long-term loan to associate Medi Telecom for 74 million euros (71 million euros at December 31, 2006).

Joint ventures

On December 27, 2002, Telefónica Móviles, S.A. and PT Movéis Serviços de Telecomunicações, S.G.P.S., S.A. (PT Movéis) set up a 50/50 joint venture, Brasilcel, N.V., via the contribution of 100% of the groups' direct and indirect shares in Brazilian cellular operators. This company is consolidated in the consolidated financial statements of the Telefónica Group by the proportionate method.

The contributions of Brasilcel, N.V. to the Telefónica Group's 2007, 2006 and 2005 consolidated balance sheets and income statements are as follows:

	Millions of euros		
	2007	2006	2005
Current assets	1,193	915	1,242
Non-current assets	4,358	3,348	3,448
Current liabilities	1,328	1,071	1,132
Non-current liabilities	644	782	1,029
Operating revenue	2,152	2,077	1,955
Operating expenses	1,778	2,097	1,858

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(10) RELATED PARTIES

Significant shareholders:

The main transactions between Telefónica Group companies and significant shareholders of Telefónica, S.A. were the following:

Banco Bilbao Vizcaya Argentaria, S.A. (BBVA) and subsidiaries comprising its consolidated group:

Financing transactions arranged under market conditions, with approximately 367 million euros drawn down at December 31, 2007 (490 million euros at December 31, 2006).

Derivative transactions arranged at market conditions, for a total nominal amount of approximately 7,160 million euros at December 31, 2007 (3,516 million euros at December 31, 2006).

Guarantees granted by BBVA for approximately 18 million euros at December 31, 2007 (18 million euros at December 31, 2006).

Services, mainly telecommunications and telemarketing, rendered by Telefónica Group companies to the BBVA Group, under market conditions.

In 2007, Telefónica acquired an 8.65% stake in Atento, N.V. from the BBVA Group (see Note 5).

Caja de Ahorros y Pensiones de Barcelona, La Caixa, and subsidiaries comprising the consolidated group:

Financing transactions arranged under market conditions, with approximately 247 million euros drawn down at December 31, 2007 (356 million euros at December 31, 2006).

Derivative transactions entered into under market conditions, for a total nominal amount of approximately 1 million euros in both 2007 and 2006.

The telecommunications services rendered by Telefónica Group companies to La Caixa group companies under market conditions.

Associates and joint ventures:

The most significant balances and transactions with associates and joint ventures were detailed in Note 9.

Directors and senior executives compensation and other information

Compensation and other benefits paid to members of the Board of Directors and senior managers, as well as the detail of the equity interests held in companies engaging in an activity that is identical, similar or complementary to that of the Company and the performance of similar activities by the directors for their own account or for third parties, are detailed in Note 21.

Table of Contents**(11) TRADE AND OTHER RECEIVABLES**

The breakdown of this consolidated balance sheet heading at December 31, 2007 and 2006 is as follows:

Millions of euros	Balance at 12/31/07	Balance at 12/31/06
Customers	10,393	10,318
Receivable from associates	74	73
Sundry receivables	590	620
Bad debt reserves	(2,070)	(1,961)
Short-term prepayments	675	616
Total	9,662	9,666

Public-sector trade receivables in the countries in which the Group operates at December 31, 2007 and 2006 amounted to 483 million and 503 million euros, respectively.

The breakdown of trade receivables at December 31, 2007 and 2006 is as follows:

Millions of euros	12/31/07	12/31/06
Trade receivables billed	7,765	7,123
Trade receivables unbilled	2,558	3,130
Bills of exchange receivable	70	65
Total	10,393	10,318

The movement in the reserve for bad debt in 2007 and 2006 is as follows:

	Millions of euros
Bad debt reserve at December 31, 2005	1,650
Allowances	594
Retirements/amount applied	(529)
Inclusion of companies	394
Exclusion of companies	(103)
Translation differences	(45)
Bad debt reserve at December 31, 2006	1,961
Allowances	774
Retirements/amount applied	(637)
Inclusion of companies	19
Exclusion of companies	(9)
Translation differences	(38)
Bad debt reserve at December 31, 2007	2,070

The balance of trade receivables billed net of provisions at December 31, 2007 amounted to 5,695 million euros (5,162 million euros at December 31, 2006), of which 3,679 million euros have payment dates after year end or are unbilled at year end (2,834 million euros at December 31, 2006).

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Of the amounts due, only 241 million euros in 2007 (269 million in 2006) are over 360 days due. They are mainly balances with public sector.

(12) EQUITY

The detail and movement in equity accounts in 2005-2007 are the following:

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Millions of euros	No. of shares	Attributable to equity holders of the parent							Minority interests	Total equity	
		Share capital	Share premium	Legal reserve	Revaluation reserve	Treasury shares	Retained earnings	Translation differences			
Balance at December 31, 2004	4,955,891,361	4,956	5,288	790	1,358	(690)	(953)	(309)	10,440	1,902	12,342
Dividends paid			(1,296)				(1,083)	7	(2,372)	(396)	(2,768)
Capital decrease	(34,760,964)	(35)	(123)			158					
Net movement in own treasury shares			(1,769)			159	(74)		(1,684)		(1,684)
Acquisitions and disposals of minority interests							(23)		(23)	1,042	1,019
Transfers			(429)				429				
Income and expense recognized in the year				130			4,132	2,135	6,397	824	7,221
Other movements							(18)	(7)	(25)	53	28
Balance at December 31, 2005	4,921,130,397	4,921	1,671	920	1,358	(373)	2,410	1,826	12,733	3,425	16,158
Dividends paid							(2,627)		(2,627)	(569)	(3,196)
Net movement in own treasury shares			1,198			44	(537)		705		705
Acquisitions and disposals of minority interests										(283)	(283)
Income and expense recognized in the year				64			6,584	(302)	6,346	241	6,587
Other movements							21		21	9	30
Balance at December 31, 2006	4,921,130,397	4,921	2,869	984	1,358	(329)	5,851	1,524	17,178	2,823	20,001
Dividends paid							(3,077)		(3,077)	(324)	(3,401)
Net movement in own treasury shares			(13)			(2,105)	(13)		(2,131)		(2,131)
										(95)	(95)

Acquisitions and disposals of minority interests												
Capital decrease (07/04/07)	(147,633,912)	(148)	(2,054)			2,202						
Income and expense recognized in the year							9,585	(1,427)	8,158	265	8,423	
Other movements			(280)		(1,178)		1,455		(3)	61	58	
Balance at December 31, 2007	4,773,496,485	4,773	522	984	180	(232)	13,801	97	20,125	2,730	22,855	

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a) Share capital and share premium

At December 31, 2007, Telefónica, S.A.'s share capital amounted to 4,773,496,485 euros and consisted of 4,773,496,485 fully paid ordinary shares of a single series, par value 1 euro, all recorded by the book-entry system and traded on the Spanish electronic trading system (Continuous Market), where they form part of the Ibex 35 Index, on the four Spanish Stock Exchanges (Madrid, Barcelona, Valencia and Bilbao) and listed on the New York, London, Paris, Frankfurt, Tokyo, Buenos Aires, Sao Paulo and Lima Stock Exchanges. In October 2007, steps were taken to delist shares of Telefónica from the Paris and Frankfurt stock exchanges. This is expected to take place in the first quarter of 2008.

On June 21, 2006, authorization was given at the Annual Shareholders Meeting of Telefónica, S.A. for 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 of Article 153.1 b) of the Spanish Corporation Law (authorized capital) up to a maximum increase of 2,460 million euros, equivalent to half of the Company's share capital at that date, by issuing and placing new ordinary shares, be they ordinary or of any other type permitted by the Law, with a fixed or variable premium, with or without pre-emptive subscription rights and, in all cases, in exchange for cash, and expressly considering the possibility that the new shares may not be fully subscribed in accordance with the terms of Article 161.1 of the Spanish Corporation Law. The Board of Directors was also empowered to disapply, partially or fully, pre-emptive subscription rights under the terms of Article 159.2 of the Spanish Corporation Law and related provisions.

In addition, at the May 10, 2007 Shareholders Meeting, authorization was given for the Board of Directors to issue fixed-income securities and preferred shares at one or several times within a maximum period of five years from that date. These securities may be in the form of debentures, bonds, promissory notes or any other kind of fixed-income security, plain or, in the case of debentures and bonds, convertible into shares of the Company and/or exchangeable for shares any of the group companies. They may also be preferred shares. The total maximum amount of the securities issued agreed under this authorization is 25,000 million euros or the equivalent in another currency. As at December 31, 2007, the Board of Directors had exercised these powers, approving a program to issue corporate promissory notes for 2008.

In addition, on May 10, 2007, shareholders voted to authorize the acquisition by the Board of Directors of treasury shares, for a consideration, up to the limits and pursuant to the terms and conditions established by the Shareholders Meeting, within a maximum period of 18 months from that date. However, it specified that in no circumstances could the par value of the shares acquired, added to that of the treasury shares already held by Telefónica, S.A. and by any of its controlled subsidiaries, exceed 5% of Telefónica's share capital.

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On June 4, 2007, the deed of capital reduction formalising the implementation by the Company's Board of Directors of the resolution adopted by the Shareholders' Meeting on May 10, 2007, was executed. Capital was reduced through the cancellation of treasury shares previously acquired by the Company as authorised by the Shareholders' Meeting. As a result, 147,633,912 Telefónica, S.A. treasury shares were cancelled and the Company's share capital was reduced by a nominal amount of 147,633,912 euros. Article 5 of the Corporate Bylaws relating to the amount of share capital was amended accordingly to indicate 4,773,496,485 euros, it was likewise decided, at the same time as permitted by Article 167.3 of the Spanish Corporate Law and to render null and void the right of opposition provided for in Article 166 of the same Law, to record a reserve for cancelled share capital for an amount equal to the par value of the cancelled shares, which can only be used if the same requirements as those applicable to the reduction of share capital are met. The cancelled shares were delisted on June 14, 2007.

Proposed appropriation of profit attributable to equity holders of the parent

Telefónica, S.A. obtained 6,620 million euros of distributable profit in 2007.

At its meeting of September 26, 2007, Telefónica, S.A.'s Board of Directors resolved to pay an interim dividend against 2007 profit of a fixed gross 0.35 euros for each of the Company's outstanding shares carrying dividend rights. This dividend was paid on November 14, 2007, and the total amount paid was 1,652 million euros.

In addition, at its meeting of February 27, 2008, the Company's Board of Directors agreed to submit for approval at the Shareholders' Meeting the distribution of a final dividend charged to 2007 profit for a fixed gross amount of 0.40 euros per outstanding share carrying dividend rights up to a total amount of 1,909 million euros.

Accordingly, the Company's Board of Directors will submit the following proposed appropriation of 2007 profit for approval at the Shareholders' Meeting:

	Millions of euros
Total distributable profit	6,620
Interim dividend (paid in October 2007)	1,652
Final dividend (maximum distributable amount of 0.40 euros per share for all shares into which the Company's share capital is divided: 4,773,496,485 shares)	1,909
Voluntary reserve	(minimum) 3,059
Total	6,620

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b) Dividends

Dividends paid in 2007

At its meeting held on February 28, 2007, the Company's Board of Directors agreed to propose to the Shareholders Meeting the payment of a final dividend against 2006 profit of a gross 0.30 euros per share. A total of 1,425 million euros was paid in May.

In addition, as indicated above, in November an interim dividend against 2007 profit of a gross 0.35 euros per share was paid, entailing a total payment of 1,652 million euros.

Dividends paid in 2006

At its meeting of February 28, 2006, Telefónica, S.A.'s Board of Directors resolved to pay an interim dividend against 2005 profit of a gross 0.25 euros per share per outstanding share carrying dividend rights. This dividend was paid on May 12, 2006, and the total amount paid was 1,169 million euros.

At its meeting of September 27, 2006, Telefónica, S.A.'s Board of Directors resolved to pay an interim dividend against 2006 profit of a gross 0.30 euros per share for each of the Company's outstanding shares carrying dividend rights. This dividend was paid on November 10, 2006, and the total amount paid was 1,458 million euros.

c) Reserves

Legal reserve

Under the revised Spanish Corporation Law, 10% of income for each year must be transferred to the legal reserve until the balance of this reserve reaches at least 20% of share capital. The legal reserve can be used to increase capital provided that the balance of the remaining reserve does not fall below 10% of the increased share capital amount. Otherwise, until the legal reserve exceeds 20% of share capital, it can only be used to offset losses provided other reserves are insufficient for this purpose.

Revaluation reserves

The balance of Revaluation reserves arose as a result of the revaluation made pursuant to Royal Decree-Law 7/1996 dated June 7, 1996.

The revaluation reserve may be used, with no tax effect, to offset potential future losses or to increase capital. From January 1, 2007, it may be allocated to unrestricted reserves, provided that the capital gain has been realized.

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The capital gain will be deemed to have been realized in respect of the portion on which the depreciation has been recorded for accounting purposes or when the revalued assets have been transferred or derecognized. In this respect, an amount of 1,178 million euros corresponding to reserves subsequently considered unrestricted has been reclassified under Retained earnings

Retained earnings

These reserves include undistributed profits from previous years of companies comprising the consolidated Group less interim dividends paid against profit for the year.

d) Translation differences on consolidation

The translation differences relate mainly to the effect of exchange rate fluctuations on the net assets of the companies located abroad after the elimination of intra-group balances and transactions (see Note 3.b). They also include exchange rate differences resulting from specific-purpose foreign-currency financing transactions relating to investments in investees and which hedge the exchange rate risk on these investments.

The Company has taken an exemption that allows all translation differences generated up to the IFRS transition date to be reset to zero, with the impact on prior years recognized in Retained earnings .

The breakdown of the accumulated contribution of translation differences at December 31 is the following:

Millions of euros	2007	2006	2005
Telefónica Latin America	669	986	1,801
Telefónica Europe	(619)	635	164
Other adjustments and intra-group eliminations	47	(97)	(139)
Total Telefónica Group	97	1,524	1,826

Table of Contents***e) Treasury shares***

At December 31, 2007 and 2006, Telefónica Group companies held the following shares in the Telefónica, S.A. parent company:

	No. of shares	Euros per share		Market Value	%
		Acquisition price	Trading price		
<i>Treasury shares at 12/31/07</i>	64,471,368	16.67	22.22	1,433	1.35061%
<i>Treasury shares at 12/31/06</i>	75,632,559	14.04	16.12	1,219	1.53689%

Telefónica, S.A. owns the only treasury shares in the Group. No other group company owns any Telefónica treasury shares.

In 2007 and 2006, the following transactions involving treasury shares were carried out:

	No. of shares	Millions of euros
Treasury shares at 12/31/05	136,647,061	
Acquisitions	214,494,091	2,888
Disposals	(31,113,135)	(469)
Lycos and Endemol employee share option plans	(51,446)	
Exchange of Telefónica, S.A. shares for Telefónica Móviles, S.A. shares	(244,344,012)	
Treasury shares at 12/31/06	75,632,559	
Acquisitions	149,099,044	2,324
Disposals	(12,621,573)	(210)
Endemol employee share option plan	(4,750)	
Share cancellation	(147,633,912)	
Treasury shares at 12/31/07	64,471,368	

The acquisition cost of treasury shares at December 31, 2007 and 2006 was 1,074 and 1,062 million euros, respectively. This cost reduces Treasury shares and Share premium in equity by 232 million and 842 million euros, respectively (261 and 801 million euros, respectively at December 31, 2006).

At December 31, 2007 there were no call options on Telefónica, S.A. shares

At December 31, 2006 the Group held call options on 85 million Telefónica, S.A. shares (see Note 16).

Table of Contents**Minority interests**

Minority interests represents the share of minority shareholders in the equity and income or loss for the year of fully consolidated Group companies. The movements in this heading of the 2007, 2006 and 2005 consolidated balance sheets are as follows:

	Balance	Profit	Change	Acquisitions			Balance
	at	(loss)	in	of			at
Millions of euros	12/31/06	for	translation	minority	Dividends	Other	12/31/07
		the	differences	interests	paid	movements	
		year		and			
				exclusion			
				of			
				companies			
Telefónica O2 Czech Republic, a.s.	1,239	92	14		(153)		1,192
C.T. Chile, S.A.	515	25	(28)	(31)	(8)		473
Telesp Participações, S.A.	445	119	35		(135)		464
Endemol, N.V.	54	11		(45)	(20)		
Brasilcel (Holdings)	493	19	35		(2)		545
Fonditel Entidad Gestora de Fondos de Pensiones, S.A.	17	4			(2)		19
Iberbanda, S.A.	21	(12)				2	11
Colombia de Telecomunicaciones, S.A., ESP		(50)				50	
Other	39	5	(4)	(19)	(4)	9	26
Total	2,823	213	52	(95)	(324)	61	2,730

	Balance	Capital	Profit	Change	Acquisitions			Balance
	at	contributions	(loss)	in	of			at
Millions of euros	12/31/05	and	for	translation	minority	Dividends	Other	12/31/06
		inclusion	the	differences	interests	paid	movements	
		of	year		and			
		companies			exclusion			
					of			
					companies			
Telefónica O2 Czech Republic, a.s.	1,274		55	66		(156)		1,239
C.T. Chile, S.A.	546		41	(92)	(28)	(18)	66	515
Telesp Participações, S.A.	459	3	136	(13)	(6)	(134)		445
Telefónica Móviles, S.A.	392		89	(32)	(254)	(195)		

Telefónica								
Publicidad e								
Información, S.A.	99		13	(5)	(49)	(58)		
Endemol, N.V.	35		24			(3)	(2)	54
Brasilcel (Holdings)	493	13	(3)	(10)				493
Fonditel Entidad								
Gestora de Fondos								
de Pensiones, S.A.	15		3			(1)		17
Iberbanda, S.A.		33	(12)					21
Other	112	5		(19)		(4)	(55)	39
Total	3,425	54	346	(105)	(337)	(569)	9	2,823

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	Balance	Capital	Profit	Change	Acquisitions			Balance
	at	contributions	(loss)	in	of		Other	at
Millions of euros	12/31/04	and inclusion of companies	for the year	translation differences	minority interests and exclusion of companies	Dividends paid	movements	12/31/05
Telefónica O2 Czech Republic, a.s.		1,198	46	30				1,274
C.T. Chile, S.A.	534		27	114		(119)	(10)	546
Terra Networks, S.A.	293		8		(301)			
Telesp Participações, S.A.	393		110	127		(171)		459
Telefónica Móviles, S.A.	236		136	78		(59)	1	392
Telefónica Publicidad e Información, S.A.	101		54	7		(42)	(21)	99
Endemol, N.V.			4				31	35
Brasilcel (Holding) Fonditel Entidad Gestora de Fondos de Pensiones, S.A.	279	136	(1)	79				493
Other	13		3			(1)		15
	54	13	(6)	8	(4)	(4)	51	112
Total	1,903	1,347	381	443	(305)	(396)	52	3,425

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2007

Movements in minority interests in 2007 included the dividends paid by Telefónica O2 Czech Republic, a.s. and Telesp Participações, S.A., as well as the profit (loss) for the year attributable to minority interests.

2006

Movements in minority interests in 2006 included the acquisition of the Telefónica Móviles Group's minority interests related to the merger, for 254 million euros, and the disposal of the Telefónica Publicidad e Información Group, for 49 million euros.

2005

2005 included the first-time consolidation of Telefónica O2 Czech Republic, s.a. (1,198 million euros), the acquisition of 23.20% of Terra Networks (301 million euros) in the merger and profit for the year attributable to minority interests (381 million euros).

Table of Contents***Gains and losses recognized in equity***

The movement in gains and losses recognized in equity in 2007, 2006 and 2005 is the following:

	Gain (loss) on measurement of available-for-sale investments	Gains (loss) on hedges	Translation differences	Gain (loss) on defined benefit plans	Share of gain (loss) directly recognized in equity	Tax effect	Total
Balance at December 31, 2004	46	(91)	(316)		52	(28)	(337)
Gain/(loss) arising in the year	(80)	(82)	2,577		(50)	58	2,423
Gain/(loss) reclassified to the income statement		(44)				15	(29)
Balance at December 31, 2005	(34)	(217)	2,261		2	45	2,057
Gain/(loss) arising in the year	584	(4)	(362)	112	(153)	(133)	44
Gain/(loss) reclassified to the income statement		14	(45)			(5)	(36)
Balance at December 31, 2006	550	(207)	1,854	112	(151)	(93)	2,065
Gain/(loss) arising in the year	(75)	875	(1,358)	54	(3)	(291)	(798)
Gain/(loss) reclassified to the income statement	107	17	(17)			(5)	102
	582	685	479	166	(154)	(389)	1,369

**Balance at
December 31, 2007**

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(13) FINANCIAL ASSETS AND LIABILITIES

The calculation of the fair values of the Telefónica Group's debt instruments required, for each currency and subsidiary, the estimation of a curve analysis for the credit differences for the quoted prices of the bonds and the Group's credit derivatives. Once the curves are estimated, all the debt is measured, factoring in the spreads relative to the most liquid and representative money-market curves.

The Group's derivatives are measured using the valuation techniques and models normally used in the market, based on these money-market curves and volatility prices available in the market.

The breakdown of financial assets and liabilities of the Telefónica Group at December 31, 2007 and 2006 is as follows:

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Millions of euros

	Fair value through profit or loss Held for trading	Fair value option	Available- for-sale	Amortized cost	Hedges	Total carrying amount	Total fair value
December 31, 2007							
Non current financial assets	525	52	2,701	1,461	1,080	5,819	5,866
Investments	122		2,113			2,235	2,235
Long-term credits		52	588	932		1,572	1,608
Long-term prepayments				97		97	84
Deposits and guarantees				813		813	456
Derivative instruments	403				1,080	1,483	1,483
Provisions				(381)		(381)	
Current financial investments	151	284	6	6,187	59	6,687	6,687
Financial investments	151	284	6	1,122	59	1,622	1,622
Cash and cash equivalents				5,065		5,065	5,065
TOTAL	676	336	2,707	7,648	1,139	12,506	12,553

Millions of euros

	Fair value through profit or loss Held for trading	Fair value option	Available- for-sale	Amortized cost	Hedges	Total carrying amount	Total fair value
December 31, 2006							
Non-current financial assets	188	93	2,741	1,278	924	5,224	5,224
Investments	111		2,100			2,211	2,211
Long-term credits		93	641	821		1,555	1,546
Long-term prepayments				132		132	128
Deposits and guarantees				685		685	338
Derivative instruments	77				924	1,001	1,001
Provisions				(360)		(360)	
Current financial assets	72	343	23	5,011	23	5,472	5,472
Financial investments	72	343	23	1,219	23	1,680	1,680
Cash and cash equivalents				3,792		3,792	3,792
TOTAL	260	436	2,764	6,289	947	10,696	10,696

Table of Contents**Non-current financial assets**

The detail of and movement in this heading and the corresponding provision at December 31, 2007 and 2006 is as follows:

	Millions of euros						
	Investments	Long-term credits	Derivative financial assets	Deposits and guarantees given	Long-term prepayments	Provisions	Total
Balance at 12/31/05	2,520	1,442	312	612	175	(380)	4,681
Additions	6	449	1,534	524	766	(4)	3,275
Disposals	(188)	(115)	(841)	(133)	(779)	7	(2,049)
Inclusion of companies	134	8		28	(8)		162
Exclusion of companies	5	(137)		(338)			(470)
Translation differences	1	(12)	3	(5)	(6)	1	(18)
Fair value adjustments	568	(60)	(2)				506
Transfers	(835)	(20)	(5)	(3)	(16)	16	(863)
Balance at 12/31/06	2,211	1,555	1,001	685	132	(360)	5,224
Additions	11	550	632	169	71	(17)	1,416
Disposals	(54)	(273)	(650)	(62)	(147)	(2)	(1,188)
Exclusion of companies		(1)	(3)	(51)			(55)
Translation differences	11	13	(2)	49	(3)		68
Fair value adjustments	95	(60)	508	2	75		620
Transfers	(39)	(212)	(3)	21	(31)	(2)	(266)
Balance at 12/31/07	2,235	1,572	1,483	813	97	(381)	5,819

Investments includes the market value of investments in companies where Telefónica does not exercise significant control and for which there is no specific disposal plan for the short term. We would highlight the investments at December 31, 2007 in Banco Bilbao Vizcaya Argentaria, S.A. (BBVA) of 607 million euros (661 million euros at December 31, 2006), in China Netcom of 682 million euros (675 million euros at December 31, 2006) and in Sogecable of 634 million euros (622 million euros at December 31, 2006).

In addition, on November 7, 2007 Portugal Telecom, S.G.P.S., S.A. granted a dividend in kind whereby Telefónica, S.A. obtained the right to receive 0.176067 shares of PT Multimedia, S.G.P.S., S.A. (listed on the Lisbon Stock Exchange and whose main shareholder was Portugal Telecom) for each share of Portugal Telecom held by the Group. The valuation of the shares received at the distribution date was 9.18 euros per share. At the end of 2007, the amount recognized for those shares under Investments was 161 million euros.

Transfers in 2006 were due mainly to the inclusion in the consolidation scope of O2 plc, which at December 31, 2005 was recognized under Investments at a carrying amount of 1,266 million euros, as well as the removal from the consolidation scope of Sogecable, carried at 502 million euros (see Note 9).

Disposals in 2006 mainly related to the sale of the shareholding in Uno e-Bank, S.A. (see Appendix I).

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Long-term credits includes mainly the investment of the net level premium reserves of the Group's insurance companies, mainly in fixed-income securities, amounting to 640 million and 734 million euros at December 31, 2007 and 2006, respectively, carried at market value. It also includes the long-term loans to associates described in Note 9, and the financing granted to Sogecable in accordance with the commitments in relation to the integration of the satellite platforms, totaling 201 million euros (221 million euros at December 31, 2006).

Derivative financial assets includes the fair value of derivatives to hedge assets or liabilities whose maturity is 12 months or greater, as part of the Group's financial risk-hedging strategy (see Note 16).

Deposits and guarantees consists of 813 million euros to cover guarantees at December 31, 2007 (685 million euros at December 31, 2006). These deposits will decrease as the respective obligations they are guaranteeing are reduced.

Current financial assets

This heading in the accompanying consolidated balance sheet at December 31, 2007 and 2006 includes mainly the following items:

Current financial assets recognized at fair value to cover commitments assumed by the Group's insurance companies, amounting to 290 million euros at December 31, 2007 (365 million euros at December 31, 2006). The maturity schedule for these financial assets is established on the basis of payment projections for the commitments.

Derivative financial assets not used to hedge non-current balance sheet items, which amounted to 210 million euros (93 million euros in 2006) (see Note 16).

Short-term deposits and guarantees, including the deposit by Telecomunicaciones de Sao Paulo of 102 million euros as downpayment for the acquisition of Navy Tree Participações, S.A. (see Appendix I).

Current investments of cash surpluses which, given their characteristics, have not been classified as Cash and cash equivalents.

Current financial assets that are highly liquid and are expected to be sold within three months or less are recorded under Cash and cash equivalents on the accompanying consolidated balance sheet.

Table of Contents**Interest bearing debt**

The detail of this heading in the years ended December 31, 2007 and 2006 is as follows:

Millions of euros	Balance at 12/31/07	Balance at 12/31/06
Issues	30,057	29,142
Interest-bearing debt	23,665	29,557
Other financial liabilities	206	358
Total	53,928	59,057
Total non-current	46,942	50,676
Total current	6,986	8,381

The breakdown of the Group's financial liabilities at 31 December 2007 and 2006 is as follows:

Millions of euros						
	Fair value through profit or loss		Liabilities at		Total	
	Held for trading	Fair value option	amortized cost	Hedges	carrying amount	Total fair value
December 31, 2007						
Issues			30,057		30,057	30,420
Interest-bearing debt	292		20,822	2,551	23,665	24,179
Other financial liabilities			206		206	206
Total financial liabilities	292		51,085	2,551	53,928	54,805

Millions of euros						
	Fair value through profit or loss		Liabilities at		Total	
	Held for trading	Fair value option	amortized cost	Hedges	Carrying amount	Total fair value
December 31, 2006						
Issues			29,142		29,142	28,942
Interest-bearing debt	184		27,315	2,058	29,557	31,724
Other financial liabilities			358		358	358
Total financial liabilities	184		56,815	2,058	59,057	61,024

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a) Issues

The detail of debentures, bonds and other marketable debt securities in 2007 and 2006 is as follows:

Millions of euros	Domestic currency issues	Foreign currency issues	Promissory notes & commercial paper	Other marketable debt securities	Total
Balance at 12/31/05	5,476	5,846	2,498	2,015	15,835
New issues	6,016	7,512	5,071	324	18,923
Redemptions, conversions and exchanges	(1,299)	(369)	(5,007)		(6,675)
Changes in consolidation scope	1,568				1,568
Revaluation and other movements	(2)	(458)	19	(68)	(509)
Balance at 12/31/06	11,759	12,531	2,581	2,271	29,142
New issues	2,031	2,178	1,026	114	5,349
Redemptions, conversions and exchanges	(1,504)	(252)	(1,507)	(374)	(3,637)
Revaluation and other movements	(570)	(399)	102	70	(797)
Balance at 12/31/07	11,716	14,058	2,202	2,081	30,057

Debentures, bonds and other marketable debt securities

The details of outstanding debentures and bonds at December 31, 2007 and 2006 is as follows:

Millions of euros	Nominal value at 12/31/07	Nominal value at 12/31/06
Issues by Telefónica, S.A. and captive finance companies	21,860	19,322
Issues by foreign operators	3,247	4,479
Promissory notes & commercial paper	2,456	2,651
Other marketable debt securities	2,000	2,362
Interest, fees and other movements	494	328
Total issues (carrying amount)	30,057	29,142

Appendix II presents the characteristics of all outstanding debentures and bond issues at year-end 2007 and 2006, as well as the significant issues made in each year.

Table of Contents*Promissory notes*

At December 31, 2007 and 2006, Telefónica, S.A. had an outstanding promissory note program with borrowing capacity of up to 2,000 million euros. The outstanding balance at December 31, 2007 was 937 million euros (1,642 million euros at December 31, 2006), carrying an average interest rate of 4.50% (3.73% at December 31, 2006).

Commercial paper

At December 31, 2007 and 2006, Telefónica Europe, B.V. had an outstanding commercial paper program with borrowing capacity of up to 2,000 million euros. The outstanding balance at December 31, 2007 was 907 million euros (924 million euros at December 31, 2006), carrying an average interest rate of 4.70% (3.57% at December 31, 2006).

Other marketable debt securities

This heading consists mainly of preferred shares issued by Telefónica Finance USA, LLC, with a redemption value of 2,000 million euros. These shares were issued in 2002 and have the following features:

Interest rate up to December 30, 2012 of 3-month Euribor, and maximum and minimum effective annual rates of 7% and 4.25%, respectively, and from then 3-month Euribor plus a 4% spread.

Interest is paid every three calendar months provided the Telefónica Group generates consolidated net income.

b) Interest-bearing debt

The detail of interest-bearing debt is as follows:

Millions of euros	Balance at 12/31/07			Balance at 12/31/06		
	Current	Non-current	Total	Current	Non-current	Total
Loans and other payables	3,069	17,753	20,822	3,235	24,080	27,315
Derivative financial liabilities (Note 16)	527	2,316	2,843	174	2,068	2,242
Total	3,596	20,069	23,665	3,409	26,148	29,557

The average interest rate on loans and other payables at December 31, 2007 was 5.29% (4.35% in 2006). This percentage does not include the impact of hedges arranged by the group.

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The detail of the main items under this heading at December 31, 2007 and 2006 is as follows:

Name/summary Holding company	Value date	Maturity date	Currency	Limit (12/31/07)	12/31/07		12/31/06	
					Balance (million)	Balance (million euros)	Balance (million)	Balance (million euros)
3bn syndicated loan BS acquisition	07/06/2004	07/06/2009	USD EUR	302	302	205	1,152 1,800	875 1,800
Syndicated loan savings banks	04/21/2006	04/21/2017	EUR	700	700	700	700	700
6bn syndicated loan Cesky acquisition	06/28/2005	06/28/2011	EUR	6,000	6,000	6,000	6,000	6,000
GBP syndicated loan O2 acquisition	12/14/2006	12/14/2008	GBP				700	1,042
		12/14/2009	GBP	1,050	1,050	1,432	1,050	1,564
		12/14/2010	GBP				1,050	1,564
		12/14/2012	GBP	2,100	2,100	2,864	2,100	3,127
		12/13/2013	GBP	1,071	1,071	1,460	2,100	3,127
EIB Holding	Misc.	Misc.	EUR	633	633	633	616	616
	Misc.	Misc.	USD	989	989	672	1,035	786
JPY loan	08/23/2007	07/27/2037	JPY	15,000	15,000	91		
ECAS structured facility	11/26/2004	11/15/2010	USD	191	191	130	266	202
Other operators								
Syndicated loan TM Chile May06	05/05/2006	01/05/2011	USD	180	180	122	180	136
Syndicated loan TM Chile Nov06	11/15/2006	11/15/2012	CLP	100,000	100,000	137	100,000	143
VIVO bilateral loan (1)	01/29/2007	01/29/2015	BRL	124	82	32		
	08/09/2007	08/15/2014	BRL	750	303	116		
EIB-VIVO financing 2007 (1)	10/31/2007	12/19/2014	USD	125	50	34		
EIB-VIVO financing 2000 (1)	08/01/2000	06/15/2008	USD	19	19	13	19	14
	08/01/2000	06/13/2008	USD	7	7	5	7	5

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Telesp bilateral loan	10/23/2007	04/23/2015	BRL	2,000	800	307		
EIB ANDINO	08/02/2006	2019	USD	100	107	73		
	07/11/2006	2017	USD	40	51	35		
	07/16/2006	2019	USD	40	60	40		
EIB financing								
Telefónica del Perú	11/30/1998	09/15/2013	USD	28	28	19	33	25
IEB financing								
Telefónica Móviles								
Perú	12/18/2006	12/18/2018	USD	38	38	26	38	29
	04/03/2007	04/03/2019	USD	13	13	9		
Other						8,512		7,802
Total						23,665		29,557

(1) VIVO
operations are
included using
proportionate
consolidation at
50%

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The main repayments made in 2007 and 2006 were as follows:

Name/summary	Signing date	Maturity date	Amount of contract		Principal repaid		Repayment date
Main repayments in 2007							
3bn syndicated loan BS acquisition	07/06/2004	07/06/2009	3,000	EUR	400	EUR	04/11/2007
					1,000	EUR	06/15/2007
					400	EUR	03/30/2007
					850	USD	07/16/2007
GBP syndicated loan O2 acquisition	12/14/2006	12/14/2008	7,000	GBP	700	GBP	01/31/2007
		12/14/2010			1,050	GBP	07/30/2007
		12/13/2013			1,600	EUR	07/30/2007
ECAS structured facility	11/26/2004	11/15/2010	191	USD	38	USD	05/15/2007
					38	USD	11/15/2007
Main repayments in 2006							
Syndicated loan February 1999	02/19/2000	02/20/2006	12,000	EUR	556	EUR	02/20/2006
ECAS structured facility	11/26/2004	11/15/2010	191	USD	38	USD	05/15/2006
					38	USD	11/15/2006
BBVA USD loan	12/21/2004	07/03/2006	115	USD	38	USD	07/03/2006

The maturity schedule of interest-bearing debt at December 31, 2007 is as follows:

Item	Millions of euros						Total
	2008	2009	2010	2011	2012	Subsequent years	
Loans and other payables	3,069	1,684	373	6,605	3,493	5,598	20,822
Derivative financial instruments	527	284	1,064	113	59	796	2,843
Total	3,596	1,968	1,437	6,718	3,552	6,394	23,665

At December 31, 2007, the Telefónica Group had total unused credit facilities from various sources amounting to over 9,250 million euros (over 8,000 million euros at December 31, 2006).

Table of Contents**Foreign-currency loans**

Foreign-currency loans at December 31, 2007 and 2006, along with the equivalent value in euros, are as follows:

Currency	Outstanding balance (in millions)			
	Currency		EUR	
	12/31/07	12/31/06	12/31/07	12/31/06
US dollars	4,167	4,455	2,833	3,384
Brazilian reais	1,537	143	590	51
Argentine pesos	631	361	136	89
Colombian pesos	7,700,091	7,433,640	2,595	2,520
Yen	81,326	57,834	493	369
Chilean pesos	99,678	165,420	231	235
New soles	1,014	768	230	183
Pounds sterling	2,205	3,962	3,008	5,865
Mexican pesos		142		10
Other currencies			7	8
Total			10,123	12,714

c) Other financial liabilities

This heading includes financial commitments at December 31, 2007 and 2006, most notably the purchase commitment with minority shareholders in Colombia de Telecomunicaciones, S.A., ESP, valued at 206 and 291 million euros, respectively (see Note 21).

(14) TRADE AND OTHER PAYABLES

The breakdown of this heading is as follows:

Millions of euros	12/31/07		12/31/06	
	Non-current	Current	Non-current	Current
Trade payables		8,642		8,450
Advances received on orders		87		82
Other payables	430	4,394	354	3,934
Deferred income	585	1,349	628	1,407
Payable to associates		84		80
Total	1,015	14,556	982	13,953

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The breakdown of current and non-current deferred income at December 31, 2007 and 2006 is as follows:

Millions of euros	12/31/07		Total	12/31/06		Total
	Non-current	Current		Non-current	Current	
Connection fees and other deferred revenues	529	1,349	1,878	575	1,407	1,982
Government grants	56		56	53		53
Total	585	1,349	1,934	628	1,407	2,035

The above amount for connection fees includes the customer connection charges not yet recognized as revenue. It will be recognized as revenue over the estimated duration of the customer relationship (see Note 3.o).

The breakdown of Other payables under current liabilities at December 31, 2007 and 2006 is as follows:

Millions of euros	Balance at 12/31/07	Balance at 12/31/06
Dividends payable by Group companies	201	3
Payables to suppliers of property, plant and equipment	2,094	2,398
Guarantees and deposits	45	40
Accrued employee benefits	737	547
Other non-financial non-trade payables	1,317	946
Total	4,394	3,934

Table of Contents**(15) PROVISIONS**

The detail of provisions in 2007 and 2006 is as follows:

Millions of euros	12/31/07			12/31/06		
	Current	Non-current	Total	Current	Non-current	Total
Employee benefits:	936	4,634	5,570	569	4,826	5,395
- <i>Post-employment plan</i>	917	3,667	4,584	569	3,798	4,367
- <i>Post-employment defined benefit plans</i>	12	718	730		814	814
- <i>Other benefits</i>	7	249	256		214	214
Other provisions	339	1,527	1,866	592	1,461	2,053
Total	1,275	6,161	7,436	1,161	6,287	7,448

Employee benefitsa) Post-employment plans

In the last few years, Telefónica has carried out early retirement plans in order to adapt its cost structure to the prevailing environment in the markets where it operates, making certain strategic decisions relating to its size and organization.

In this respect, on July 29, 2003, the Ministry of Labor and Social Affairs approved a labor force reduction plan for Telefónica de España that included up to 15,000 job reductions in the period from 2003 to 2007, through voluntary, universal and non-discriminatory programs. The approval of the labor force reduction plan was announced on July 30, 2003. In 2007 and 2006, the Company approved a total of 1,102 and 2,985 requests for voluntary severance, for which provisions amounting to 361 million and 934 million euros, respectively, were recorded (see Note 19), with a charge to Personnel expenses in the consolidated income statement.

The entire plan concluded on December 31, 2007, with 13,870 employees taking part for a total cost of 3,916 million euros.

Provisions recorded for this plan at December 31, 2007 and 2006 amounted to 2,976 and 2,990 million euros, respectively.

Furthermore, at December 31, 2007 the Group had allocated provisions totaling 966 million euros (1,366 million euros at December 31, 2006) for other planned adjustments to the workforce and plans prior to 2003.

The companies bound by these commitments calculated provisions required at 2007 year-end using actuarial assumptions pursuant to current legislation, including the PERM/F-2000 C mortality tables and a variable interest rate based on market yield curves.

The Group is still making efforts to adapt headcount in line with the integration of its businesses, for which it has recorded provisions of 838 million euros, mainly in Latin America (306 million euros), Spain (325 million euros) and Europe (158 million euros) (see Note 19).

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The movement in provisions for post-employment plans in 2007 and 2006 is as follows:

Millions of euros	Total
Provisions for post-employment plans at 12/31/05	4,247
Additions	1,045
Retirements/amount applied	(919)
Transfers	(6)
Provisions for post-employment plans at 12/31/06	4,367
Additions	1,277
Retirements/amount applied	(1,105)
Transfers	53
Translation differences	(8)
Provisions for post-employment plans at 12/31/07	4,584

b) Post-employment defined benefit plans.

The Group has a number of defined benefit plans in the countries where it operates. The following tables present the main data of these plans:

12/31/07	Millions of euros					Total
	ITP	Survival	O2 Group	Telesp	Other	
Obligation	483	152	984	99	40	1,758
Assets			(1,014)	(89)	(65)	(1,168)
Asset limitation			7	20	14	41
Net provision	483	152	35	37	23	730
Net assets			58	7	34	99

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12/31/06	Millions of euros					Total
	ITP	Survival	O2 Group	Telesp	Other	
Obligation	534	153	1,027	82	29	1,825
Assets			(983)	(64)	(45)	(1,092)
Asset limitation					6	6
Net provision	534	153	44	18	65	814
Net assets					75	75

The amount recognized directly in equity in 2007 and 2006 related to these plans is the following:

Millions of euros	2007	2006
ITP and Survival	25	36
O2 Group	36	87
Telesp	(11)	(10)
Other	4	(1)
Total	54	112

The Group's principal defined benefit plans are:

a) Plans in Spain:

- a. ITP: Telefónica Spain 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 (Institución Telefónica de Previsión). Once the aforementioned supplementary pension payments had been quantified, they became 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.

The amount for this provision totaled 483 million euros at December 31, 2007 (534 million euros at December 31, 2006).

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- b. Survival: Serving employees who did not join the defined pension plan continue to be entitled to receive survivorship benefits at the age of 65.

The amount for this provision totaled 152 million euros at December 31, 2007 (153 million euros at December 31, 2006).

These plans do not have associated assets which qualify as assets assigned to the plan under IAS 19.

The main actuarial assumptions used in valuing these plans are as follows:

	Survival		ITP	
	12/31/07	12/31/06	12/31/07	12/31/06
Discount rate	4.224 - 4.463%	3.6582%	4.1792	3.5108%
Expected rate of salary increase	2.50%	2.50%		
Mortality tables	PERM/F-2000C combined with OM77	PERM/F-2000C combined with OM77	PERM/F 2000-C	PERM/F 2000-C

The accompanying consolidated income statement includes employee benefits expense for the cost of services corresponding to current employees totaling 6 million euros in both 2007 and 2006.

The financial expense recorded for these commitments totaled 27 million euros in 2007 (25 million in 2006)).

b) Plans in the rest of Europe:

The various O2 Group companies consolidated within the Telefónica Group have defined benefit post-employment plans, covered by qualifying assets.

The number of employees covered by these plans at December 31, 2007 is as follows:

	Employees
UK	4,650
Germany	4,963
Other	393
Total	10,006

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The main actuarial assumptions used in valuing these plans are as follows:

	UK	Germany	Other
Nominal rate of salary increase	4.65%-5.15%	3.0%	4.9%
Nominal rate of pension payment increase	3.2%-3.4%	2.0%	3.2%-3.4%
Discount rate	5.7%	5.3%	5.7%
Expected inflation	3.4%	2.0%	3.4%
Expected return on plan assets			
- Shares	7.6%	N/A	7.6%
- UK government bonds	4.4%	N/A	4.4%
- Other bonds	5.0%	N/A	5.0%
- Rest of assets	4.4%	4.25%	4.4%
		Heubeck	
Mortality tables	Pa92mc	2005	Pa92mc

The commitments under these plans, as well as the value of the associated assets at December 31, 2007 are as follows:

Millions of euros	UK	Other	Total
Fair value of plan assets:			
- Shares	830	25	855
- Bonds	72	17	89
- Rest of assets	25	45	70
Total fair value of plan assets	927	87	1,014
Present value of obligations	869	115	984
Provision before asset limitation	(58)	28	(30)
Asset limitation		7	7
Provision on balance sheet	(58)	35	(23)

In the consolidated income statement, the expenses for the cost of current employees of companies belonging to the O2 Group, net of contributions by employees, as employee benefits expenses amounted to 34 million euros in 2007 (47 million euros in 2006).

The financial expense recognized for discounting the commitments amounted to 53 million euros (43 million euros in 2006), which, net of the expected return on the related assets, totaling 70 million euros (56 million euros in 2006), led to financial revenues amounting to 17 million euros (13 million euros in 2006).

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The movements in the present value of the commitments relating to these plans in 2007 are as follows:

	Millions of euros
Present value of obligation at 01/31/06	989
Translation differences	13
Current service cost	56
Accrued past service cost	1
Interest cost	43
Actuarial losses (gains)	(69)
Benefits paid	(6)
Present value of obligation at 12/31/06	1,027
Translation differences	(96)
Current service cost	39
Accrued past service cost	1
Interest cost	53
Actuarial losses (gains)	(29)
Benefits paid	(11)
Present value of obligation at 12/31/07	984

The movements in the fair value of the assets associated with these obligations are as follow.

	Millions of euros
Fair value of the assets at 01/31/06	855
Translation differences	12
Expected return on plan assets	56
Actuarial losses (gains)	18
Company contributions	39
Employee contributions	9
Benefits paid	(6)
Fair value of the assets at 12/31/06	983
Translation differences	(87)
Expected return on plan assets	70
Actuarial losses (gains)	7
Company contributions	47
Employee contributions	5
Benefits paid	(11)
Fair value of the assets at 12/31/07	1,014

Table of Contents*c) Plans in Latin America:*

Telecomunicações de São Paulo, S.A., and its subsidiaries had various pension, medical insurance and life insurance obligations with employees.

The main actuarial assumptions used in valuing these plans are as follows:

	12/31/07	12/31/06
Discount rate	10.77%	10.24%
Nominal rate of salary increase	6.59%	6.08%
Expected inflation	4.50%	4.00%
Cost of health insurance	7.64%	7.12%
Expected return on plan assets	9.61-11.15%	10.61-12.75%
Mortality table	AT 83	AT 83

Employee benefits expenses recognized in relation to current service costs at Telesp group companies totaled 1 million euros in 2007 and 2006.

Furthermore, financial expenses recognized for discounting the cost of these commitments in 2007 and 2006 totaled 9 and 8 million euros, respectively. The expected return on plan assets generated financial revenues totaling 8 million euros in both 2007 and 2006.

The valuations used to determine the value of the obligations and plan assets, where appropriate, were performed on December 31, 2007 by external and internal actuaries. The projected unit credit method was used in all cases.

c) Other benefits

This heading mainly includes the amount recorded by Telefónica de España for accrued long-service bonuses to be awarded to employees after 25 years service.

Table of Contents**Other provisions**

The movement of the provisions under this heading in 2007 and 2006 is as follows:

	Millons of euros
Other provisions at December 31, 2005	1,814
Additions	661
Retirements/amount applied	(506)
Transfers	(33)
Inclusion of companies	160
Exclusion of companies	(17)
Translation differences	(26)
Other provisions at December 31, 2006	2,053
Additions	618
Retirements/amount applied	(342)
Transfers	(29)
Inclusion of companies	61
Exclusion of companies	(536)
Translation differences	41
Other provisions at December 31, 2007	1,866

Other provisions at December 31, 2007 include the amount recorded in the year in relation to the 152 million euro fine imposed on Telefónica de España, S.A.U. by the EC anti-trust authorities (see Note 21).

Also included are the asset retirement obligations recognized by Group companies in the amount of 151 million euros (128 million euros in 2006).

Exclusion of companies mainly relates to provisions for the Endemol Group, which at December 31, 2006 amounted to 486 million euros.

Finally, Other Provisions in 2007 and 2006 also includes the provisions recorded (or used) by the Group companies to cover the risks inherent in the realization of certain assets, the contingencies arising from their respective business activities and the risks arising from commitments and litigation acquired in other transactions, recognized in accordance with Note 3.1.

Given the nature of the risks covered by these provisions, it is not possible to determine a reliable schedule of potential payments, if any.

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(16) DERIVATIVE FINANCIAL INSTRUMENTS AND RISK MANAGEMENT POLICIES

The Telefónica Group is exposed to various financial market risks as a result of (i) its ordinary business activity, (ii) debt taken on to finance its business, (iii) investments in companies, and (iv) other financial instruments related to the above commitments.

The main market risks affecting the Group are as follows:

1. Exchange rate risk

Exchange rate risks arise mainly from two sources. The first is Telefónica's international presence, through its investments and businesses in countries that use currencies other than the euro. These are largely in Latin America, but also in the Czech Republic and the UK. The second is debt denominated in currencies other than that of the country where the business is conducted or the home country of the company taking on the debt.

2. Interest rate risk

This arises from changes in (i) financial expenses on floating rate debt (or short-term debt likely to be renewed), due to changes in interest rates and (ii) the value of long-term liabilities at fixed interest rates.

3. Share price risk

This arises from changes in the value of equity investments that may be bought, sold or otherwise involved in transactions, from changes in the value of derivatives associated with such investments, from treasury shares and from equity derivatives.

The Group is also exposed to liquidity risk if a mismatch arises between its financing needs (operating and financial expense, investment, debt redemptions and dividend commitments) and its sources of finance (revenues, divestments, credit lines from financial institutions and capital market operations). The cost of finance could also be affected by movements in the credit spreads (over benchmark rates) demanded by lenders.

Finally, there is so-called country risk (which overlaps with market and liquidity risks). This refers to the possible decline in assets, cash flows generated or cash flows returned to the parent company as a result of political, economic or social instability in the countries where Telefónica Group operates, especially in Latin America.

The Telefónica Group actively manages these risks with a view to stabilize:

cash flows, to facilitate financial planning and take advantage of investment opportunities,

the income statement, to make it easier for investors to understand and forecast company results,

share capital, to protect the value of the investment.

Where these aims conflict, the Group's financial management will decide which should be given priority.

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Telefónica uses derivatives to manage risks, basically on exchange rates, interest rates and shares.

Exchange rate risk

The fundamental objective of the Group's exchange rate risk management policy is to offset (at least partly) any impairment of assets related to Telefónica's business due to declines in exchange rates versus the euro, with savings on the euro value of foreign-denominated debt (which will decline simultaneously). The degree of hedging (i.e. the proportion of foreign currency debt as a percentage of foreign currency assets) tends to be higher in the following circumstances:

the closer the estimated correlation between the value of the asset and the value of the currency, and

the cheaper the estimated cost of hedging (measured as the difference between the additional financial expenses of borrowing in local currency and the expected depreciation in the local currency versus the euro).

the more liquid the local currency and derivative markets.

In general, the correlation between asset values and the exchange rate is closer when cash flows generated by the asset in the early years of the investment represent a large proportion of its estimated value.

At December 31, 2007 net financial debt¹ in Latin American currencies amounted to nearly 6,968 million euros (7,306 million euros in 2006). However, this debt is not distributed in proportion to the cash flows generated in each country. Its future effectiveness as a hedge of exchange rate risks therefore depends on which currencies depreciate.

The Group further protects itself against declines in Latin American exchange rates affecting its assets through the use of dollar-denominated debt, either in Spain (where such debt is associated with the investment as long as it is considered to be an effective hedge) and in the country itself, where the market for local currency financing or hedges may be inadequate or non-existent. At December 31, 2007 the Group's net dollar-denominated debt amounted to the equivalent of 1,481 million euros net of the effect of the derivative contracts and financial assets in dollars (1,462 million euros in 2006).

¹ **Net financial debt =**
 LT financial debt+ST
 financial
 debt-short-term
 investments-cash and
 cash
 equivalents-financial
 and other non-current
 assets.

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To protect its investment in the Czech Republic, the Group has synthetic debt denominated in Czech crowns which, at December 31, 2007, amounted to the equivalent of 3,102 million euros, compared to 1,997 million euros in 2006. This increase was due to a change in the hedging objective in 2007 from 50% to 70% of the initial acquisition cost due to the expected appreciation of the Czech crown vis-à-vis the euro.

Regarding protection of the investment in the UK, the disposal of Airwave for 1,932 million pounds sterling prompted the Group to modify the hedging objective to 50% from 70%. Debt denominated in pounds sterling at December 31, 2007 was equivalent to 6,702 million euros, which is less than the 11,095 million euros at December 31, 2006.

The Group also manages exchange rate risk by seeking to minimize the negative impact of any remaining exchange rate exposure on the income statement. Such exposure can arise for any of three reasons: (i) a thin market for local derivatives or difficulty in sourcing local currency finance, which makes it impossible to arrange a low-cost hedge (as in Argentina and Venezuela for example), (ii) financing through intra-group loans, where the accounting treatment of exchange rate risk is different from that for financing through capital contributions, (iii) as the result of a deliberate policy decision.

In 2007, exchange rate management resulted in gains totaling 7.3 million euros (61 million euros in 2006).

If the exchange rate position affecting the income statement at the end of 2007 would remain constant in 2008 and Latin American currencies depreciated against the US dollar and the rest of the currencies against the euro by 10%, the impact on the income statement would be an expense of 69 million euros. However, as mentioned above, the Group follows an active management policy to reduce these impacts.

As indicated previously, the fundamental objective of the Group's exchange rate risk management policy is to offset (at least partly) any impairment of assets related to Telefónica's business due to declines in exchange rates versus the euro, with savings on the euro value of foreign-denominated debt (from depreciation by the euro). For some investments, the hedge benchmark is a percentage of acquisition cost (e.g. pound sterling and Czech crown), whereas others are defined in terms of expected cash flows in the next two years (mainly Latin America). As management's objective is not an accounting indicator, no sensitivity analysis is presented of changes in translation differences (equity) due to currency appreciation against the euro.

Table of Contents**Interest rate risk**

Telefónica's financial expenses are exposed to changes in interest rates. In 2007, the rates applied to the largest volumes of short-term debt were based on the Euribor, sterling Libor (because of the acquisition of O2 plc), Brazilian SELIC, the dollar Libor and the Colombian UVR. At December 31, 2007, 50.4% of total nominal net debt (or 51.1% of nominal long-term net debt) was at fixed rates for over one year, compared to 45.4% of total debt² (46.3% of long-term debt) in 2006. Of the remaining 49.6% (debt at floating or fixed rates maturing in less than one year), the interest rate on 46 percentage points was set for a period of more than one year (27% of long-term debt), compared to 41 percentage points on debt at floating or fixed rates maturing in less than one year (23% of long-term debt) at December 31, 2006. In 2007, cap and floor structures were arranged for an equivalent amount of 7,972 million euros to increase and extend the term of the hedged debt.

In addition, early retirement liabilities were discounted to present value over the year using the forward interest rate curve on the swap markets. The increase in interest rates has reduced the size of these liabilities.

The net financial result for 2007 showed a loss of 2,844 million euros, 4% higher than in 2006. Excluding exchange rate differences, interest expense in 2007 and 2006 was 2,851 million euros and 2,795 million euros, respectively, implying a 2% increase in adjusted finance costs in 2007 compared to 2006. This increase is the result of two offsetting factors. On the one hand, the 5.8% decrease in the total average net debt balance (3,471 million euros at December 31, 2007) led to a decline of 200.4 million euros. On the other hand, interest expense rose by 257 million euros as a result of: a) a 38bp increase in the average cost of debt, mostly because the average net debt was at higher rates than the average for 2006 due to the higher relative weight of Latin American debt and the hikes in rates in GBP, EUR and USD versus 2006, and b) a 50 million euro increase in non-recurring income and the expense related to positions measured at fair value. The figure for financial expenses in 2007 implies an average cost of average total net debt of 5.59%, or 5.61% stripping out exchange rate gains.

To illustrate the sensitivity of finance costs to variability in short-term interest rates, assuming a 100 basis point rise in all currencies in which the Company has a financial position and no change in the currency make-up and balance of the position at year end, the financial expense would increase by 182 million euros.

² **Total debt =**
 Net financial
 debt+financial
 guarantees not
 considered in
 net financial
 debt+net
 personnel
 reorganization
 commitments.

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Share price risk

In 2007, Telefónica carried out the share buyback program announced in October 2003 and renewed in April 2005, for a value estimated at 6,000 million euros to 2007 (inclusive), which depended on the generation of cash flows and on the share price. Although at the end of 2007 there were no commitments to buy back more shares, Telefónica could acquire new commitments in this respect in the future if so decided at the General Shareholders Meeting.

At December 31, 2007, Telefónica, S.A. held 64,471,368 treasury shares (see Note 12). The net asset value of the treasury shares could increase or decrease depending on variations in the Telefónica share price.

At the Shareholders Meeting of Telefónica, S.A. on June 21, 2006, shareholders approved the introduction of a long-term incentive plan for managers and senior executives of Telefónica, S.A. and other Telefónica Group companies. Under this plan, selected participants who met the qualifying requirements were given the rights to earn a certain number of Telefónica, S.A. shares as a form of variable remuneration (see Note 20.a).

This plan consisted of a number of cycles. For the first cycle (July 1, 2006), the maximum number of shares amounted to 6,530,615, while in the second that maximum number to be assigned would be 5,556,234. According to the plan, the shares may be either (a) treasury shares in Telefónica, S.A., acquired by either Telefónica, S.A. itself or any of the Telefónica Group companies, in compliance with the legal requirements in force in this connection; or (b) newly-issued shares. The possibility of delivering shares to employees in the future, in accordance with relative shareholder remuneration or profit, implies a risk since there could be an obligation to hand over a maximum number of shares at the end of each cycle, whose acquisition (in the event of acquisition in the market) in the future could imply a higher cash outflow than required on the start date of each cycle if the share price is above the corresponding price on the cycle start date. In the event that new shares are issued for delivery to the beneficiaries of the plan, there would be a dilutive effect for the ordinary shareholder as a result of the higher number of shares outstanding.

To reduce risk and ensure the company has enough shares to meet its commitments at the end of the cycle commenced in 2006, Telefónica bought an instrument from a financial institution that will deliver to Telefónica, at the end of the cycle, a number of shares based on the same measure of success used in the plan. The maximum number of shares which Telefónica could receive is 7,200,000. The cost of this instrument was 46 million euros which, in unit terms, is equivalent to 6.43 euros per share (see Note 20).

Telefónica is also exposed to fluctuations in the share price of its investees, especially where these fall outside its core business and could be sold. In 2007, Telefónica sold its entire stakes in Airwave O2, Ltd. and Endemol Investment Holding, B.V. and part of its holding in Portugal Telecom, S.G.P.S., S.A. (representing 1.809% of share capital). Also in 2007, due to the non-monetary dividend paid by Portugal Telecom, Telefónica has received, directly and indirectly, a total of 16,879,406 shares of PT Multimedia, S.G.P.S., S.A (see Note 9).

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Liquidity risk

Telefónica seeks to match the schedule for its debt maturity payments to its capacity to generate cash flows to meet these maturities, allowing some flexibility. In practice, this translates into two key principles:

1. Group debt must have a longer average maturity than the time it will take to earn the cash to pay it (assuming internal projections are met, and all cash flows generated go to pay down debt rather than on dividends or acquisitions).
2. The Group must be able to pay all commitments over the next 12 months without accessing new borrowing or tapping the capital markets (although including firm credit lines arranged with banks), assuming budget projections are met.

As of December 31, 2007, the average maturity of the Group's 45,284 million euros net financial debt was 6.24 years. The Group would need to generate around 7,257 million euros per year to repay the debt in this period if it used all its cash for this purpose. Cash generation in 2007 amply exceeded this amount, so that if it maintains the same pace of cash generation during the average lifetime of the debt, the Group would repay the debt in its entirety before 6.24 years if it used all its cash for this purpose.

Gross debt maturities in 2008 amount to approximately 6,776 million euros (including the net position of hedges) and are lower than the availability of the funds, calculated as the sum of: a) current financial investments and cash at December 31, 2007 (6,477 million euros excluding derivative financial instruments); b) annual cash generation projected for 2008; and c) undrawn credit facilities arranged with banks whose initial maturity is over one year (more than 4,000 million euros at December 31, 2007). Accordingly, Telefónica will not need to tap the capital or credit markets in at least the next 12 months.

As a result of the higher debt at Telefónica following the acquisition of O2 shares and the excessive concentration of short-term debt maturities, Telefónica embarked on an ambitious refinancing plan, which led to the following actions in 2006 and 2007: (1) the refinancing of approximately 15,977 million euros via issues of bonds and debentures in international capital markets such as the euro, pound sterling, US dollar, yen and Czech crown (of which 3,974 million euros were issued in 2007 before the deterioration of the credit market – see Note 13-), and approximately 11,000 million euros in the syndicated credit and loan market; (2) the extension of the debt maturity (including the additional debt taken on after the acquisition of O2 in the UK) and, as a result, the extension of the average life of net financial debt from 3.75 to 6.24 years at the end of 2007; and (3) an approximately 5,389 million euro decrease in net financial debt in 2007 and an approximately 1,610 million euro decrease in post-employment benefit obligations.

The liquidity cushion existing after the execution of the refinancing plan (assuming the internal projections are met) will allow the Company to meet the rest of the financial commitments it acquires, focus on growing the business through new investment and/or bringing forward or increasing shareholder remuneration.

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The breakdown of estimated interest maturities without considering the remeasurement of financial liabilities existing at December 31, 2007 is as follows:

Millions of euros	Total	1 year	2 years	3 years	4 years	5 years	Over 5 years
Total	19,813	2,495	3,278	2,254	2,055	1,491	8,240

The estimate of interest rates applicable to floating rate debt is made based on forward rates of the most liquid money-market curves.

Country risk

Telefónica has managed or mitigated country risk by pursuing two lines of action (in addition to its normal business practices):

1. partly matching assets to liabilities (those not guaranteed by the parent company) in its Latin American companies such that any potential asset impairment would be accompanied by a reduction in liabilities,
2. repatriating funds generated in Latin America that are not required for the pursuit of new, profitable business development opportunities in the region.

Regarding this first point, Telefónica's Latin American companies now have external net debt not guaranteed by the Spanish companies of 4,385 million euros, i.e. 8.7% of the Group's total net financial debt, with Colombia (2,650 million euros), Brazil (1,292 million euros) and Peru (809 million euros), accounting for the bulk of the total.

Regarding the second point repatriation of funds Telefónica repatriated 2,250 million euros from Latin America in 2007, mostly through inter-group loans (repayment of principal and interest payment), capital decreases (1,398 million euros) and dividends (852 million euros) and the rest as interest and the payment of management fees.

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In this regard, it is worth noting that since February 2003, Venezuela has had an exchange control mechanism in place. The Currency Administration Commission (CADIVI) was set up to manage the exchange control system and determine authorizations of currency sales. This body has issued a number of regulations (*providencias*) governing the types of currency sales in Venezuela at the official exchange rate. Foreign companies which are duly registered as foreign investors are entitled to request approval to acquire currencies at the official exchange rate by the CADIVI, in line with regulation number 029, article 2, section c) Remittance of earnings, profits, income, interest and dividends from international investment. Telcel, the Group's subsidiary in Venezuela, obtained approval on 137 million US dollars under this heading in 2006 and 240 million US dollars in 2007. The final dividend of 365 million US dollars proposed recently is pending approval. Accordingly, the Group will have to continue obtaining the necessary authorizations in future for requests submitted to the CADIVI. It expects this to occur with the same diligence and frequency as in the past, enabling it to continue carrying out its businesses in Venezuela as normal and to repatriate funds from this country.

Credit risk

The Telefónica Group trades in derivatives with creditworthy counterparties. Telefónica, S.A. trades with credit entities with senior debt ratings of at least A. In Spain, where most of the Group's derivatives portfolio is, there are netting agreements with financial institutions, with debtor or creditor positions offset in case of bankruptcy, thus limiting the risk to the net position. Wherever operations allow, Telefónica, S.A. attempts to net risk positions with the various counterparties when arranging new trades. For example, if it takes a pay position in currency D, it will look for counterparties that have a receive position and it will settle with them when the conditions of the trade warrant. This reduces its potential credit risk. If the rating of a counterparty falls below A, it will study on a case-by-case basis whether to cancel the trades. The factors considered are: the period of the trade, whether the global position is a debtor position (no current credit risk) or creditor position, and the new rating.

For other subsidiaries, particularly those in Latin America, given the stable sovereign rating provides a ceiling and is below A, trades are with local financial entities whose rating by local standards is considered to be of high creditworthiness.

The Telefónica Group considers managing commercial credit risk as crucial to meeting its business and customer base growth targets in a manner that is consistent with its risk-management policy.

Therefore, the Group's commercial credit risk-management approach is based on continuous monitoring of the risk assumed and the resources necessary to manage the Group's various units, in order to optimize the risk-reward relationship in the development and implementation of their business plans in their ordinary management.

For this, uniform policies, procedures, authorization lines and management practices are established for all Group companies bearing in mind the individual needs and international best practice in this area, and including the commercial credit-risk management model in the Group's decision-making process, at both the strategic and the day-to-day operations level.

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Meanwhile, with credit risk arising from cash and cash equivalents, the Telefónica Group places its cash surpluses in high quality and highly liquid money-market assets. These placements are regulated by a General Framework, revised annually based on the conditions of the market and countries where the Group operates. The General Framework sets: (i) the maximum amounts to be invested by counterparty based on its rating (short- and long-term debt rating); (ii) the maximum period of the investment; and (iii) the instruments in which the surpluses may be invested. For Telefónica, S.A., the company which places the bulk of the Group's surpluses, the maximum placement in 2007 was 180 days and the creditworthiness of the counterparties used, measured by their debt ratings, remained above A- and/or A3 by S&P and Moody's, respectively.

The Group's maximum exposure to credit risk is initially represented by the carrying amounts of the financial assets (Notes 11 and 13) and the guarantees given by the Group (Note 20).

Capital management

The finance department of Telefónica, S.A., which is in charge of the Group's capital management, takes into consideration several factors when determining the company's capital structure.

The first is the consideration of cost of capital at all times to achieve a combination that optimizes this. For this, the company monitors the financial markets and updates to standard industry approaches for calculating cost of capital (WACC, weighted average cost of capital) in determining this variable. The second, a gearing ratio that enables the Company to obtain and maintain the desired credit rating over the medium term, and with which the Company can use to match its potential cash flow generation and the alternative uses of this cash flow at all times.

These general arguments are rounded off with other considerations and specifics, such as country risk in the broadest sense, tax efficiency and volatility in cash flow generation, when determining the Company's financial structure.

Derivatives policy

At December 31, 2007, the nominal value of outstanding derivatives with external counterparties amounted to 130,715 million euros. This amount is just 8.7% higher than in 2006 (120,267 million equivalent euros). This figure is inflated by the use in some cases of several levels of derivatives applied to the nominal value of a single underlying liability. For instance, a foreign currency loan can be hedged into floating rate, and then each interest rate period can be fixed using an FRA. Even using such techniques to reduce the position, it is still necessary to take extreme care in the use of derivatives to avoid problems arising through error or a failure to understand the real position and its associated risks.

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The Group's derivatives policy emphasizes the following points:

- 1) Derivatives based on a clearly identified underlying.

Acceptable underlyings include profits, revenues and cash flows in either a company's functional currency or another currency. These flows can be contractual (debt and interest payments, settlement of foreign currency payables, etc.), reasonably certain or foreseeable (investment program, future debt issues, commercial paper programs, etc.). The acceptability of an underlying asset in the above cases does not depend on whether it complies with IFRS requirements for hedge accounting, as is required in the case of certain intra-group transactions, for instance. Parent company investments in subsidiaries with functional currencies other than the euro also qualify as acceptable underlying assets.

Economic hedges, i.e. hedges with a designated underlying asset and which in certain circumstances offset fluctuations in the underlying asset value, do not always meet the requirements and effectiveness tests laid down by the various accounting standards for treatment as hedges. The decision to maintain positions that cease to qualify as effective or fail to meet other requirements will depend on the marginal impact on the income statement and how far this might compromise the goal of a stable income statement. In any event, the variations are recognized in the income statement.

- 2) Matching of the underlying to one side of the derivative.

This matching basically applies to foreign currency debt and derivatives hedging foreign currency payments by Group subsidiaries. The aim is to eliminate the risk arising from changes in foreign currency interest rates. Nonetheless, even when the aim is to achieve perfect hedging for all cash flows, the lack of breadth to certain markets, especially in Latin American currencies, has meant that historically there have been mismatches between the terms of the hedges and those of the debts they are meant to hedge. The Telefónica Group intends to reduce these mismatches, provided that doing so does not involve disproportionate costs. In this regard, if adjustment does prove too costly, the financial timing of the underlying asset in foreign currency will be modified in order to minimize interest rate risk in foreign currency.

Sometimes, the timing of the underlying as defined for derivative purposes may not be exactly the same as the timing of the contractual underlying.

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- 3) Matching the company contracting the derivative and the company that owns the underlying.

Generally, Telefónica aims to ensure that the hedging derivative and the hedged asset or liability belong to the same company. Sometimes, however, the holding companies (Telefónica, S.A. and Telefónica Internacional, S.A.) have arranged hedges on behalf of a subsidiary that owns the underlying asset. The main reasons for separating the hedge and the underlying asset were possible differences in the legal validity of local and international hedges (as a result of unforeseen legal changes) and the different credit ratings of the counterparties (whether Group companies or the banks).

- 4) Ability to measure the derivative's market value using the valuation systems available to the Group.

Telefónica uses a number of tools to measure and manage risks in derivatives and debt. The main ones are Kondor+, licensed by Reuters, which is widely used by financial institutions, and MBRM specialist financial calculator libraries.

- 5) Sale of options only when there is an underlying exposure.

Options can only be sold when: i) there is an underlying exposure (on the balance sheet or associated with a highly probable cash outflow) that would offset the potential loss for the year if the counterparty exercised the option, or ii) the option is part of a structure in which another derivative offsets any loss. The sale of options is also permitted in option structures where, at the moment they are taken out, the net premium is either positive or zero.

For instance, it would be possible to sell short-term options on interest rate swaps that entitle the counterparty to receive a certain fixed interest rate, below the level prevailing at the time the option was sold. This would mean that if rates fell and the counterparty exercised its option, Telefónica would swap part of its debt from floating rate to a lower fixed rate, having received a premium.

- 6) Hedge accounting:

The main risks that may qualify for hedge accounting are as follows:

Variations in market interest rates (either money-market rates, credit spreads or both) that affect the value of the underlying asset or the measurement of the cash flows.

Variations in exchange rates that change the value of the underlying asset in the company's functional currency and affect the measurement of the cash flow in the functional currency.

Variations in the volatility of any financial variable, asset or liability that affect either the valuation or the measurement of cash flows on debt or investments with embedded options, whether or not these options are separable.

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Variations in the valuation of any financial asset, particularly shares of companies held in the available-for-sale portfolio.

Regarding the underlying,

Hedges can cover all or part of the value of the underlying.

The risk to be hedged can be for the whole period of the transaction or for only part of the period.

The underlying may be a highly probable future transaction, or a contractual underlying (loan, foreign currency payment, investment, financial asset, etc.) or a combination of both that defines an underlying with a longer term.

This may on occasion mean that hedges have longer terms than the contractual underlying that they cover. This happens when Telefónica enters into long-term swaps, caps or collars to protect itself against interest rate rises that may raise the financial expense of its promissory notes, commercial paper and some floating rate loans which mature earlier than their hedges. These floating rate financing programs are highly likely to be renewed and the company commits to this by defining the underlying asset in a more general way as a floating rate financing program whose term coincides with the maturity of the hedge.

Hedges can be of three types:

Fair value hedges.

Cash flow hedges, which can be set at any value of the risk to be hedged (interest rates, exchange rates, etc.) or for a defined range (interest rates between 2% and 4%, interest rates above 4%). In this last case, the hedging instrument used is options and only the intrinsic value of the option is recognized as an effective hedge. Changes in the time value of the option are taken to the income statement.

Hedges on net investment in consolidated foreign subsidiaries. Generally such hedges will be arranged by Telefónica, S.A. and the other Group holding companies. Wherever possible, these hedges are implemented through real debt in foreign currency. Often, however, this is not always possible as many Latin American currencies are non-convertible, making it impossible for non-resident companies to issue local currency debt. It may also be that the debt market in the currency concerned is too thin to accommodate the required hedge (Czech crown, pound sterling), or that an acquisition is made in cash with no need for market finance. In these circumstances the Group uses derivatives, either forwards or cross-currency swaps to hedge the net investment. Pay fixed-rate foreign currency cross-currency swaps are valued using the forward method (the interest spread and changes in value of the derivative due to movements in interest rates are taken to equity).

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Pay floating rate foreign currency swaps are valued by the spot method (the interest spread and changes in value of the derivative due to movements in interest rates are taken to the income statement). As an exception to this general rule, for currencies with high interest spreads to the euro (such as the Brazilian real) the Group opts for short-term structures (around 1 year) and uses the spot rate method even when it is paying fixed-rate foreign currency, to make the income statement easier to understand. Hedges using forwards are analyzed on a currency-by-currency basis. Where technical market issues arise or the perception of exchange rate risk changes, the Group may decide to cancel the designation of a position as a hedge early, irrespective of its maturity. Similarly, for hedging positions nearing maturity (less than 3 months), due to technical market reasons such as liquidity etc., maturity may be brought forward (by taking an offsetting position or selling the derivative in the market). If it has been decided not to renew the hedge, the designation will be cancelled and the transaction can then be treated as effectively the same as the hedge reaching maturity. Otherwise, the hedge can be renewed early, in which case the first hedge's designation is cancelled and the new hedge designated in its stead. Sometimes, a derivative-based hedge may be renewed using foreign currency debt instruments.

Hedges can comprise a combination of different derivatives.

There is no reason to suppose management of accounting hedges will be static, with an unchanging hedging relationship lasting right through to maturity. In fact, hedging relationships may change to allow appropriate management that serves the Group's stated principles of stabilizing cash flows, stabilizing net financial income/expense and protecting the Group's share capital. The designation of hedges may therefore be cancelled, before maturity, either because of a change in the underlying or because of a change in perceived risk on the underlying. Derivatives included in these hedges may be reassigned to new hedges where they meet the effectiveness test and the new hedge is well documented. To gauge the efficacy of transactions defined as accounting hedges, the Group analyzes the extent to which the changes in fair value or in the cash flows attributable to the hedge would offset the changes in fair value or cash flows attributable to the hedged risk, using a linear regression model in the analysis.

The main guiding principles for risk management are laid down by Telefónica Group's Corporate Finance Department and implemented by company CFOs (responsible for balancing the interests of each company and those of the Group). The Corporate Finance Department may allow exceptions to this policy where this can be justified, normally when the market is too thin for the volume of transactions required or on clearly limited and small risks. New companies joining the Group as a result of mergers or acquisitions may also need time to adapt.

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The breakdown of the financial results in 2007, 2006 and 2005 is as follows:

Millions of euros	12/31/07	12/31/06	12/31/05
Finance income			
Interest income	524	883	581
Dividends received	72	71	33
Other finance income	107	128	16
Total	703	1,082	630
 Finance costs			
Contractual interest expenses (IRR)	3,181	3,612	2,236
Less: amount capitalized			
Ineffective portion of cash flow hedges	43	(4)	
Ineffective portion of hedges of net investment in foreign operations			
Discount to present value of provisions and other liabilities	200	138	170
Changes in fair value of financial assets at fair value through profit and loss:	(25)	55	28
Held for trading	(27)	42	20
Voluntary designation	2	13	8
Changes in fair value of financial liabilities at fair value through profit and loss:	4	24	(52)
Held for trading	4	24	(52)
Voluntary designation			
Transfer from profit and loss from cash flow hedges	17	14	(44)
Transfer from equity to profit and loss from available-for-sale assets	107		
(Gain)/loss on fair value hedges	(75)	79	70
Loss/(gain) on adjustment to items hedged by fair value hedges	102	(41)	12
Total finance costs	3,554	3,877	2,420

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The breakdown of the Group's derivatives at December 31, 2007, their fair value at year-end and the expected maturity schedule is as follows:

Derivatives	Fair value 12/31/07	Millions of euros Notional value Maturity				Total
		2008	2009	2010	Subsequent years	
Interest rate hedges	(342)	118	1,033	(90)	1,009	2,070
Cash flow hedges	(278)	133	1,030	(72)	4,550	5,641
Fair value hedges	(64)	(15)	3	(18)	(3,541)	(3,571)
Exchange rate hedges	1,104	35	887	2,413	1,459	4,794
Cash flow hedges	1,168	414	887	2,413	1,459	5,173
Fair value hedges	(64)	(379)	0	0	0	(379)
Interest and exchange rate hedges	589	(123)	(217)	221	3,265	3,146
Cash flow hedges	382	481	0	224	3,307	4,012
Fair value hedges	207	(604)	(217)	(3)	(42)	(866)
Hedge of net investment in foreign operations	61	(1,876)	(943)	(550)	(1,396)	(4,765)
Derivatives not designated as hedges	(262)	551	(2,155)	(2,157)	3,459	(302)
Interest rate	(64)	(1,411)	(626)	(480)	2,358	(159)
Exchange rate	(270)	2,470	(1,296)	(1,539)	1,026	661
Interest and exchange rate	72	(508)	(233)	(138)	75	(804)
For hedges, the positive amount is in terms of fixed payment						

For exchange rate hedges, a positive amount means payment in functional vs. foreign currency.
A list of derivative products entered into at December 31, 2007 and 2006 is provided in Appendix III.

Table of Contents**(17) TAX MATTERS****Consolidated tax group**

Pursuant to a Ministerial Order dated December 27, 1989, since 1990 Telefónica, S.A. has filed consolidated tax returns for certain Group companies. In 2007, the consolidated tax group comprised 39 companies (43 in 2006).

Modification of tax rates

In several countries where the Telefónica Group operates, the tax authorities have passed legislation modifying income tax rates. In this respect, the tax rate in Spain was reduced from 35% to 32.5% in 2007 and to 30% from January 1, 2008. Similarly, in the UK the tax rate will decrease from 30% to 28% in 2008 and in Germany from 38.6% to 29.8%. The income tax rate in the Czech Republic will fall from 24% in 2007 to 21% in 2008, 20% in 2009 and 19% in 2010.

This amendment reduces the tax rate applicable to affected companies' profits, but also means less can be claimed back on tax losses carried forward from previous years on the accompanying consolidated balance sheet.

Based on estimates of taxable income and recovery of the deferred tax assets and liabilities recognized on the consolidated balance sheet, the Company quantified the impact of this change on the 2006 financial statements attributable to Spanish companies, recognizing a 355 million euro charge to Income tax expense, and a 14 million euro charge directly in equity. In addition, due to the changes in estimates made as a result of operations during the year indicated above, a tax revenue of 36 million euros was recognized in 2007 under Income tax expense.

Deferred income tax

The movements in deferred taxes in 2007 and 2006 are as follows:

	Millions of euros	
	Deferred tax assets	Deferred tax liabilities
Balance at December 31, 2006	8,701	4,700
Increases	762	339
Decreases	(1,345)	(462)
Changes to tax rates	(245)	(281)
Transfers	(28)	(56)
Net international movements		(122)
Company movements and others	(16)	(192)
Balance at December 31, 2007	7,829	3,926

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	Millions of euros	
	Deferred tax assets	Deferred tax liabilities
Balance at December 31, 2005	8,385	2,477
Increases	2,841	738
Decreases	(2,997)	(419)
Changes to tax rates	(450)	(81)
Transfers	4	(65)
Net international movements	(65)	(50)
Company movements and others	450	(88)
Tax effect O2 allocation	533	2,188
Balance at December 31, 2006	8,701	4,700

Tax credits for loss carryforwards

The tax loss carryforwards in Spain at December 31, 2007 at the main Group companies totaled 3,851 million euros (3,561 million euros for the Tax Group), of which 332 million and 3,229 million were incurred in 2003 and 2002, respectively. These can be utilised over a maximum of 15 years.

The balance sheet at December 31, 2007 includes a 481 million euro deferred tax asset corresponding to 1,567 million euros of tax loss carryforwards.

The 2002 income tax return included a negative adjustment for 2,137 million euros from Telefónica Móviles, S.A. (now Telefónica, S.A.). This arose through the transfer of certain holdings acquired in previous years where the fair value differed from the carrying amount (underlying book value) as a result of having implemented article 159 of the Spanish Corporation Law. However, as past rulings by the tax authorities differ from the interpretation being put forward by the Company, no adjustment has been made to the financial statements in this respect.

In relation to the sale by Terra Networks, S.A. (now Telefónica, S.A.) of its stake in Lycos Inc. in 2004, the Company has begun procedures to recognize a higher tax loss of up to 7,418 million euros because of measuring as acquisition value for tax purposes, the market value of Lycos Inc. shares received, rather than their carrying amount, in conformity with Article 159 of the Spanish Corporation Law. No accounting adjustments have been made until the Company receives a ruling on this procedure.

O2 Germany GMBH, the O2 Group's German subsidiary, has tax loss carryforwards amounting to 5,746 million euros, of which 396 million euros have been recognized as deferred tax in line with the prospects of generating future taxable earnings.

Unused tax credits recorded on the consolidated balance sheet at the Latin American subsidiaries at December 31, 2007 totaled 370 million euros, of which 217 million and 96 million euros corresponded to Brasilcel and the Argentine operators, respectively.

Table of Contents**Deductions**

In the consolidated balance sheet at December 31, 2007, the Group had capitalized 1,889 million euros of tax credits in connection with double tax deductions, export activity tax credits and a tax credit associated with the reinvestment of the capital gain.

Temporary differences

Temporary differences are generated as a result of the difference between tax bases of the assets and liabilities and their respective carrying amounts. Deductible temporary differences, tax deductions and credits and tax loss carryforwards give rise to deferred tax assets on the balance sheet, whereas taxable temporary differences in tax bases give rise to deferred tax liabilities. The sources of deferred tax assets and liabilities from temporary differences recorded at December 31, 2007 and 2006 are as follows:

	Millions of euros			
	2007		2006	
	Deferred tax assets	Deferred tax liabilities	Deferred tax assets	Deferred tax liabilities
Property, plant and equipment	862	380	629	469
Intangible assets	55	2,469	36	3,151
Personnel commitments	1,528	17	1,550	3
Provisions	635	2	758	180
Investments in subsidiaries, associates and joint ventures	1,221	196	957	393
Other	392	862	549	504
Total	4,693	3,926	4,479	4,700

Tax payables and tax receivables

Current tax payables and receivables at December 31, 2007 and 2006 are as follows:

	Millions of euros	
	Balance at 12/31/07	Balance at 12/31/06
Taxes payable:		
Tax withholdings	155	108
Indirect taxes payable	718	1,162
Social Security	184	202
Current income taxes payable	561	903
Other	539	466
Total	2,157	2,841

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	Millions of euros	
	Balance at 12/31/07	Balance at 12/31/06
Tax receivables:		
Indirect tax receivables	507	919
Current income taxes receivable	368	520
Other	135	115
Total	1,010	1,554

Reconciliation of book profit before tax to taxable income

The reconciliation of the book profit before tax to the taxable income for corporate income tax purposes and the determination of the corporate income tax expense for 2007, 2006 and 2005 is as follows.

	Millions of euros		
	2007	2006	2005
Book profit before tax	10,684	6,764	6,607
Tax expense at prevailing statutory rate	3,472	2,367	2,312
Effect of statutory rate in other countries	458	199	(71)
Variation in tax expense from new taxes	(22)	6	
Permanent differences	(1,893)	553	223
Changes in deferred tax charge due to changes in tax rate	(36)	355	2
Capitalization of tax deduction and tax relief	(200)	(1,375)	(138)
Use of loss carryforwards	(203)	(144)	(307)
Increase/(decrease) in tax expense arising from temporary differences	(8)	(46)	(54)
Consolidation adjustments	(3)	(133)	(58)
Adjustments to provision to return		(1)	(5)
Corporate income tax charge	1,565	1,781	1,904
Breakdown of current/deferred tax expense			
Current tax expense	2,152	3,116	2,610
Deferred tax expense	(587)	(1,335)	(706)
Total corporate income tax charge	1,565	1,781	1,904

Permanent differences arise mainly from events that produce taxable income not recognized in the consolidated income statement.

In 2007, the Company recognized a tax credit arising from the recognition of a higher tax loss carryforward amounting to 2,812 million euros generated on the disposal of the stake in Endemol Investment Holding, B.V. (see Note 2) as a difference between the tax and book value of the Endemol shares at the time of disposal. The positive impact recognized in Income tax expense in the consolidated income statement for the year amounted to 914 million euros, present in the table above under Permanent differences.

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Also included under Permanent differences is the accounting gain on this disposal, of 1,368 million euros, and the accounting gain on the disposal of Airwave for 1,296 million euros (see Note 2).

On September 25, 2002, tax inspections commenced at several companies included in Tax Group 24/90, of which Telefónica, S.A. is the parent company. The taxes inspected were corporate income tax (for the years from 1998 to 2000) and VAT, tax withholdings and prepayments relating to personal income tax, tax on investment income, property tax and non-resident income tax (1998 to 2001). The tax audits were concluded in 2005. The final outcome of the tax assessments is not expected give rise to significant additional liabilities on the Telefónica Group consolidated financial statements.

These assessments, which included settlement agreements and imposed fines on Telefónica, S.A. were signed by the company in disagreement in October 2004 and July 2005. The total amount of the assessments was 140 million euros. In April 2007, Telefónica, S.A. filed an administrative appeal before the National Court of Justice. The company also requested that the execution of the appealed settlements and penalties be suspended by providing the appropriate guarantees. On July 26, 2007 the lawsuit was formalized, with Telefónica, S.A. providing expert testimonies supporting its allegations. In December, the parties submitted the evidence on which their cases were based.

In addition, on June 17, 2006, a new inspection commenced. The taxes and years subject to review are corporate income tax for the years 2001 to 2004, VAT, tax withholdings and payments on account in respect of personal income tax, tax on investment income, property tax and non-resident income tax for 2002 to 2004. The inspections are not yet complete, but it is considered unlikely that the current actions of the tax authorities will give rise to significant additional liabilities.

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 audit 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 investment income, property tax, non-resident income tax and VAT; and the years since 2001 for corporate income tax (since 2001 and 2000, respectively, for the other Spanish companies).

In the other countries in which the Telefónica Group has a significant presence, the years open for inspection by the relevant authorities are generally as follows:

The last five years in Argentina, Brazil, Mexico, Colombia, Uruguay and the Netherlands.

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The last four years in Ecuador, Nicaragua, Peru and Venezuela.

The last three years in Chile, El Salvador, the US and Panama.

The last three years at the O2 Group. In addition, the period between March 2001 and March 2004 is open to inspection at O2 UK and O2 Third Generation.

The tax audit of the open years is not expected to give rise to additional significant liabilities for the Group.

(18) DISCONTINUED OPERATIONS

None of the Group's main operations were discontinued in 2007.

In 2006, Telefónica, Publicidad e Información, S.A.'s (TPI) operations were discontinued. The disposal of this investment (see Note 2) represented the Telefónica Group's exit from the directories business.

TPI's results in 2006 and 2005 until the effective date of its sale in 2006 are as follows:

Millions of euros	2006	2005
Operating income	270	654
Operating expense	(219)	(459)
Operating profit (loss)	51	195
Financial income (loss)	(4)	(5)
Profit before minority interests and tax	47	190
Corporate income tax	(14)	(66)
Profit for the year from a discontinued operation	33	124

Net cash flows in 2006 and 2005 until the effective date of its sale in 2006 are as follows:

Millions of euros	2006	2005
From operating activities	65	134
From/(used in) investing activities	(7)	(14)
From/(used in) financing activities	(141)	(124)
Foreign currency risk	(2)	3
Total increase/(decrease) in net cash	(85)	(1)

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The gain on the sale of this company was as follows:

	Millions of euros
Non-current assets	69
Current assets	286
Non-current liabilities	(78)
Current liabilities	(271)
Total	6
Sale price	1,838
Gain on disposal	1,832

The tax expense generated by the disposal of this company was 269 million euros.

Although TPI remained fully operational in 2005, its earnings results are presented under Profit after taxes from discontinued operations on the consolidated 2005 income statement for comparison purposes.

(19) REVENUE AND EXPENSES**Net sales and services:**

The breakdown of sales and services rendered is the following:

Millions of euros	2007	2006	2005
Services rendered	52,436	49,241	34,519
Net sales	4,005	3,660	2,864
Total revenue	56,441	52,901	37,383

Other income

The breakdown of this heading is as follows:

	Millions of euros		
	2007	2006	2005
Non-core and other current operating income	601	517	437
Internal expenditures capitalized	708	719	601
Government grants	57	47	75
Gain on disposal of assets	2,898	288	303
Total	4,264	1,571	1,416

Gain on the disposals of assets mainly include the gains on the sales during the year of the holdings in Airwave O2, Ltd. and Endemol Investment Holding, B.V. for 1,296 million and 1,368 million euros, respectively (see Note 2).

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Also included are gains on the disposal of properties in line with the Telefónica Group's real estate efficiency plan via the selective sale of properties, which amounted to 161, 100 and 66 million euros in 2007, 2006 and 2005, respectively.

The figure for 2006 includes the gain of 142 million euros obtained from Telefónica's acceptance of the takeover bid for Sogecable (see Note 13).

The figure for 2005 includes 80 million euros of proceeds from the sale of the 14.41% shareholding in US company Infonet Services Corporation, Inc. and 56 million euros from the offering of Endemol shares.

Other expenses

The breakdown of this heading in 2007, 2006 and 2005 is as follows:

Millions of euros	2007	2006	2005
Leases	938	900	489
Advertising	2,198	2,071	1,665
Other external services	6,854	6,259	4,503
Taxes other than income tax	974	905	781
Other operating expenses	303	220	228
Changes in trade provisions	666	609	471
Losses on disposal of non-current assets	148	131	75
Total	12,081	11,095	8,212

In 2007, 2006 and 2005, research and development costs recognized directly in profit and loss are not significant.

Estimated schedule

The estimated payment schedule for the next few years on operating leases and acquisition commitments is as follows:

31/12/2007	Total	Less than 1 year	1 to 3 Years	3 to 5 Years	Over 5 years
Operating leases	5,432	812	1,426	1,036	2,158
Purchase commitments	2,388	1,407	549	232	200

The main finance lease transactions are described in Note 22.

Table of Contents**Personnel expenses**

The breakdown of Personnel expenses is as follows:

	Millions of euros		
	2007	2006	2005
Wages, salaries and other personnel expenses	6,694	6,539	4,921
Personnel reorganization expenses	1,199	1,083	611
Total	7,893	7,622	5,532

Personnel reorganization expenses recorded by the Group include the costs of the Telefónica de España labor force reduction program of 361, 934 and 578 million euros in 2007, 2006 and 2005, respectively (see Note 15.a).

The heading also includes the impact of the various staff reduction plans undertaken in 2007 (see Note 15.a), which amounted to 838 million euros.

Number of employees

The table below presents the breakdown of the Telefónica Group's average number of employees in 2007, 2006 and 2005, together with total headcount at December 31 each year. The employees shown for each subgroup include the Telefónica Group companies with similar activities in accordance with its segment reporting.

	2007		2006		2005	
	Average	Year-end	Average	Year-end	Average	Year-end
Telefónica Spain	37,688	35,792	39,169	38,616	40,588	39,613
Telefónica Latin America	48,844	49,946	48,315	47,833	46,004	47,175
Telefónica Europe	29,249	29,305	26,248	27,844	9,888	10,531
Subsidiaries and other companies	128,271	133,444	111,744	118,703	95,675	107,380
Total	244,052	248,487	225,476	232,996	192,155	204,699
TPI Group			1,661		2,931	2,942
Total	244,052	248,487	227,137	232,996	195,086	207,641

The number of employees shown in the table above corresponds to the consolidated companies. It is worth highlighting the large number of employees at the various companies of the Atento Group performing contact center activities, whose average and year-end headcount for 2007 were 116,949 and 123,592, respectively.

Of the final headcount at December 31, 2007, approximately 47.6% are women.

Table of Contents**Employee benefits**

The Telefónica Group has arranged a defined contribution pension plan for its employees in Spain. Under this plan, the company makes contributions of 4.51% of the regular base salary (6.87% for employees of Telefónica de España, S.A.U. whose hiring date was prior to June 30, 1992). This is in addition to a 2.21% compulsory contribution by each participant. This plan is entirely externalized in outside funds.

At December 31, 2007, a total of 32,865 Group employees were covered by the pension plans managed by the subsidiary Fonditel Entidad Gestora de Fondos de Pensiones, S.A. (36,209 and 45,662 at December 31, 2006 and 2005, respectively). The contributions made by the various companies in 2007 amounted to 95 million euros (95 and 94 million euros in 2006 and 2005, respectively).

Furthermore, in 2006, the Group approved a Pension Plan for Senior Executives, wholly funded by the company, which complements the previous plan. This plan envisages annual defined contributions equivalent to specific percentages of the executives' fixed remuneration, in accordance with their professional category, and extraordinary contributions in accordance with the circumstances of each executive, payable in line with the conditions of said Plan.

No provision was made for this plan as it has been fully externalized.

With regard to investee Atento Brasil, a number of labor disputes are underway with the Brazilian Social Security Institute (INSS) and the Regional Labor Department. The claims amount to approximately 58 million euros. The company has obtained reports from external advisors confirming the reasonableness of the actions carried out in this respect.

Depreciation and amortization

The breakdown of Depreciation and amortization on the consolidated income statement is as follows:

Millions of euros	2007	2006	2005
Depreciation of property, plant and equipment	6,497	6,636	5,217
Amortization of intangible assets	2,939	3,068	1,476
Total	9,436	9,704	6,693

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Estimated amortization over the next five years of intangible assets on the consolidated balance sheet at December 31, 2007 is as follows:

Millions of euros	Total
2008	2,758
2009	2,497
2010	2,256
2011	1,690
2012	1,459

Net finance results

Note 16 provides a breakdown of the various components of financial results in 2007 and comparison with 2006 and 2005.

Earnings per share

Basic earnings per share amounts are calculated by dividing net profit for the year attributable to ordinary equity holders of the parent by the weighted average number of ordinary shares outstanding during the year.

Diluted earnings per share amounts are calculated by dividing net profit for the year attributable to ordinary equity holders of the parent (adjusted for any dilutive effects inherent in converting potential ordinary shares issued) by the weighted average number of ordinary shares outstanding during the year plus the weighted average number of ordinary shares that would be issued on the conversion of all the dilutive potential ordinary shares into ordinary shares.

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Both basic and diluted earnings per share attributable to equity holders of the parent are calculated based on the following data:

	2007	Millions of euros 2006	2005
Profit attributable to ordinary equity holders of the parent from continuing operations	8,906	4,650	4,375
Profit attributable to ordinary equity holders of the parent from discontinued operations		1,583	71
Total profit for calculating basic earnings per share attributable to equity holders of the parent	8,906	6,233	4,446
Adjustment for dilutive effects of the conversion of potential ordinary shares			
Total profit for the purposes of calculating diluted earnings per share attributable to equity holders of the parent	8,906	6,233	4,446
No. of shares	2007	Thousands 2006	2005
Weighted average number of ordinary shares (excluding treasury shares) for basic earnings per share	4,758,707	4,778,999	4,870,852
Dilutive effect of conversion of potential ordinary shares			
Endemol employee share option plans		421	833
Terra Lycos employee share option plans			22
Weighted average number of ordinary shares (excluding treasury shares) outstanding for diluted earnings per share	4,758,707	4,779,420	4,871,707

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The denominators used in the calculation of both basic and diluted earnings per share have been adjusted to reflect any transactions that changed the number of shares outstanding without a corresponding change in equity as if they had taken place at the start of the first period under consideration. Specifically, an adjustment was made for the distribution of part of the share premium via the delivery of shares (1-for-25) approved at the General Shareholders Meeting of May 31, 2005, which was carried out in June 2005.

There have been no transactions involving existing or potential ordinary shares between the end of the year and the date of preparation of the consolidated financial statements.

Basic and diluted earnings per share attributable to equity holders of the parent broken down by continuing and discontinued operations are as follows:

Figures in euros	Continuing operations			Discontinued operations			Total		
	2007	2006	2005	2007	2006	2005	2007	2006	2005
Basic earnings per share	1.872	0.973	0.898		0.331	0.015	1.872	1.304	0.913
Diluted earnings per share	1.872	0.973	0.898		0.331	0.015	1.872	1.304	0.913

(20) SHARE-BASED PAYMENT PLANS

In 2007 and 2006, the Telefónica Group maintained the following shared-based payment plans linked to the share price of Telefónica, S.A. or one of its subsidiaries.

a) Telefónica, S.A. share plan: Performance Share Plan

At the General Shareholders Meeting of Telefónica, S.A. on June 21, 2006, its shareholders approved the introduction of a long-term incentive plan for managers and senior executives of Telefónica, S.A. and other Telefónica Group companies. Under this plan, selected participants who met the qualifying requirements were given a certain number of Telefónica, S.A. shares as a form of variable compensation.

The Plan is initially intended to last seven years. It is divided into five phases, each three years long, beginning on July 1 (the Start Date) and ending on June 30 three years later (the End Date). At the start of each phase the number of shares to be awarded to Plan beneficiaries is determined based on their success in meeting targets set. The shares are delivered, assuming targets are met, at the End Date of each phase. Each phase is independent from the others. The first started on July 1, 2006 (with shares to be delivered, if targets are met, from July 1, 2009) and the fifth phase begins on July 1, 2010 (with any shares earned delivered from July 1, 2013).

Award of the shares is subject to a number of conditions:

The beneficiary must continue to work for the company throughout the three years of the phase, subject to certain special conditions related to departures.

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The actual number of shares awarded at the end of each phase will depend on success in meeting targets and the maximum number of shares assigned to each executive. Success is measured by comparing the total shareholder return (TSR), which includes both share price and dividends offered by Telefónica shares, with the TSRs offered by a basket of listed telecoms companies that comprise the comparison group. Each employee who is a member of the plan is assigned at the start of each phase a maximum number of shares. The actual number of shares awarded at the end of the phase is calculated by multiplying this maximum number by a percentage reflecting their success at the date in question. This will be 100% if the TSR of Telefónica is equal to or better than that of the third quartile of the Comparison Group and 30% if Telefónica's TSR is in line with the average. The percentage rises linearly for all points between these two benchmarks. If the TSR is below average no shares are awarded.

The maximum number of the shares issuable in each of the two outstanding phases at December 31, 2007 is as follows:

	No. of shares	Unit value	End date
1st phase July 1, 2006	6,530,615	6.43	June 30, 2009
2nd phase July 1, 2007	5,556,234	7.70	June 30, 2010

This plan is equity-settled via the delivery of shares to the participants. Accordingly, a balancing entry for the 23 and 8 million euro of employee benefits expenses recorded in 2007 was made in equity.

To ensure the Company has enough shares to meet its obligations at the end of the phase commenced in 2006, Telefónica purchased an instrument from a financial institution that will deliver to Telefónica, at the end of the phase, a number of shares determined using the same measure of success as the plan, i.e. an instrument that mirrors the features of the plan. The cost of this instrument was 46 million euros, which in unit terms is 6.43 euros for every maximum number of shares (see Note 16).

b) Telefónica, S.A. share option plan targeted at employees of O2: (O2 Performance Cash Plan)

In addition to the Performance Share Plan, another plan called the Performance Cash Plan, operating under the same conditions as the Performance Share Plan is targeted at employees of the O2 Group. This plan entails delivery to O2 executives of a specific number of theoretical options in Telefónica, S.A. which, in the event, would be cash-settled at the end of each phase via a payment equivalent to the market value of the shares on settlement date up to a maximum of three times the notional value of the values at the delivery date.

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The value of the theoretical options is established as the average share price in the 30 days immediately prior to the start of each phase, except for the first phase, where the average share price during the 30 days immediately prior to May 11, 2006 (12.83 euros) was taken as the reference.

The estimated duration of this plan is also 7 years, with 5 phases, each of three years, commencing on July 1 of each year, starting in 2006.

Like the Telefónica, S.A. Performance Share Plan, the performance rate for setting payments is measured based on the TSR on Telefónica shares with respect to the comparison group's TSRs, in line with the following criteria:

Below average	0%
Average	30%
Equal to or higher than the third quartile	100%

The number of options assigned to the two phases outstanding at December 31, 2007 is 794,473 and 632,027, respectively.

The fair value of the options delivered in the second phase at December 31, 2007 was 13.33 euros per option. The fair value of the options delivered in the first phase at that date was 18.89 euros per option (16.86 euros at December 31, 2006). This value is calculated by taking the Telefónica share price and including the estimated TSR and is updated at each year end.

c) Terra Networks, S.A. (now Telefónica, S.A.) share option plan

The Terra Networks, S.A. share option plan was approved at the Shareholders' 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 share options by their holders, for the ownership by the employees and executives of the Terra-Lycos Group companies of a portion of the capital of Terra Networks, S.A. up to a maximum of 14,000,000 shares of Terra Networks, S.A.

As a result of the Telefónica, S.A. and Terra Networks S.A. merger approved at the General Shareholders' meeting held on May 31, 2005 and recorded in the Madrid Mercantile Register on July 16, 2005, Telefónica, S.A. took over responsibility for Terra Networks S.A.'s outstanding share option plans.

Consequently, the options on Terra Networks, S.A. shares were automatically translated into options on Telefónica, S.A. shares at the exchange ratio used in the merger.

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The main features of the plan are as follows:

1. Each option entitles the holder (employee or executive) to acquire one share of Terra Networks, S.A. (now shares in Telefónica, S.A.) at an exercise price established at the time the options are granted.
2. The options are exercisable for four to six years following the grant date.
3. The exercise of the options is contingent upon the beneficiary remaining an employee of the Terra-Lycos Group (now the Telefónica Group).
4. At the exercise date, the options may be either equity-settled in Terra Networks, S.A. (now Telefónica, S.A.) shares, once the beneficiary has paid the option exercise price, or net cash-settled.

At December 31, 2007 all options outstanding were cancelled.

The movement in 2007, 2006 and 2005 is as follows:

	Number of options	Average exercise price (euros)
Options outstanding at December 31, 2004 (on Terra shares)	2,383,820	14.21
Equivalent outstanding options at December 31, 2004 (on Telefónica shares)	529,738	63.95
Options granted	33,276	27.50
Options expired/cancelled	(445,114)	70.67
Options outstanding at December 31, 2005	117,900	28.28
Options granted	13,278	22.70
Options expired/cancelled	(78,067)	31.12
Options outstanding at December 31, 2006	53,111	22.70
Options expired/cancelled	(53,111)	22.70
Options outstanding at December 31, 2007		

Table of Contents**d) Share option plan of Terra Networks, S.A. (now of Telefónica, S.A.) resulting from the assumption of Lycos, Inc. s share option plan**

Under the agreements entered into for the acquisition of Lycos, Inc., 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, a resolution was passed at the Shareholders Meeting of Terra Networks, S.A. to take over Lycos, Inc. s share option plan.

At the time of the sale of all the shares in Lycos, Inc in 2004, it was agreed that Terra Networks, S.A. would remain responsible for the obligations arising from share options on Terra Networks, S.A. shares to beneficiaries of Lycos, Inc. although Lycos, Inc. could carry out, on behalf of and at the expense of Terra Networks, S.A. whatever actions were necessary or advisable in relation to the exercise of the options by the beneficiaries.

After the merger of Terra Networks, S.A. into Telefónica, S.A., these options became options on Telefónica, S.A. shares.

At December 31, 2007, employees of Lycos, Inc. had outstanding options on 93,269 shares, at a post-merger weighted average price of 68.18 US dollars.

The movement in 2007, 2006 and 2005 is as follows:

	Number of options	Average exercise price (USD)	Average share price (USD)
Options outstanding at December 31, 2004 (on Terra shares)	10,863,239	20.39	
Equivalent outstanding options at December 31, 2004 (on Telefónica shares)	2,414,053	91.76	
Options exercised	(161,982)	17.47	20.39
Options expired/cancelled	(1,724,646)	108.58	
Options outstanding at December 31, 2005	527,425	59.57	
Options exercised	(124,974)	14.37	15.68
Options expired/cancelled	(287,204)	76.15	
Options outstanding at December 31, 2006	115,247	67.26	
Options expired/cancelled	(21,978)	63.38	
Options outstanding at December 31, 2007	93,269	68.18	

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The breakdown of options outstanding at December 31, 2007 is as follows:

Range of exercise prices (USD)	Number of options outstanding	Average exercise price (USD)	Average remaining exercise period (years)
54,90 68,90	72,682	58.25	2.30
74,65 136,13	20,587	103.22	1.74
Options outstanding at December 31, 2007	93,269	68.18	2.17

e) Telefónica, S.A. share option plan aimed at employees of Endemol (EN-SOP Program).

In order to fulfill the commitments assumed by Telefónica, S.A. in the acquisition of the Dutch company Endemol and 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. share option plan targeted at the employees of Endemol Entertainment N.V. and its subsidiaries, known as the EN-SOP Program.

This program consisted of granting to the beneficiaries (all the Endemol Group's permanent employees on January 1, 2001, who are not participating in another similar share or share option plan), effective January 1, 2001, 2002, 2003 and 2004, of a certain number of purchase options on Telefónica, S.A. shares. The exercise period of the options is four years from the grant date, and the options may be exercised at a rate of one-half per year, three and four years after the related grant date.

The option exercise price was the related annual reference value set on each grant date, and the exercise terms are 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 is interrupted prior to the exercise of the options.

The options could be settled through the acquisition by the beneficiary of the underlying shares or, alternatively, through a net-equity or cash settlement.

The disposal of the holding in Endemol by Telefónica in 2007 led to the cancellation and settlement of the plan. It was no longer in effect at December 31, 2007.

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The movement in 2007, 2006 and 2005 is as follows:

	Number of options	Average exercise price (euros)	Average share price (euros)
Options outstanding at December 31, 2004	6,682,799	11.54	
Options exercised	(492,277)	11.88	13.82
Options expired/cancelled	(1,280,688)	14.29	
Options outstanding at December 31, 2005	4,909,834	10.78	
Options exercised	(1,824,754)	10.34	12.72
Options expired/cancelled	(336,326)	10.81	
Options outstanding at December 31, 2006	2,748,754	11.07	
Options exercised	(1,734,755)	10.39	16.39
Options expired/cancelled	(1,013,999)	12.24	
Options outstanding at December 31, 2007			

Of all the options exercised in 2007, 4,750 were equity-settled (3,050 and 1,525 options in 2006 and 2005, respectively) (see Note 12) and the remainder cash-settled for an amount of 10 million euros (4.86 and 1.02 million euros in 2006 and 2005, respectively).

(21) OTHER INFORMATION***a) Litigation***

Telefónica and its group companies are party to several lawsuits which are currently in progress in the law courts and administrative and arbitration bodies of the various countries in which the Telefónica Group is present.

It is reasonable to assume that this litigation will not materially affect the financial position or solvency of Telefónica Group, regardless of the outcome. The Company also has the support of reports by its legal counsel. We highlight the following unresolved cases:

1. Procedures deriving from bankruptcy proceeding of Sistemas e Instalaciones de Telecomunicación, S.A.U. (Sintel).

Sintel, a former subsidiary of Telefónica was declared bankrupt in 2001. As a result of the voluntary bankruptcy proceeding heard by Madrid Court of First Instance no. 42 (case 417/2001), two criminal proceedings commenced which affect Telefónica.

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In the first proceeding (Abbreviated proceeding no. 273/2001) being heard by Central Examining Court No. 1, on September 24, 2002, Telefónica and Telefónica de España, S.A.U. filed a civil suit for damages against the directors of Sintel and of Mastec Internacional, S.A.

The second proceeding (Preliminary proceeding No. 362/2002), being heard by Central Examining Court no. 1, was for a possible offence of extortion. This proceeding was subsequently assimilated to the preliminary proceedings in case No. 273/2001 above.

The two proceedings were combined in April 2004. The motion filed by counsel for Telefónica to have the case dismissed was rejected and it was ruled that the preliminary proceedings should continue. Nonetheless, to date no liability has been established against Telefónica and the plaintiffs claim in this regard has been explicitly dismissed.

In its ruling of December 12, 2007, Examining Court No. 1 changed into an Abbreviated proceeding the suit for bankruptcy due to criminal negligence and crimes against the Spanish Treasury, charging those that could be responsible, all managers and directors of Sintel, S.A., long after the sale of the company by Telefónica.

2. Contentious proceedings in connection with the takeover bid for Terra Networks, S.A. and its subsequent merger with Telefónica

Proceedings derived from the takeover bid

2.1. On May 29, 2003, certain Terra Networks, S.A. shareholders filed two class actions with the Supreme Court of New York State against Telefónica, Terra Networks, S.A. and certain directors of Terra Networks, S.A.

The actions alleged mainly that the takeover bid by Telefónica was the result of non-compliance with the fiduciary commitments of this company, and of the Board of Directors of Terra Networks, S.A. Since the actions were brought, both have remained inactive.

2.2. The World Association of Shareholders of Terra Networks, S.A. (ACCTER) filed an appeal for judicial review at the National Appellate Court -Telefónica appears as an intervening non-party- against the ruling of June 19, 2003 by the Spanish National Securities Market Commission (CNMV) authorizing the takeover offer by Telefónica for Terra Networks, S.A.

The appeal was rejected by the National Appellate Court via ruling issued January 27, 2006, against which ACCTER filed an administrative appeal. The Third Section of the Supreme Court has yet to rule on the admissibility of this appeal.

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Proceedings derived from the merger

- 2.3.** On June 30, 2005, ACCTER and its President, on his own account, filed a complaint contesting the merger resolution adopted at the Shareholders Meeting of Terra Networks, S.A. of June 2, 2005.

The Court of First Instance rejected the claim and the plaintiffs filed an appeal which has yet to be resolved.

- 2.4.** On September 26, 2006, Telefónica and one of its directors were notified of the claim filed by former shareholders of Terra Networks, S.A. (Campoaguas, S.L., Panabeni, S.L. and others) alleging breach of contract by Telefónica with the shareholders of Terra in respect of the terms and conditions set forth in the Prospectus of the Initial Public Offering of shares of Terra Networks, S.A. The court date has been set for July 19, 2008.

3. Claim at the ICSID

As a result of the enactment by the Argentine government of Public Emergency and Exchange Rules Reform Law 25,561 of January 6, 2002, Telefónica considered that the terms and conditions of the Share Transfer Agreement approved by Decree 2332/90 and the Pricing Agreement ratified by Decree 2585/91, both of which were executed by the Company with the Argentine government, were affected appreciably, since the Law rendered ineffective any dollar or other foreign currency adjustment clauses, or indexation clauses based on price indexes of other countries, or any other indexation mechanism in contracts with the public authorities. The law also required that prices and rates derived from such clauses be denominated in pesos at an exchange rate of one peso (ARS 1) to one US dollar (USD1).

Accordingly, since negotiations with the Argentine Government were unsuccessful, on May 14, 2003, Telefónica filed a request for arbitration with the International Center for Settlement of Investment Disputes (ICSID) pursuant to the Agreement for the Promotion and Reciprocal Protection of Investments between the Argentine Republic and the Kingdom of Spain. On July 6, 2004, the first hearing at the ICSID took place in Washington and a 90-day stay was ordered in an attempt to reach a settlement. Following the expiration of the stay without any settlement having been achieved, on December 6, 2004, Telefónica filed the memorial or claim with the ICSID together with the initial supporting testimonies. The Court is currently considering a plea filed by the Argentine government alleging that the matter is outside the jurisdiction of the arbitration court.

On February 15, 2006, Telefónica Argentina signed a memorandum of understanding with the Argentine government as a prerequisite to reaching an agreement to renegotiate the transfer contract approved by Royal Decree-Law 2332/90 pursuant to the provisions of Article 9° of Law 25,561.

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Among other issues, this memorandum of understanding envisaged the suspension by Telefónica de Argentina and Telefónica for a period of 210 working days, of proceedings for all claims, appeals and demands planned or underway, with the administrative, arbitrational or legal courts of Argentina or abroad, which were based on events or measures taken as a result of the emergency situation established by Law N° 25,561 with regard the Transfer Agreement and the license granted to the Company. The suspension came into force on October 6, 2006.

This preliminary agreement could put an end to the litigation.

As the initial stay expired, Telefónica requested a six-month extension starting October 5, 2007 which the Argentina government did not oppose. The courts agreed to extend the stay.

4. Appeal for judicial review of the Spanish Competition Court (TDC) ruling of April 1, 2004.

On April 1, 2004, the TDC ruled that Telefónica de España, S.A.U. had engaged in unfair trade practices prohibited under Article 6 of Antitrust Law 16/1989, dated July 17, and Article 82 of the EC Treaty, consisting of the abuse of a dominant market position, by conditioning the provision of certain services to the non-existence of predialling arrangements with rival operators and running disloyal advertising campaigns. It imposed a fine of de 57 million euros.

Telefónica de España, S.A.U. filed an appeal for judicial review of this decision.

On January 31, 2007, the National Appellate Court ruled in favor of the appeal, thereby overturning the TDC's ruling. The State attorney filed an appeal to overturn the Supreme Court ruling in which Telefónica appeared.

5. Cancellation of the UMTS license granted to Quam GMBH in Germany.

In December 2004, the German Regulatory Authority for Telecommunications and Post (RegTP) revoked the UMTS license granted to Quam GMBH in 2000. After obtaining a suspension of the revocation order, on January 16, 2006, Quam filed a suit against the order with the German courts. There were two main parts to this claim: the first seeking to uphold the suspension of the license revocation order issued by the RegTP, and the second, in the event the first did not prosper, seeking the total or partial repayment of the original amount paid for the license.

Towards the end of February 2007, Quam filed allegations, and the public hearing was scheduled for April 25, 2007. At the hearing, the court issued a ruling rejecting Quam's claim. This rule has been appealed.

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6 Appeal against the European Commission ruling of July 4, 2007 against Telefónica de España, S.A.U. s broadband pricing policy.

On February 22, 2006, Telefónica was sent a statement of objections, initiating disciplinary proceedings for conduct that goes against Article 82 of EC Treaty rules. Subsequently, on July 9, 2007, the European Commission issued a decision, imposing a 152 million euro fine on Telefónica and Telefonica de España S.A.U. The ruling charged Telefónica with applying a margin squeeze between the prices it charged competitors to provide regional and national wholesale broadband services and its retail broadband prices using ADSL technology from September 2001 to December 2006. Telefónica de España, S.A.U. and Telefónica both filed appeals to overturn the decision before the Court of First Instance of the European Communities. The Kingdom of Spain also lodged an appeal to overturn the decision.

7 Proceedings by Agência Nacional de Telecomunicações (ANATEL) against various companies from the Brasilcel, N.V. Group (Telerj Celular, S.A., Telems Celular, S.A., Tele Centro Oeste Celular Participações, S.A., and others) regarding the inclusion of interconnection revenues and revenues from network usage by operators in the Fundo de Universalização de Serviços de Telecomunicações (FUST).

The Brasilcel, N.V. (VIVO) Group operators appealed ANATEL s decision modifying the basis for calculating amounts payable into the Fund for Universal Access to Telecommunications Services (FUST for its initials in Portuguese), a fund to pay for telecommunications services providers obligations to provide universal service (wireline and wireless). The FUST s income consists of 1% of the operators gross operating revenues.

According to ANATEL criteria, revenues obtained from transfers received by other operators (interconnection and network usage) should be included in FUST s taxable income, with no deduction of interconnection expenses from the tax base.

The operators of Brasilcel, N.V., together with other wireless operators, requested a stay of execution in order to be able to continue calculating the FUST calculation basis exclusive of said revenues. Their petition was rejected on January 24, 2006. However, on March 13, 2006, the plaintiffs were granted an injunction allowing that revenues from transfers received by other operators be excluded from the base for calculating the FUST s taxable income.

In addition, at the same time Telecomunicações de São Paulo, S.A. Telesp and Telefónica Empresas S.A., together with other wireline operators through ABRAFIX (Associação Brasileira de Concessionárias de Serviço Telefonico Fixo Comutado), requested an injunction that would allow them to continue including these revenues and deducting expenses from FUST s taxable income. The request was rejected on January 9, 2006. On April 17, 2006 an injunction was granted, allowing ANATEL s decision to modify the revenues included in taxable income for the FUST s calculation to not have any retroactive effect.

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- 8 Appeal for judicial review against the ruling of the Central Economic-Administrative Tribunal dated February 15, 2007 rejecting several economic-administrative claims filed by Telefónica against assessments from the National Inspection Office of the Spanish Treasury related to consolidated taxes in 1998, 1999 and 2000.**

See Note 17 for unresolved proceedings regarding corporate income tax.

- 9 Proceeding before Prague District Court no. 3 initiated by Telefónica O2 Czech Republic, a.s. against the ruling of the Czech Telecommunications Office dated December 22, 2003 (Reference n° 27865/2003-603/IV).**

On December 22, 2003, the Czech Telecommunications Office issued a ruling that required Cesky Telecom, a.s. (now Telefónica O2 Czech Republic, a.s.) to pay T-mobile Czech Republic, a.s. (T-mobile) 898,606,196 Czech crowns in interconnection fees (call termination) for the period from January to November 2001.

At the petition of Telefónica O2 Czech Republic, a.s., the court granted a stay of execution on the Czech Telecommunications Office's ruling during the judicial procedure.

On October 27, 2006, the District Court of Prague issued a ruling rejecting Telefónica O2 Czech Republic's action, considering that the decision corresponded to an administrative proceeding. This ruling was appealed and upheld by the Appellate Court, bringing the civil proceeding to an end.

As a result, Telefónica O2 Czech Republic, a.s. filed a new suit before the administrative courts requesting that the execution of the Czech Telecommunications Office's ruling be suspended. The procedure arising from this suit is still pending.

Although this administrative procedure had yet to be resolved, in 2007 T-mobile asked Prague District Court 3 to execute the ruling of December 23, 2003 entailing an amount of 1,859,277,925.29 Czech crowns (in principal and interest). The court accepted the petition and on May 23, 2007 issued a ruling to initiate the execution against any asset of Telefónica O2 Czech Republic, a.s. pursuant to a request by Telefónica O2 Czech Republic, s.a., this execution has been suspended until a final ruling by the Courts on the case is handed down.

Recently, Telefónica O2 Czech Republic, a.s. requested that the execution ordered by Prague District Court 3 be ruled inadmissible. No ruling has been made.

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10 Suit filed by the Treasury of Sao Paulo (Brazil) against Telecomunicações de São Paulo, S.A. -Telesp.

Three lawsuits were filed by the State Treasury of Sao Paulo against Telecomunicações de São Paulo, S.A. Telesp (Telesp) in relation to the Merchandise Circulation Tax (ICMS) -similar to the VAT levied on telecommunications services- applicable to revenue from international calls during different periods between 1996 and 1999. The amount claimed is approximately 168 million euros.

Two of the administrative procedure concluded with an unfavourable ruling for Telesp. The company filed the related appeals, but no judicial rulings have been issued as of yet. No administrative ruling has been issued on the third.

In accordance with applicable legislation and the services provided by Telesp in this period (which did not include international carrier services, as these were provided by another operator at the time), the company considers that it is not liable for the tax claimed by the Brazilian tax authorities.

b) Commitments

Agreements with Portugal Telecom (Brazil)

On January 23, 2001, Telefónica, S.A. and its now defunct subsidiary Telefónica Móviles, S.A., and Portugal Telecom S.G.P.S., S.A. and its subsidiary PT Móveis, S.G.P.S., S.A., agreed to group together all their wireless telephony businesses in Brazil. They therefore undertook to contribute all their wireless telephony assets in Brazil to a joint venture, which, subject to the necessary regulatory authorizations, would be a subsidiary of the two groups, and in which they would each have a 50% ownership interest. In addition, under the terms of this agreement, the two parties expressed their interest in increasing their reciprocal ownership interests, subject to compliance with the applicable regulations and bylaws.

On October 17, 2002, Telefónica Móviles, S.A. and Portugal Telecom, S.G.P.S., S.A. and its subsidiary PT Móveis, S.G.P.S., S.A. entered into the definitive agreements (Shareholders 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.

On July 29, 2006, the merger of Telefónica Móviles, S.A. into Telefónica, S.A. was filed with the Mercantile Register. As a result of this merger and the dissolution of Telefónica Móviles, S.A., Telefónica, S.A. retained all the rights and obligations of Telefónica Móviles, S.A. including those arising from the agreements signed with Portugal Telecom, S.G.P.S., S.A. and its subsidiary PT Móveis, S.G.P.S., S.A.

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In accordance with the aforementioned definitive agreements, Telefónica, 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 ownership of either of the parties falls below 40% during an uninterrupted period of six months. In this event, Brasilcel N.V.'s governing bodies would deliberate with a simple majority. As for the quorum required to hold the Shareholders' Meeting, attendance by shareholders representing the majority of share capital would suffice.

As for the Portugal Telecom Group's right to sell its shares in Brasilcel N.V. to Telefónica, S.A. if its equity interest were diluted to below 40% during a period of six months, this put option expired on December 31, 2007.

Also, in accordance with the definitive agreements, the Portugal Telecom Group will be entitled to sell to Telefónica, 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., or at any other subsidiary of the latter that held a direct or indirect ownership interest in Brasilcel N.V. Similarly, Telefónica, S.A. will be entitled to sell to the Portugal Telecom Group, which will be obliged to buy, its holding in Brasilcel, N.V. if there is a change of control at Portugal Telecom, S.G.P.S., S.A., at PT Móveis, S.G.P.S., S.A. or at 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 put option, in cash or in shares of the wireless telephony operators contributed by the related party, making up the difference, if any, in cash.

Medi Telecom (Morocco)

On June 15, 2006, Telefónica Móviles España, S.A.U., as shareholder of Medi Telecom, signed a new Shareholders Support Agreement together with PT Móveis Serviços de Telecomunicações, S.G.P.S., SAL, HOLDCO, FINANCE.COM and RMA WATANYA (the last two form part of the BMCE Group) replacing the previous agreement dated October 12, 2000. This commitment requires the signatories, in line with their stake in the share capital of Medi Telecom, to provide the latter with up to 260 million euros of financial assistance in the event of non-compliance with financial covenants or a shortfall in funds at Medi Telecom that would prevent it from meeting its debt servicing obligations. If Medi Telecom attains certain levels of operating earnings before amortization and depreciation during four consecutive quarters, and at the latest on the date of full repayment of its debt (i.e. 2012), this financial commitment will be automatically cancelled.

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As a result of the loans and capital increases subscribed by, inter alia, Telefónica Móviles España, S.A.U., during 2003, the aforementioned commitment between the latter, PT Moveis-Serviços de Telecomunicações, SGPS, SAL and the BMCE group was reduced to 168 million euros at December 31, 2006, broken down as follows:

Telefónica Móviles España, S.A.U.: 54 million euros

PT Movéis Serviços de Telecomunicações, S.G.P.S., S.A.L: 54 million euros

RMA WATANYA: 22 million euros

FINANCE.COM: 8 million euros

HOLDCO: 30 million euros

Guarantees provided for Ipse 2000 (Italy)

The Telefónica Group has provided guarantees for the Italian company Ipse 2000 S.p.A. (holder of a UMTS license in Italy) in which it owns an indirect stake through Telefónica Móviles, S.A.U. and Solivella B.V. for the 365 million euros payable to the Italian government in connection with the grant of the license.

Telefónica, S.A. (together with the other strategic partners of Ipse 2000, S.p.A) arranged a counterguarantee for a bank which, in turn, issued a bank guarantee for the Italian authorities as security for the deferred payment of the UMTS license.

In the wake of the decision by the Italian government to revoke the UMTS license granted to Ipse, the Company considered that, with the contractual conditions governing payment of the license having changed, Ipse was no longer obliged to pay the remaining amount and, accordingly, the principal obligation no longer existing, the bank guarantee and the partners' counterguarantee (cash collateral) had become extinct. Consequently, the Company has lodged an appeal against the government to keep the guarantee from being executed and to return the cash collateral to the shareholders in their respective investments.

In defense of its interests, the Company was obliged to file a number of claims:

Requesting the cancellation of the revocation order.

Requesting reimbursement of said cash collateral to the Company's shareholders.

Requesting acceptance by the Italian government of the return by Ipse 2000 of a further 5Mhz of spectrum granted to it following the award of the UMTS license, and requesting an 826 million euros reduction in payments owed (corresponding to the 5Mhz of spectrum).

Requesting cancellation of the amounts pending payment deriving from the award of the UMTS license, based on the new regulatory framework, which establishes a maximum annual price per 5Mhz lower than that set in the license awarded to Ipse 2000 SpA. This could imply a reduction with respect to the initial amount of some 1,200 and 2,300 million euros.

Requesting cancellation of the allocation by the Italian government of GSM frequencies free of charge.

The proceedings are at different hearings (civil court in Rome, appeal before the state council, administrative court of Lazio) and a ruling is expected to be issued during the course of 2008.

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In line with the above, in November 2007 and 2006, Ipse had to make its annual license payment; however, it asked for an injunction to enable it to defer any payment until after a decision had been made. At December 31, 2007, the amount outstanding for this concept was 602 million euros.

Commitments relating to audiovisual content (Telefónica de Contenidos)

At December 31, 2007, Telefónica de Contenidos had the following commitments relating to sports broadcasting rights:

1. In December 2004, Canal Satélite Digital, S.A. gave its approval to allow Telefónica de Contenidos to broadcast on a non-exclusive basis under the pay-per-view (PPV) system the signal for the soccer games of the First and Second Divisions of the Spanish National Soccer League and of the King's Cup (Copa de S.M. El Rey) (except for the final) produced by Audiovisual Sport, from January 1, 2005. The rights were acquired at prevailing market prices for this type of content and for a period that will depend on the soccer seasons for which the content provider is able to renew its current agreements with the soccer clubs.
2. Likewise in December 2004, an agreement was entered into with Audiovisual Sport for the provision of the broadcast signal to Telefónica de Contenidos and/or the Telefónica Group companies to which Telefónica de Contenidos assigns the signal, for the soccer games specified in the agreement with Canal Satélite Digital, at market prices for this type of content for each match, with guaranteed minimum payments per season to Audiovisual Sport from January 1, 2005, and for a period that will depend on the soccer seasons for which the content provider is able to renew its agreements with the soccer clubs.

Telefónica Internacional, S.A.U. as strategic partner of Colombia Telecomunicaciones S.A. ESP

Following the selection on April 7, 2006 of the bid presented by Telefónica Internacional, S.A.U. to become the strategic partner of Colombia Telecomunicaciones S.A. ESP, on April 18, 2006 Telefónica Internacional, S.A.U., the Colombian government and Colombia Telecomunicaciones S.A. ESP signed a framework investment agreement (the Framework Agreement) establishing, inter alia, the following commitments on the part of Telefónica Internacional, S.A.U. Compliance with these commitments is guaranteed by Telefónica Internacional, S.A.U. via a pledge contract on the shares which Telefónica Internacional, S.A.U. holds in Colombia Telecomunicaciones S.A. ESP, signed on May 2, 2006.

Telefónica Internacional, S.A.U. undertakes not to sell, transfer, pledge, hand over the use of, or in any other manner encumber or dispose of its shares in Colombia Telecomunicaciones S.A. ESP during the first five years of the agreement (until April 28, 2011).

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Since April 28, 2006, the shareholders of Colombia Telecomunicaciones S.A. ESP may offer, at any time and in a single package, all the shares they hold at that time in Colombia Telecomunicaciones S.A. ESP to Telefónica Internacional, S.A.U., who shall be obliged to acquire them, either directly or via one of its subsidiaries. The sale/purchase price of each share will be determined based on the valuation of each share offered in sale by an independent investment banker designated by agreement between the two parties.

Telefónica Internacional, S.A.U. undertakes, during the duration of the Framework Agreement, to not perform, either directly or indirectly (via subsidiaries), within the territory of the Republic of Colombia, the sale, distribution, marketing, agency or intermediation of (i) data transmission services (including clear channel, frame relay, IP and ATM) via the different existing transmission technologies, (ii) IT application hosting services, (iii) data center services, (iv) private telecommunications network operation services and/or (v) total IT systems operations, which are competitive with those provided or marketed by Colombia Telecomunicaciones S.A. ESP, via companies whose revenues derive mainly from the provision of this kind of services or operations. Exempt from the aforementioned commitment are providers of wireless telephony services (TMC and PCS).

If, during the life of the Framework Agreement, Telefónica Internacional, S.A.U. acquires shareholdings which enable it to gain control of companies located in the Republic of Colombia operating in the activities set forth in the above paragraph, Telefónica Internacional, S.A.U. undertakes to present to the Shareholders Meeting of Colombia Telecomunicaciones S.A. ESP, and its shareholders undertake to vote in favor of (i) the merger of said companies into Colombia Telecomunicaciones S.A. ESP or (ii) to issue shares without preference rights in exchange for delivery of the assets of said companies to Colombia Telecomunicaciones S.A. ESP. The above undertaking shall not apply in the event that the proposed transaction results in a reduction in the shareholding of the Colombian government in Colombia Telecomunicaciones S.A. ESP to less than twenty percent (20%).

In the event that the option presented by Telefónica Internacional, S.A.U. is not ratified by the shareholders of Colombia Telecomunicaciones S.A. ESP, Telefónica Internacional, S.A.U. shall be free to perform said activities via the company whose control it has acquired directly or indirectly.

Other commitments in the form of performance bonds for concessions or licenses

Telefónica Móviles España, S.A.U., a subsidiary of Telefónica Móviles, S.A. (merged into Telefónica, S.A. in July 2006), provided certain financial guarantees to the Spanish State amounting to 1,100 million euros in relation to the UMTS license in Spain granted to Telefónica Móviles España, S.A.U. These guarantees ensure fulfillment of the commitments assumed by the company awarded the license in relation to network roll-out, job creation, investments, etc.

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Telefónica Móviles España, S.A.U. initiated negotiations with the Ministry of Science and Technology with a view to changing the existing system of guarantees. This process was completed through an Official Notice issued by the Secretary of State for Telecommunications and for the Information Society on July 28, 2003, as a result of which the 71 guarantees in force at that date amounting to 631 million euros that were securing the commitments assumed under the UMTS license were returned to Telefónica Móviles España, S.A.U., after the latter had arranged, in the same month, a guarantee of 168 million euros with the Government Depositary, to secure compliance with the UMTS service commitments prior to launch of the UMTS and the commitments of the first year from the date of commercial launch, in accordance with the new system of guarantees. In September 2003, Telefónica Móviles España, S.A.U. cancelled the returned guarantees at the respective banks.

On June 23, 2004, the Ministry of Industry, Tourism and Commerce issued an order authorizing the change in the commitments assumed by Telefónica Móviles España, S.A.U. in connection with the operation of the third-generation wireless telecommunications (UMTS) service. Under this order, the requests filed by Telefónica Móviles España, S.A.U. in this respect were upheld, compliance with certain commitments was reinterpreted and other commitments were eliminated for the benefit of public interest.

As a result of this change, the amount to be guaranteed by Telefónica Móviles España, S.A.U. as a performance bond for the commitments assumed prior to the launch of the UMTS service and in the first year of service was reduced to 158 million euros, the amount of the guarantee at December 31, 2006.

Subsequently, Telefónica Móviles de España, S.A. carried out the procedures to accredit its first year of operating the UMTS service before the Ministry. Compliance with the commitments was ratified by a resolution from the Ministry of Industry, Tourism and Commerce dated January 24, 2007, authorizing the partial cancellation of the guarantee, for 42 million euros. Accordingly, the total amount of the guarantee in force at December 31, 2007 was 116 million euros.

Telefónica Móviles de España has completed the procedures for accrediting before the Ministry its compliance with the commitments of the second year of operating the UMTS service. This led to a further decrease in the amount guaranteed.

Commitments relating to VIVO Participações S.A.

On August 2, 2007, VIVO Participações S.A., a subsidiary of Brasilcel N.V., signed an agreement with Telpart Participações S.A. for the acquisition of 53.9% of the voting stock and 4.27% of the preference shares of Telemig Participações S.A., and of 51.86% of the voting stock and 0.09% of the preference shares of Tele Norte Participações S.A.

In accordance with the terms of the agreement, the acquisition should be carried out simultaneously once approval by the Brazilian telecoms regulator, ANATEL, is given.

On November 6, 2007, ANATEL approved the acquisition of Telemig Participações S.A., but did not issue a ruling on the acquisition of Tele Norte Participações S.A.

On November 12, VIVO Participações S.A. received a proposal from TNL PCS S.A. (the Telemar Group) to acquire the shares of Tele Norte Participações S.A. mentioned above.

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Considering the importance to the company of acquiring Telemig Participações S.A. as soon as possible and the difficulties expected in obtaining ANATEL's approval of the acquisition of Tele Note Participações S.A. within a reasonable period of year, on December 20, 2007 the Board of Directors of VIVO Participações S.A. agreed to sign a contract with TNL PCS S.A. (the Telemar Group) whereby it undertook, provided approval by ANATEL is given beforehand, to sell to TNL PCS S.A. the shares of Tele Norte Participações S.A. that Telpart Participações S.A. is obliged to sell to VIVO Participações S.A., under similar terms and conditions as those VIVO Participações S.A. undertook to acquire the shares.

ANATEL is expected to authorize this transaction soon.

The contingencies arising from the litigation and commitments described above were evaluated (see Note 3.1) when the consolidated financial statements for the year ended December 31, 2007 were prepared, and the provisions recorded in respect of the commitments taken as a whole are not material.

Environmental matters

Through its investees and in line with its environmental policy, the Telefónica Group has undertaken various environmental-management initiatives and projects. In 2007 and 2006 these initiatives and projects resulted in expenditure and investment for insignificant amounts, which were recognized in the consolidated income statement and consolidated balance sheet, respectively.

The Group has launched various projects with a view to reducing the environmental impact of its existing installations, with project costs being added to the cost of the installation to which the project relates.

The Group has also rolled out internal control mechanisms sufficient to pre-empt any environmental liabilities that may arise in future, which are assessed at regular intervals either by Telefónica staff or renowned third-party institutions. No significant risks have been identified in these assessments.

d) Auditors fees

The fees paid in 2007 and 2006 to the various member firms of the Ernst&Young international organization, to which Ernst&Young, S.L. (the auditors of the Telefónica Group) belongs amounted to 23.77 and 23.47 million euros, respectively.

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The detail of these amounts is as follows:

	Millions of euros	
	2007	2006
Audit services (1)	21.94	22.04
Audit-related services (2)	1.56	0.92
Tax services (3)	0.00	0.11
Other non-audit work (4)	0.27	0.40
TOTAL	23.77	23.47

(1) Audit services:

Services included under this heading are mainly the audit of the annual and interim financial statements, work to comply with the requirements of the Sarbanes-Oxley Act (Section 404) and the review of the 20-F report to be filed with the US Securities and Exchange Commission (SEC).

(2) Audit-related services: This heading mainly includes services related to the review of the information required by regulatory authorities, agreed financial reporting

procedures not requested by legal or regulatory bodies and the review of corporate responsibility reports.

(3) Tax services:

These basically comprise tax consulting services.

(4) Other non-audit services:

The services included under this heading relate to other permissible advisory services (non-current assets and other).

Ernst&Young's fees include amounts paid in respect of fully and proportionately consolidated Spanish and foreign Telefónica Group companies. In 2007, a total of 0.89 million euros corresponding to 50% of the fees paid by proportionately consolidated companies was included.

Fees paid to other auditors in 2007 and 2006 amounted to 18.28 million euros and 32.69 million euros, respectively, as follows:

	Millions of euros	
	2007	2006
Audit services	0.98	2.90
Audit-related services	4.23	4.95
Tax services	4.33	4.81
Other non-audit services	8.74	20.03
TOTAL	18.28	32.69

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Other auditors' fees include amounts paid in respect of fully and proportionately consolidated Spanish and foreign Telefónica Group companies. In 2007 and 2006, a total of 0.68 and 1.09 million euros, respectively, corresponding to 50% of the fees paid by proportionately consolidated companies, were included.

e) Trade guarantees

The Company is required to issue trade guarantees in the ordinary course of its business. No significant additional liabilities in the accompanying consolidated financial statements are expected to arise from trade guarantees issued.

f) Directors and Senior Executive compensation and other benefits

The compensation of Telefónica's directors is governed by Article 28 of the bylaws, which states that the compensation paid by the Company to its directors shall be determined at the Shareholders' Meeting and shall remain in force until a resolution is adopted at the Shareholders' Meeting to amend it. The Board of Directors is responsible for setting the exact amount to be paid within the stipulated limits and distributing it among the directors. On April 11, 2003, shareholders set the maximum gross annual amount to be paid to the Board of Directors at 6 million euros. This includes a fixed payment and fees for attending meetings of the Board of Directors' advisory or control committees.

Therefore, the compensation of Telefónica's directors in their capacity as members of the Board of Directors and/or of the Standing Committee and the advisory and control committees consists of a fixed amount payable monthly plus fees for attending the meetings of the Board's advisory or control committees. In addition, it was agreed that from September 2007, executive directors would not receive the fixed amounts established for their membership of the Board of Directors and Standing Committee, but only receive the corresponding amounts for discharging their executive duties as stipulated in their respective contracts.

The total compensation paid to Telefónica directors for discharging their duties as such in 2007 entailed: fixed payments of 3,704,333 euros and attendance fees of 211,250 euros for attending the Board of Directors' advisory committee meetings. It should also be noted that the compensation paid to Company directors sitting on the Boards of other Telefónica Group companies amounted to 405,192 euros. In addition, the six Company directors who are members of the Catalonia, Andalusia and Valencia advisory committees received a total 73,750 euros in 2007.

In addition, in their capacity as company executives, the executive directors César Alierta Izuel, Julio Linares López, José María Álvarez-Pallete López, Peter Erskine (who stepped down from his executive duties on December 31, 2007) and Antonio Viana-Baptista (who stepped down from his executive duties on January 31, 2008) received: 12,368,727 euros in salaries and variable compensation; 33,018 euros in contributions made to Company-sponsored pension plans and 126,302 euros of compensation in kind, which included other insurances (general medical and dental insurance), as well as life insurance premiums.

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- i) In addition, it should be noted that Peter Erskine received the following amounts: (i) 615,283 euros as periodic payment in cash relating to the commitments previously acquired by O2 plc. in connection with his pension plan, this item set forth in the Document containing the Tender offer, (ii) 3,838,077 euros under the 2005 O2 Share Plan, which was likewise set forth in the Document containing the Tender offer, and (iii) in accordance with the conditions of O2 acquisition, 24,331,831 euros for stepping down from his executive duties, broken down as follows: variable compensation for 2007, a payment for the advance notice clause in his employment contract, a payment for his employment commitment in accordance with the terms of the Framework Agreement signed in relation to the takeover bid for O2 plc. shares and the payment of the obligations acquired at the time by O2 plc. regarding pension plans, this concepts was included likewise in the takeover document. The bulk of this last payment was made in 2007, with the remainder paid in January 2008.

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In order to make this information more transparent and easier to understand, the following table presents the breakdown by concept, remuneration and benefits paid to Telefónica directors in 2007:

<i>Euros</i> Director	Board of Directors	Standing Committee	Board Committees		TOTAL
			Fixed payment	Attendance fees	
Chairman					
César Alierta Izuel	290,000	96,667			386,667
Vice chairmen					
Isidro Fainé Casas	241,667	96,667			338,334
Gregorio Villalabeitia Galarraga ⁽¹⁾	137,500	55,000	22,500	20,000	235,000
Vitalino Manuel Nafría Aznar	186,667		7,000	3,750	197,417
Members					
Julio Linares López	95,000	63,333	8,667	7,500	174,500
José María Abril Pérez ⁽²⁾	62,500	41,667	3,500	1,250	108,917
José Fernando de Almansa					
Moreno-Barreda	145,000		40,000	20,000	205,000
José María Álvarez-Pallete López	95,000				95,000
David Arculus	145,000				145,000
Maximino Carpio García ⁽³⁾	145,000	96,667	40,833	26,250	308,750
Carlos Colomer Casellas	145,000	96,667	13,333	2,500	257,500
Peter Erskine	95,000	63,333			158,333
Alfonso Ferrari Herrero	145,000		60,333	26,250	231,583
Gonzalo Hinojosa Fernández de Angulo	145,000		73,667	35,000	253,667
Pablo Isla Álvarez de Tejera	145,000		50,500	17,500	213,000
Antonio Massanell Lavilla	145,000		47,000	23,750	215,750
Enrique Used Aznar ⁽⁴⁾	145,000		60,333	27,500	232,833
Antonio Viana-Baptista	95,000	63,333			158,333

(1) Gregorio Villalabeitia Galarraga was a director of Telefónica until July 25, 2007, being replaced as Vicechairman by Vitalino Manuel Nafría Aznar.

(2)

José María
Abril Pérez was
appointed direct
of Telefónica on
July 25, 2007.

- (3) Maximino
Carpio García
was a director of
Telefónica until
December 19,
2007.

- (4) Enrique Used
Aznar was a
director of
Telefónica until
December 19,
2007.

For a better understanding of the information provided above, the following table presents the amounts established for fixed compensation and attendance fees, where appropriate, of the Board of Directors, Standing and Advisory or Control Committees.

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Board of Directors. Fixed payment for each director (euros):

Position	2007
Chairman	290,000
Vice chairmen	241,667
Directors:	
Executives	95,000
Non-independent external directors	145,000
Independent external directors	145,000
Other external directors	145,000

* Directors
receive no
attendance fees
for Board and
Standing
Committee
meetings.

Standing Committee. Fixed payment for each director forming part of the Standing Committee, by position (euros):

Position	2007
Chairman	96,667
Deputy Chairman	96,667
Members	96,667

* Directors
receive no
attendance fees
for Board and
Standing
Committee
meetings.

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Other Board committees.

A) Fixed payment for each director forming part of one of the Board committees, by position (euros):

Position	2007
Chairman	26,667
Members	13,333

B) Total fees paid to directors in 2007 for attending meetings of the advisory or control committees (euros):

Committee	2007
Audit and Control	Attendance fee per meeting: 1,250 Number of meetings paid: 11
Appointments, Compensation and Good Governance	Attendance fee per meeting: 1,250 Number of meetings paid: 10
Human Resources, Reputation and Corporate Responsibility	Attendance fee per meeting: 1,250 Number of meetings paid: 4
Regulation	Attendance fee per meeting: 1,250 Number of meetings paid: 11
Service Quality and Customer Service	Attendance fee per meeting: 1,250 Number of meetings paid: 4
International Affairs	Attendance fee per meeting: 1,250 Number of meetings paid: 5

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In addition, the total paid to executive directors César Alierta Izuel, Julio Linares López, José María Álvarez-Pallete López, Peter Erskine and Antonio Viana-Baptista for discharging their executive duties, by item (in euros), is the following:

Item	2007
Salary ⁽¹⁾	5,688,154
Variable compensation ⁽²⁾	6,680,573
Compensation in kind	126,302
Contributions to pension plans	33,018

(1) It is stated for the record that in addition, Mr. Peter Erskine received the amount of 615,283 euros as periodic payment in cash relating to the commitments previously acquired by O2 plc. in connection with his pension plan, this item set forth in the Document containing the Tender offer,

(2) In addition, it is stated, for the record, that Mr. Peter Erskine received the following amounts: (i) in accordance with the conditions of O2 acquisition, 24,331,831 euros for

relinquishing his
status as a
Company
executive under
the terms
indicated above,
and (ii)
3,838,077 euros
under the 2005
O2 Share Plan,
which was
likewise set
forth in the
Document
containing the
Tender offer,

In addition, related to the Performance Share Plan authorized at the General Shareholders Meeting of June 21, 2006 (see Note 20), the maximum number of shares corresponding to the first and second phases of the Plan will be given (on July 1, 2009 and July 1, 2010) to each of the executive directors of Telefónica, S.A. if all the terms established for such delivery are met, is as follows: César Alierta Izuel (129,183 shares in the first phase and 116,239 shares in the second); Julio Linares López (65,472 and 57,437 shares, respectively); José María Álvarez-Pallete López (62,354 and 53,204 shares, respectively); Antonio Viana-Baptista (62,354 and 53,204 shares, respectively). With respect to Peter Erskine (who was allocated 181,762 shares in the first phase and 151,863 shares in the second), he will receive, within the first three months of 2008, the number of shares he is entitled to, if any, based on the period of each phase during which he was an executive of the Telefónica Group.

It should be noted that the non-executive directors do not receive and did not receive in 2007 any compensation in the form of pensions or life insurance, and they do not participate in the compensation plans linked to Telefónica's share price.

In addition, the Company does not grant and did not grant in 2007 any advances, loans or credits to the directors, or to its top executives, thus complying with the requirements of the Sarbanes-Oxley Act passed in the U.S. which is applicable to Telefónica as a listed company in that market. Meanwhile, the four senior executives³ of the Company, excluding those that are also members of the Board of Directors, received a total for all items in 2007 of 4,813,277 euros.

³ For these purposes, Senior Executives are understood to be individuals who perform senior management functions in a company reporting directly to the management bodies, executive committees or CEOs,

including the
person in charge
of the internal
audit.

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In addition, the maximum number of shares corresponding to the first and second phases of the Performance Share Plan to be delivered to all the Company's senior executives if all the established terms are met is 157,046 shares and 130,911 shares, respectively.

In addition, with respect to the Pension Plan for directors (see Note 19), the total amount of contributions made by the Telefónica Group in 2007 was 1,707,237 euros for executive directors and 786,261 euros for directors who held positions of senior executives at the Company in 2007.

Finally, we would note that the senior executive contracts, including those of executive directors, generally include a severance clause entailing three years of salary plus another year based on the length of service at the Company. The annual salary on which the indemnity is based is the director's last fixed salary and the average amount of the last two variable payments received by contract.

g) Detail of the equity interests in companies engaging in an activity that is identical, similar or complementary to that of the Company and the performance of similar activities by the directors on their own behalf or on behalf of third parties:

Pursuant to Article 127 ter. 4 of the Spanish Corporation Law, introduced by Law 26/2003 of July 17, which amends Securities Market Law 24/1988 of July 28, and the revised Spanish Corporation Law, in order to reinforce the transparency of listed corporations, details are given below of the companies engaging in an activity that is identical, similar or complementary to the corporate purpose of Telefónica, S.A., in which the members of the Board of Directors own equity interests, and of the functions, if any, that they discharge in them:

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Director	Investee	Activity	% of ownership⁴	Position
David Arculus	Vodafone Group, Plc.	Telecommunications	< 0.01%	
	British Sky Broadcasting Group, Plc.	Telecommunications	< 0.01%	
	BT Group, Plc.	Telecommunications	< 0.01%	
Isidro Fainé Casas	Abertis Infraestructuras, S.A.	Telecommunications	< 0.01%	Chairman
Antonio Viana-Baptista	PT Multimedia-Serviços de Telecomunicações e Multimedia, S.G.P.S., S.A.	Internet	< 0.01%	
	Portugal Telecom, S.G.P.S., S.A.	Telecommunications	< 0.01%	Director

The table below, in accordance with the same Law, gives details of activities carried out, on their own account or on behalf of third parties, by the various members of the Company Board of Directors that are identical, similar or complementary to the corporate purpose of Telefónica, S.A.

⁴ > 0.01% is shown if the holding is less than 0.01% of the share capital.

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Name	Activity	Arrangement under which the activity is performed⁵	Company through which the activity is performed	Position held or functions performed
César Alierta Izuel	Telecommunications	On behalf of third parties	Telefónica O2 Europe, Plc. (1)	Director
	Telecommunications	On behalf of third parties	Telecom Italia, S.p.A.	Director
	Telecommunications	On behalf of third parties	China Netcom Group Corporation	Director
Isidro Fainé Casas	Telecommunications	On behalf of third parties	Abertis Infraestructuras, S.A.	Chairman
Julio Linares López	Telecommunications	On behalf of third parties	Telefónica de España, S.A.U.	Director
	Telecommunications	On behalf of third parties	Telefónica DataCorp, S.A.U.	Director
	Telecommunications	On behalf of third parties	Telefónica O2 Europe, Plc	Director
	Telecommunications	On behalf of third parties	Telefónica O2 Czech Republic a.s.	1 st Vice Chairman of Supervisory Board
	Television, telecommunications and audiovisual production services	On behalf of third parties	Sogecable, S.A.	Director
	Telecommunications	On behalf of third parties	Telecom Italia, S.p.A.	Director

⁵ Only applicable where the service is provided on behalf of third parties and, accordingly, through a company.

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Name	Activity	Arrangement under which the activity is performed⁵	Company through which the activity is performed	Position held or functions performed
Fernando de Almansa Moreno-Barreda	Telecommunications	On behalf of third parties	Telefónica Internacional, S.A.U.	Director
	Telecommunications	On behalf of third parties	Telefónica del Perú, S.A.A.	Director
	Telecommunications	On behalf of third parties	Telefónica de Argentina, S.A.	Director
	Telecommunications	On behalf of third parties	Telecomunicações de Sao Paulo, S.A.	Director
	Telecommunications	On behalf of third parties	Telefónica Móviles México, S.A. de C.V.	Director
José María Álvarez-Pallete López (5)	Telecommunications	On behalf of third parties	Telefónica Internacional, S.A.U.	Executive Chairman
	Telecommunications	On behalf of third parties	Telefónica Móviles España, S.A.U.	Director
	Telecommunications	On behalf of third parties	Telefónica de España, S.A.U.	Director
	Telecommunications	On behalf of third parties	Telefónica DataCorp, S.A.U.	Director

⁵ Only applicable where the service is provided on behalf of third parties and, accordingly, through a company.

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Name	Activity	Arrangement under which the activity is performed⁵	Company through which the activity is performed	Position held or functions performed
José María Álvarez-Pallete López (5)	Telecommunications	On behalf of third parties	Telefónica O2 Europe, Plc. (2)	Director
	Telecommunications	On behalf of third parties	Telefónica de Argentina, S.A. (6)	Director/Vice Chairman
	Telecommunications	On behalf of third parties	Telecomunicações de Sao Paulo, S.A.	Director/Vice Chairman
	Telecommunications	On behalf of third parties	Compañía de Telecomunicaciones de Chile, S.A.	Acting Director
	Telecommunications	On behalf of third parties	Telefónica Móviles México, S.A. de C.V.	Director/Vice Chairman
	Telecommunications	On behalf of third parties	Colombia Telecomunicaciones, S.A. ESP	Director
	Telecommunications	On behalf of third parties	Telefónica del Perú, S.A.A.	Acting Director
	Telecommunications	On behalf of third parties	China Netcom Group Corporation	Director
	Telecommunications	On behalf of third parties	Brasilcel, N.V.	Chairman of Supervisory Board
	Telecommunications	On behalf of third parties	Telefónica Móviles Colombia, S.A.	Director

⁵ Only applicable where the service is provided on behalf of third parties and, accordingly, through a company.

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Name	Activity	Arrangement under which the activity is performed⁵	Company through which the activity is performed	Position held or functions performed
David Arculus	Telecommunications	On behalf of third parties	Telefónica O2 Europe, Plc.	Director
Peter Erskine	Telecommunications	On behalf of third parties	Telefónica O2 Europe, Plc.(3)	Executive Chairman
	Telecommunications	On behalf of third parties	Telefónica O2 Czech Republic, a.s. (7)	Chairman of Supervisory Board
Alfonso Ferrari Herrero	Telecommunications	On behalf of third parties	Compañía de Telecomunicaciones de Chile, S.A.	Director
	Telecommunications	On behalf of third parties	Telefónica de Perú, S.A.A.	Director
	Telecommunications	On behalf of third parties	Telefónica Móviles Chile, S.A.	Director
Antonio Viana-Baptista	Telecommunications	On behalf of third parties	Portugal Telecom, SGPS, S.A.(4)	Director
	Telecommunications	On behalf of third parties	Telefónica O2 Europe, Plc.	Director

⁵ Only applicable where the service is provided on behalf of third parties and, accordingly, through a company.

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- (1) On January 16, 2008, César Alierta Izuel stepped down from his post as director of Telefónica O2 Europe, Plc.
- (2) On January 16, 2008, José María Álvarez-Pallete López stepped down from his post as director of Telefónica O2 Europe, Plc.
- (3) On December 31, 2007, Peter Erskine stepped down from his post as director and executive chairman of Telefónica O2 Europe, Plc. Subsequently, on February 1, 2008, he was reappointed a director of the Company.
- (4) On January 31, 2008, Antonio Viana-Baptista stepped down from his post as director of Portugal Telecom, SGPS, S.A.
- (5) On February 12, 2008, José María Álvarez- Pallete López was appointed a director of Portugal Telecom, SGPS, S.A.
- (6) On February 21, 2008, José María Álvarez-Pallete López stepped down from his post as director of Telefónica de Argentina, S.A. and became acting director.

On the same date, Francisco Javier de Paz Mancho was appointed director Telefónica de Argentina, S.A.

- (7) On February 21, 2008, Peter Erskine stepped down from his post as member of the Supervisory Board of Telefónica O2 Czech Republic, a.s. and, therefore, his post as Chairman of this board.

- * On February 19, 2008 Francisco Javier de Paz Mancho was appointed director Telecomunicações de Sao Paulo, S.A.

Pursuant to Article 114.2 of the Spanish Corporation Law, also introduced by Law 26/2003 of July 17, it is stated that in the year to which these annual financial statements refer, the directors, or persons acting on their behalf, did not perform any transactions with Telefónica or any other company in the Telefónica Group other than in the normal course of the Company's business or that were not at arm's length.

Table of Contents**(22) FINANCE LEASES**

The principal finance leases at the Telefónica Group are as follows:

- a) Future minimum lease payment commitments in relation to finance leases at O2 Group companies.

Millions of euros	Minimum payments	Finance costs	Present value
Within one year	38	(16)	22
From one to five years	209	(38)	171
After five years	130	(10)	120
Total	377	(64)	313

These commitments arise from plant and equipment lease agreements. Between March 30, 1991 and April 9, 2001, finance lease agreements were signed between O2 UK and a number of US leasing trusts. A substantial part of the radio and switch equipment of its GSM network is subject to the terms of said agreements. The agreements have a term of 16 years and an early purchase option after the first 12 years.

At December 31, 2007 and 2006, assets under this lease amounting to 323 and 389 million euros, respectively, were recognized under property, plant and equipment.

- b) Finance lease agreement at Colombia de Telecomunicaciones, S.A., ESP.

Similarly, via its subsidiary Colombia de Telecomunicaciones, S.A., ESP, the Group has a finance lease agreement with PARAPAT, the consortium which owns the telecommunications assets and manages the pension funds for the entities which were predecessors to Colombia de Telecomunicaciones, S.A., E.S.P., and which regulate the operation of assets, goods and rights relating with the provision of telecommunications services by the company, in exchange for financial consideration.

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This agreement includes the transfer of these assets and rights to Colombia de Telecomunicaciones, S.A., ESP once the last installment of the consideration has been paid in line with the payment schedule over a period of 17 years from 2006:

	Present value	Revaluation	Installments Pending payments
2008	122	17	139
2009	118	34	152
2010	113	51	164
2011	109	70	179
2012	144	123	267
Subsequent years	1,184	3,154	4,338
Total	1,790	3,449	5,239

The net amount of property, plant and equipment recorded under the terms of this lease was 705 million euros at December 31, 2007 (816 million euros at December 31, 2006).

(23) CASH FLOW ANALYSIS**Net cash flow from operating activities**

In 2007, the Telefónica Group obtained operating cash flow less payments to suppliers for expenses and employee benefits expenses totaling 20,105 million euros, 6.9% more than the 18,810 million euros generated in 2006. This increase was largely due to the contribution of synergies arising from the integrated management of operations, to cost cutting and to the growth in consolidated revenue. In 2006, operating cash flow less payments to suppliers for expenses and employee benefits expenses rose 36.1% from 2005 (13,821 million euros), due mostly to the contribution of the acquisition of O2's wireless operators in early 2006 and a solid operating performance.

Customer collections in 2007 increased by 11.4% to 67,129 million euros (60,285 million euros in 2006). This growth was due to the strong performance of revenues driven by the increase in the customer base from the success of the campaigns to win and retain customers. Customer collections in 2006 rose 35.9% from 2005 (44,353 million euros) due to the healthy business performance and, above all, the changes in the consolidation scope following the acquisition of O2's wireless operators.

Cash payments to suppliers and employees to December 31, 2007 totaled 47,024 million euros, up 13.4% (2006: 41,475 million euros). This increase was due to greater commercial efforts in the various geographic areas while maximizing the efficiency of the cost structure, and to higher interconnection charges. Cash payments to suppliers and employees at December 31, 2006 rose 35.8% (2005: 30,532 million euros) due largely to changes in the consolidation scope with the inclusion of O2's wireless operators in 2006 and in the management and performance of the business.

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Payments for employee benefits expense was higher in 2007 than in 2006, mainly in line with the increase in average headcount. The increase in payments for employee benefits expense in 2006 from 2005 was due mainly to the inclusion of the workforces of O2's wireless operators.

Payments for net interest and other finance expenses in 2007 amounted to 3,221 million euros, up 35.8% from 2006 (2,372 million euros). This increase was mostly due to the payment of coupons on bonds and debentures issued in 2006 and to the increase in interest rates. In 2006, the increase was 56.1% (2005: 1,520 million euros), as a result of the increase in debt.

In addition, taxes paid in 2007 rose 32.5%, to 1,457 million euros from 1,100 million euros in 2006. This increase was due to the higher profit stated in 2006 compared to 2005 corresponding to the Latin American subsidiaries. In 2005, the tax charge was 1,233 million euros, 10.8% more than in 2006.

Accordingly, net cash flow from operating activities totaled 15,551 million euros in 2007 (15,414 million euros in 2006). Cash flow from operating activities in 2006 was 38.4% higher than in 2005 (11,139 million euros).

Net cash flows used in investment activities

Net cash used in investing activities decreased by 23,460 million euros in 2007 to 4,592 million euros from 28,052 million euros in 2006. This net decrease was due mainly to the decline in payments on investments in companies (net of cash and cash equivalents acquired) to 2,798 million euros from 23,757 million euros. This included the 2,314 million euro investment for the 42.3% stake in Telco SpA (see Note 2). The main investment in 2006 was the acquisition of O2 Plc for 23,554 million euros. In 2006, net cash used in investing activities increased by 18,460 million euros to 28,052 million euros from 9,592 million euros in 2005. This net increase was due mainly to payments on investments in companies (net of cash and cash equivalents acquired), which totaled 23,757 million euros in the year compared to 6,571 million euros the year before, mostly on the O2 plc acquisition for 23,553 million euros (see Note 3). The main investments in 2005 were the acquisition of Czech operator Telefónica O2 Czech Republic, a.s. for 3,663 million euros, as well as the first disbursement of 1,266 million euros in connection with the acquisition of O2 plc.

Investment in property, plant and equipment and intangible assets in 2007 totaled 7,274 million euros, an increase of 341 million euros from the year before. In 2006, investments in property, plant and equipment and intangible assets amounted to 6,933 million euros, 2,510 million euros more than in 2005 due to the consolidation of O2 plc, which accounted for 2,234 million euros.

Proceeds from disposals of investments in companies, net of cash and cash equivalents acquired, amounted to 5,346 million euros in 2007. This included disposals of stakes in Airwave and Endemol, for 2,841 and 2,107 million euros, respectively (see Note 2). In 2006, proceeds from disposals of investments in companies, net of cash and cash equivalents acquired, amounted to 2,294 million euros, including 1,816 million euros from the sale of TPI and 300 million euros from divestment in Sogecable.

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Net cash flow used in financing activities

Net cash used in financing activities totaled 9,425 million euros in 2007, compared with the 14,572 million euros obtained from financing activities in 2006. The 23,997 million euro difference is due basically to the change in financing transactions, mainly the repayment of part of the financing arranged in the prior year. In 2006, net cash from financing activities amounted to 14,572 million euros, compared to net cash used in financing activities of 435 million euros in 2005. The 15,007 million euro difference essentially reflects the increase in fund raising, which in 2006 entailed net issuance of 20,114 million euros, compared to 4,387 million euros in 2005.

(24) EVENTS SUBSEQUENT TO YEAR END

Significant events affecting the Telefónica Group taking place from December 31, 2007 to the date of preparation of these consolidated financial statements included:

Acquisition of an additional 2.22% of China Netcom Group Corporation.

On January 18, 2008, Telefónica Internacional, S.A. signed four contracts to acquire shares representing 0.5542% each of the shares capital of China Netcom Group Corporation (Hong Kong) Limited (CNC) with Shanghai Alliance Investment Ltd., Information and Network Centre of the State Administration of Radio Film and Television, P.R.C., Chinese Academy of Sciences Holdings Co., Ltd., and China Railway Communications Center. Therefore, provided authorization is given by the pertinent regulators, Telefónica Internacional, S.A. has acquired a commitment to purchase a total additional stake of approximately 2.22% of CNC. After the acquisition, the Telefónica Group's stake in this company will be approximately 7.22%.

The additional stake in CNC will require a total investment of approximately 309 million euros (depending on the exchange rate applicable when the transaction is completed).

EIB financing

On January 15, 2008, Telefónica Finanzas, S.A. paid off at maturity the balance on the 200 million dollar loan taken out with the European Investment Bank (EIB) on January 9, 1998, guaranteed by Telefónica.

On January 17, 2008, Telefónica Finanzas, S.A. arranged a 75 million euro facility (Tranche B of the Telefonica Mobile Telephony II project) with a bank guarantee and counter guarantees by Telefónica maturing January 29, 2016.

On January 30, 2008, Telefónica Finanzas, S.A. drew down the amounts of the facilities arranged with the EIB on December 3, 2007 and January 17, 2008 of 375 and 75 million euros, respectively, comprising Tranches A and B of the Telefonica Mobile Telephony II project.

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Repayment of Telefónica Móviles Colombia financing

On December 10, 2007, Telefónica Móviles Colombia, S.A. signed a financing arrangement with the Inter-American Development Bank (IDB) for 600 million dollars divided in two tranches. Tranche A entailed a 7-year 125 million dollar bilateral loan with the IDB, and Tranche B a 5-year 475 million dollar syndicated credit facility with a group of banks, in which the IDB acted as agent bank. On January 15, 2008, Telefónica Móviles Colombia, S.A. drew down the entire amount of financing arranged on December 10, 2007, for a total of 600 million US dollars.

(25) ADDITIONAL NOTE FOR ENGLISH TRANSLATION

These financial statements are presented on the basis of International Reporting Standards adopted by the European Union which for the purposes of the Telefónica Group are not different from those issued by the International Accounting Standard Board (IASB). Consequently, certain accounting practices applied by the Group not conform with generally accepted principles in other countries.

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APPENDIX I: CHANGES IN THE SCOPE OF CONSOLIDATION

The following changes took place in the consolidation scope in 2007:

Telefónica O2 Europe

In April, Telefónica O2 Europe PLC, a wholly owned subsidiary of Telefónica, S.A., and its 100%-owned subsidiary O2 Holdings LTD, sold 100% of the shares of UK company Airwave O2 Ltd. for 1,932 million pounds sterling (equivalent to 2,841 million euros at the transaction date), obtaining a gain of 1,296 million euros. This company, which had been fully consolidated in the Telefónica Group, was removed from the consolidation scope.

On December 20, 2007, the O2 Group transferred legal ownership of the entire business in Germany to Telefónica, S.A. through a dividend in kind for 8,500 million euros.

Telefónica Latin America

In April, the 54% stake held by US company Katalyx, Inc. in Brazilian company Mercador, S.A. was sold. The company, which had been consolidated in the Telefónica Group's financial statements using the equity method, was removed from the consolidation scope.

In June, US company Telefónica USA, Inc., a wholly owned subsidiary of the Spanish company Telefónica Datacorp, S.A., acquired 100% of the assets and shares of US company Katalyx Inc. The company is still fully consolidated in the Telefónica Group.

In 2007, Brazilian company Telecomunicações de São Paulo, S.A. acquired 100% of Brazilian company NavyTree Participações, S.A. for 361 million euros. This company was included in the consolidation scope using the full consolidation method.

Other companies

In February 2007, 100% of the shares of Endemol France were sold to Endemol, N.V., a company in which the Telefónica Group had a 75% stake.

In May, Telefónica, S.A. signed an agreement to sell its 99.7% stake in Dutch company Endemol Investment Holding, B.V. to a newly created consortium owned equally by Mediacinco Cartera, S.L., a newly created company owned by Italian company Mediaset and its listed Spanish subsidiary Gestevisión Telecinco, Cyrté Fond II, B.V. and G.S. Capital Partners VI Fund, L.P. for 2,629 million euros, obtaining capital gains of 1,368 million euros. This sale was carried out on July 3. The company, which had been fully consolidated in the Telefónica Group, was removed from the consolidation scope.

Spanish companies Comunicapital Gestión, S.A. and Terra Lycos Intangibles, S.A. were liquidated in 2007. Both companies, which had been fully consolidated, were therefore eliminated from the scope of consolidation.

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In the first quarter of 2007, the Telefónica Group disposed of shares in Italian company Ipse 2000 S.p.A., lowering its shareholding to 39.9158%. The Telefónica Group still carries this company using the equity method of accounting.

In June 2007, Telefónica, S.A. sold all the shares it held in the Spanish company Sistemas Técnicos de Loterías del Estado, S.A., which represented 31.75% of its share capital. The company, which had been accounted for the Telefónica Group using the equity method, was removed from the consolidation scope.

In June, Spanish company Atento Teleservicios España, S.A. incorporated US company Contact US Teleservices Inc., contributing 100% of the start-up capital for 0.1 million US dollars. This company has been included in the Telefónica Group's consolidated scope using the full consolidation method. In August, US Teleservices Inc. held a 0.55 million US dollar rights issue, fully subscribed by Atento Teleservicios España, S.A.

In August 2007, the Telefónica Group disposed of its 100% holding in Spanish company Azeler Automoción, S.A. for 0.34 million euros. The company, which had been fully consolidated in the Telefónica Group, was removed from the consolidation scope.

On April 28, 2007, Telefónica, S.A., together with its partners Assicurazioni Generali, S.p.A., Intesa Sanpaolo, S.p.A., Mediobanca, S.p.A. and Sintonía, S.A. (Benetton), entered into a Co-Investment Agreement and Shareholders Agreement with a view to establishing the terms and conditions of their acquisition of an indirect shareholding in Telecom Italia, S.p.A. through an Italian company, currently called Telco, S.p.A., in which Telefónica has a 42.3% interest. Both agreements were modified on October 25, 2007 following the inclusion of the Assicurazioni Generali Group companies indicated hereafter and the Shareholders Agreement was further amended on November 19, 2007.

On October 25, 2007 Telco, S.p.A. acquired 100% of Olimpia, S.p.A., which held 17.99% of the voting shares of Telecom Italia, S.p.A. Also on that date, Assicurazioni Generali, S.p.A. (together with its group companies Alleanza Assicurazioni, S.p.A., INA Assitalia, S.p.A., Volksfürsorge Deutsche Lebensversicherung, A.G. and Generali, Vie S.A.) and Mediobanca, S.p.A. contributed a total share of 5.6% of Telecom Italia, S.p.A.'s voting shares (4.06% and 1.54%, respectively) to Telco, S.p.A.

On December 10, 2007, an agreement was reached to takeover and merge Olimpia, S.p.A. into Telco, S.p.A., making Telco, S.p.A.'s entire stake in the voting shares of the Italian operator (23.6%) direct and leaving Telefónica with an indirect holding in the voting shares of Telecom Italia, S.p.A. of 9.98% (6.88% of the dividend rights) for 2,314 million euros.

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The Shareholders Agreement signed on April 28, 2007 contained a general clause whereby both Telefónica, at the shareholders meetings of Telco, S.p.A. and Telecom Italia, S.p.A., and the Telefónica directors appointed to the companies' respective boards, would abstain from participating in and voting at the meetings dealing with issues regarding the provision of telecommunications services by companies controlled by Telecom Italia, S.p.A., in countries where there are legal or regulatory restrictions on the exercise of voting rights by Telefónica.

However, as indicated above, on November 19, 2007 the partners expounded on and detailed the Shareholders Agreement, as well as the bylaws of Telco, S.p.A., to include the specific limitations imposed by the Brazilian telecommunications regulator, Agência Nacional de Telecomunicações (ANATEL), as initially posted on its website on October 23, 2007 and subsequently published on November 5, 2007 as ANATEL's Ato no. 68,276 dated October 31, 2007.

Pursuant to clause 8.5(a) of the Shareholders Agreement, on November 6, 2007 Telco, S.p.A. and Telefónica entered into a Call Option Agreement giving Telefónica the option to buy shares of Telecom Italia, S.p.A. in the event Telco, S.p.A. adopted a resolution to sell or pledge shares Telecom Italia, S.p.A. (or rights related to its shares, such as voting rights) by simple majority and Telefónica were the dissenting party, under the terms of the Shareholders Agreement.

In December, Telefónica, S.A. sold 18,558,181 shares of Portuguese company Portugal Telecom, S.G.P.S., S.A. This sale lowered the Telefónica Group's shareholding in this company to 8.32%, or 9.155% including Portugal Telecom's treasury shares. The company is still accounted for in the Telefónica Group's consolidated financial statements using the equity method.

In December, Telefónica, S.A. incorporated, as its sole shareholder, the Spanish company Atento Holding, Inversiones y Teleservicios, S.A., with start-up capital of 24 million euros and a share premium of 138 million euros. The shares were fully subscribed and paid via the non-monetary contribution of all of the shares in Dutch company Atento, N.V., of which Telefónica, S.A. was the sole shareholder. The company has been fully consolidated in the Telefónica Group.

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Changes to the consolidation scope in 2006 are:

Spain

On July 29, 2006, the takeover documents related to the merger of Telefónica Móviles, S.A. by Telefónica, S.A. were filed with Mercantile Registry of Madrid. The merger was carried out via an exchange offer and the exchange ratio was set at 4 shares of Telefónica, S.A., a par value of 1 euro, for every 5 shares of Telefónica Móviles, S.A., par value of 0.5 euros. Accordingly, Telefónica delivered 244,344,012 of its treasury shares to the shareholders of Telefónica Móviles, S.A., representing approximately 7.08% of Telefónica Móviles, S.A.'s share capital. The merger also entailed two extraordinary dividends totaling 0.435 euros per share, which combined with the ordinary 0.205 euro per share dividend against 2005 earnings, brought the total gross dividend to 0.64 euros per share, which was paid out on July 21. Telefónica Móviles, S.A., which had been fully consolidated in the Telefónica Group, was therefore removed from the consolidation scope.

In February 2006, the Spanish company Telefónica Cable, S.A. acquired 15% of the share capital of Telefónica Cable Galicia, S.A. Following this acquisition, Telefónica Cable became the company's sole shareholder. The company continues to be fully consolidated in the Telefónica Group.

In June 2006, Telefónica Cable, S.A. absorbed Sociedad General de Cablevisión Canarias, S.A.U. Following this transaction, the absorbed company, which was previously fully consolidated, was removed from the Telefónica Group's consolidation scope.

In July, 2006, Telefónica de España, S.A. took over and merged Terra Networks España, S.A. and Telefónica Data España, S.A. Both companies had been fully consolidated in the financial statements of the Telefónica Group but were then removed from the consolidation scope.

Also in July, Telefónica de España, S.A. acquired 51% of the share capital of Iberbanda, S.A. for 37 million euros. The Telefónica Group consolidates this company using the full consolidation method.

Latin America

Brazilian company Santo Genovese Participações Ltda., the holding company for all the share capital of Atrium Telecomunicações Ltda. (also Brazilian) was liquidated in the first quarter of 2006, following the absorption of its subsidiary, Atrium. Both companies, which had been fully consolidated by the Telefónica Group, were removed from the consolidation scope.

In April 2006, Telefónica Internacional, S.A. acquired 50% plus one share in Colombian company Colombia de Telecomunicaciones, S.A. ESP in a public offer. In December 2006, Colombia Telecom, S.A. absorbed Telefónica Data Colombia, S.A., also from Colombian, which was accordingly removed from the consolidation scope. As a result of the takeover and merger, the Telefónica Group increased its stake in Colombia Telecom to 52.03%. The company was included in the Telefónica Group's consolidated scope by the full consolidation method.

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In May 2006, Telefónica del Perú, S.A.A. absorbed its subsidiary Telefónica Empresas Perú, S.A.A. This company, which had been fully consolidated in the Telefónica Group, was removed from the consolidation scope.

On July 29, 2006, Brazilian company Telecomunicações de São Paulo, S.A. (Telesp) absorbed subsidiary Telefónica Data Brasil Holding. This company, which had been fully consolidated in the Telefónica Group, was removed from the consolidation scope.

Telefónica Finance, Ltd. and Telefónica Venezuela Holding, B.V. merged with Telefónica International Holding, B.V. Both companies had been fully consolidated in the financial statements of the Telefónica Group, but were then removed from the consolidation scope.

Spanish company Telefónica Soluciones de Informática y Comunicación, S.L. was absorbed by Telefónica Datacorp, S.A. (also Spanish) in December 2006. This company, which had been fully consolidated in the Telefónica Group, was removed from the consolidation scope.

As a result of the cancellation of treasury shares by Telesp in 2006, the acquisition of the minority interests in Telefónica Data Brasil and its subsequent merger into Telesp, the Telefónica Group's interest in the share capital of Telesp rose to 88.01%. The company is still fully consolidated in the Telefónica Group.

In 2006, Mexican companies Katalyx México S.A. de C.V. and Telefónica Empresas México S.A. de C.V., 100%-owned subsidiaries of the Telefónica Internacional Group, were sold. Both companies had been fully consolidated in the financial statements of the Telefónica Group, but were then removed from the consolidation scope.

On February 22, 2006, approval was given at the respective shareholders' meetings of Telesp Celular Participações S.A. (TCP), Tele Centro Oeste Celular Participações S.A., (TCO), Tele Sudeste Celular Participações S.A. (TSD), Tele Leste Celular Participações, S.A. (TBE) and Celular CRT Participações S.A. (CRT Part) for a corporate restructuring entailing the exchange of TCO shares for TCP shares and the absorption of TSD, TBE, and CRT Part by TCP. As a result, TCO became a 100%-owned subsidiary of TCP.

Following VIVO Participações' capital increase and the restructuring undertaken at Brasilcel in 2006, Brasilcel, N.V.'s stake in VIVO Participações increased to 62.94%.

In June 2006, the Telefónica Group increased its stake in Telefónica Móviles Perú from 98.03% to 98.40% through the acquisition of minority shareholdings for 1.02 million US dollars. This company continues to be fully consolidated in the Telefónica Group.

Throughout 2006, Telefónica Móviles El Salvador Holding, S.A. de C.V. acquired 2,220 shares in Telefónica Móviles El Salvador, S.A. de C.V., bringing its stake in the latter to 99.08%. This company continues to be fully consolidated in the Telefónica Group.

Telefónica Móviles Argentina, S.A. absorbed the following Argentine companies in 2006: Compañía de Radiocomunicaciones Móviles, S.A., Radio Servicios, S.A. and Compañía de Teléfonos del Plata, S.A. As a result, these companies were removed from the consolidation scope.

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In November 2006, the Telefónica Group's investees in Uruguay were restructured. Ablitur SA, Redanil SA and T. Móviles Uruguay, which were 100%-owned by Group companies, were liquidated. As a result of the restructuring, the Telefónica Group's mobile telephony investees in Uruguay were structured as follows: Wireless Network Ventures Ltd became wholly-owned by Telefónica Móviles Holding Uruguay S.A. and Telefónica Móviles del Uruguay SA (formerly Abiatar) was then 68%-owned by LACH B.V. Both companies continue to be fully consolidated in the Telefónica Group.

In 2006, US company Panama Cellular Holdings, LLC was liquidated. This company, which had been fully consolidated in the Telefónica Group, was removed from the consolidation scope.

In 2006, Mexican subsidiary Telecomunicaciones Punto a Punto México, S.A. de C.V. was sold, generating a capital gain of 10 million euros recognized under Gain on disposal of investments in consolidated companies in the Telefónica Group's consolidated income statement. This company, which had been fully consolidated in the Telefónica Group, was removed from the consolidation scope.

In 2006 the subsidiaries of Venezuelan company Comtel Comunicaciones Telefónicas, S.A. were restructured. As a result, the following companies were liquidated:

Promociones 4222. C.A., S.T. Mérida, C.A., S.T. Ciudad Ojeda, C.A., S.T. San Cristóbal, S.T. Maracaibo, C.A., S.T. Punto Fijo, C.A., S.T. Valera, C.A., S.T. Valencia, C.A., SyRed, T.E.I., C.A., Servicios Telcel Acarigua, C.A., Servicios Telcel Barquisimeto, C.A., Servicios Telcel Charallave, S.T. Cumana, C.A., S.T. Guarenas, C.A., S.T. Los Teques, C.A., S.T. Maracay, C.A., S.T. Margarita, C.A., S.T. Maturín, C.A., S.T. Puerto Ordaz, C.A., S.T. Puerto la Cruz, CA, S.T. and La Guaira, C.A.

All these Venezuelan companies, previously fully consolidated, were removed from the consolidation scope.

Europe

On October 31, 2005, Telefónica, S.A. made a binding offer to acquire all the shares of British company O2 Plc. Once the process was completed, Telefónica owned 100% of the share capital. On March 7, 2006, the shares were delisted from the London Stock Exchange. The cost of the acquisition of the O2 Group was 26,135 million euros (17,887 million pounds sterling). The Telefónica Group's financial statements include the results of the O2 Group from February 1, 2006. The company became fully consolidated within the Telefónica Group.

On July 1, 2006 Eurotel Praha, spol. s.r.o. (Eurotel) was taken over and merged by its parent company Cesky Telecom., a.s., giving rise to the new integrated operator named Telefónica O2 Czech Republic, a.s. Following this transaction, Eurotel, which had been fully consolidated in the Telefónica Group, was removed from the consolidation scope.

In June 2006, O2 UK Ltd. acquired 100% of British internet service provider, Be Un Limited (Be) for 50 million pounds sterling (approximately 73.5 million euros). Be was then fully consolidated in the Telefónica Group.

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In 2006, Telefónica Deutschland GMBH was sold to the German subsidiary of the O2 Group, Interkom. These two companies were subsequently merged to create a new company, Telefónica Deutschland GMBH, which is fully consolidated within the Telefónica Group's financial statements.

During the third quarter of 2006, Telefónica O2 Czech Republic, a.s.'s subsidiary, Telefónica O2 Slovakia, s.r.o., won a third wireless license in the Slovak Republic. The Slovak subsidiary is still fully consolidated in the Telefónica Group.

In October, 2006 the O2 Group acquired the remaining 60% of the share capital of the UK firm, The Link Stores, Ltd. for 28 million pounds sterling. Following the transaction, the Telefónica Group owns 100% of this company. Accordingly, The Link Stores, Ltd., which was accounted for under the equity method until September 2006, became fully consolidated in the Telefónica Group from October 1, 2006.

Telefónica, S.A. and other businesses

In March 2006 Prisa launched a partial takeover bid for 20% of Sogecable, S.A. The Telefónica Group sold shares to Prisa representing a 6.57% interest in Sogecable, S.A., thereby reducing its stake from 23.83% to 17.26%. Subsequently, also in March, Sogecable held a rights offering in which the Telefónica Group did not participate, thereby diluting its holding in the company to 16.84%. In April, Sogecable undertook an additional capital increase in order to service its share option plans for company directors, executives and management. Redeemable Class B and Series B2005 shares were converted into ordinary Class A shares, further diluting the Telefónica Group's stake to 16.80%. In December, Sogecable converted 405,000 redeemable Class and Series B2006 shares into ordinary Class A shares, reducing the Telefónica Group's interest in the company at December 31, 2006 to 16.75%. As a result of this dilution, at December 31, 2006, the investment in Sogecable was recognized under Other investments. This company, which had been accounted for by the Telefónica Group using the equity method, was removed from the consolidation scope.

In July 2006, Telefónica, S.A. accepted the public takeover bid launched by Yell Group Plc for 100% of the shares of Telefónica Publicidad e Información, S.A. (TPI). It therefore accepted Yell's bid for the 216,269,764 shares Telefónica owned in TPI, representing 59.905% of its share capital.

The gain from the sale and the results of the TPI Group through June 30, 2006 were recognized under Profit after taxes from discontinued operations in the Telefónica Group's consolidated income statement. In addition, for comparability, the Telefónica Group's 2005 financial statements were modified to classify the results of the TPI Group under the same heading.

In May 2006, the Telefónica de Contenidos Group sold all the shares it held in Argentine company Patagonik Film Group, S.A. This company had been accounted for under the equity method and was removed from the consolidation scope.

During 2006 Atento NV incorporated Argentine companies Atento Mar del Plata, S.A. (subsequently renamed Mar de Plata Gestiones y Contactos, S.A.) and Atento Salta, S.A. (subsequently renamed Centro de Contacto Salta, S.A.) with capital of 0.1 million Argentine pesos. Both companies are fully consolidated in the Telefónica Group.

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In May 2006, Chilean subsidiary Atento Chile Holding acquired Impresora y Comercial Publicguías, S.A.'s shareholding in Atento Chile, S.A. This increased the Atento Group's stake in Atento Chile from 69.99% to 71.16%. The Telefónica Group still consolidates the company using the full consolidation method.

In May 2006, Argentine company Atento Microcentro, S.A. (subsequently renamed Microcentro de Contacto, S.A.) was incorporated, with share capital of 0.05 million Argentine pesos. The company was fully consolidated in the financial statements of the Telefónica Group.

In June 2006, Atento, N.V. acquired 100% of the Uruguay firm, Woknal, S.A. for 0.4 million Uruguay pesos, approximately 0.01 million euros. The company was fully consolidated in the financial statements of the Telefónica Group.

In August 2006, Argentine company Atento Córdoba, S.A. (subsequently renamed Córdoba Gestiones y Contactos, S.A.) was incorporated with share capital of 0.05 million Argentine pesos. The company was fully consolidated in the financial statements of the Telefónica Group.

Andalucía Digital Multimedia, S.A. held a rights offering in which Telefónica de Contenidos, S.A. subscribed for shares, raising its interest in the company to 24.20%. The Telefónica Group still accounts for this investment using the equity method.

In February 2006, Compañía Española de Tecnología, S.A. (Comet) increased its share capital by 0.23 million euros by increasing the par value of its shares. In March that year, Comet undertook another capital increase. Both issues were fully subscribed and paid in by the company's sole shareholder, Telefónica. The Telefónica Group still consolidates the company using the full consolidation method.

Ifigenia Plus, S.A., which was fully consolidated in the financial statements of the Telefónica Group, was liquidated in 2006 and therefore removed from the consolidation scope.

The principal changes in the consolidation scope in 2005 are the following:

Latin America

The acquisitions of 100% of the Chilean and Argentine operators owned by BellSouth were concluded on January 7 and January 11, 2005, respectively, thereby completing the purchase of the Latin American cellular operators from BellSouth.

The total acquisition cost for Telefónica Móviles, adjusted for the outstanding net debt at these two operators, was 519 million euros for Radiocomunicaciones Móviles, S.A. (Argentina) and 318 million euros for Telefónica Móviles Chile, S.A.

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Europe

On June 10, 2005 the European Commission authorized Telefónica's bid to take over Czech operator Cesky Telecom a.s. by acquiring 51.1% of its share capital. The acquisition was completed on June 16 at a price of 502 Czech crowns per share. Telefónica then launched a tender offer for the remaining 48.9% of Cesky Telecom in the hands of minority shareholders. The tender offer closed on September 19, with Telefónica acquiring 58,985,703 shares at a price of 456 Czech crowns per share. In total, Telefónica paid 3,663 million euros in exchange for its interest in the Czech operator. After these acquisitions, Telefónica owned 69.41% of the company. The company was included in the Telefónica Group's consolidated scope by the full consolidation method.

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TELEF. EMISIONES OCTUBRE 06	EUR	3M	EUR	20000%	4.81%	300											30
TELEF. EMISIONES DECEMBER 06	GBP			5.89%	5.89%											682	68
TELEF. EMISIONES JANUARY 06																	
TRANCHE A	1xEUR	6M	EUR	0.83000%	0.83000%											55	5
TELEF. EMISIONES JANUARY 06																	
TRANCHE B	1xEUR	3M	EUR	0.70000%	0.70000%											24	2
TELEF. EMISIONES FEBRURARY 07	EUR			4.67%	4.67%											1,500	1,50
TELEF. EMISIONES MARCH 07	1xEUR	3M	EUR	0.13000%	0.13000%			350									35
TELEF. EMISIONES JUNE 07	CZK	PRIB_	CZK	0.1600%	4.24%					90							9
TELEF. EMISIONES JUNE B 07	CZK			4.35%	4.35%							113					11
TELEF. EMISIONES JUNE C 07	CZK			4.62%	4.62%											98	9
TELEF. EMISIONES JULY A 07	USD			5.86%	5.86%											509	50
TELEF. EMISIONES JULY B 07	USD	3M	USD	33000%	5.21%											577	57
TELEF. EMISIONES JULY C 07	USD			6.22%	6.22%											476	47
																	15,79
Total bonds								721	1,029	3,038	2,929	795	12,432	20,94			
Total issues:								721	1,829	3,054	2,929	795	12,532	21,86			

Foreign operators			Maturity (Nominal)					Subsequent	
Debt	Currency	% Interest rate	2008	2009	2010	2011	2012	years	Total
Marketable debentures	USD	9.125			144				144
Marketable debentures	USD	8.85				91			91
Marketable debentures	USD	8.85							
Marketable debentures	USD	9.125	85						85
TASA			85		144	91			320
Series F	UF	6	2	2	2	2	2	7	16
Series L	UF	3.75					80		80
CTC CHILE:			(2)	2	2	2	82	7	96
		91-day CETES +							
Peso bonds, Series A	MXN	0.61			500				500
Peso bonds, Series B	MXN	9.25					219		219
Telefónica Finanzas México					500		219		719
O2 sterling issue	GBP	7.625					511		511
O2							511		511
2.5% 2008 bond	CZK	3.5	225						225
Telefónica O2 Czech Republic			225						225
8 th issue T. Peru bonds	USD	3.8125		11					11
7 th issue T. Peru bonds	PEN	7.9375	14						14
T. Peru 1 st Program (2 nd)	PEN	VAC + 7		10					10
T. Peru 3 rd Program (1 st)	PEN	VAC + 5			11				11
T. Peru 4 th Program (10 th Series A)	PEN	7.875					7		7
T. Peru 4 th Program (10 th -Series B)	PEN	6.4375					12		12
T. Peru 4 th Program (12 th -Series A)	PEN	VAC + 3.6875						16	16
T. Peru 4 th Program (14 th -Series A)	PEN	6.375			11				11
T. Peru 4 th Program (16 th -Series A)	PEN	6					23		23
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T. Peru 4 th Program (19 th -Series A)	PEN	VAC + 3.625					16	16
T. Peru 4 th Program (36 th -Series A)	PEN	VAC + 3.6875					34	34
T. Peru 4 th Program (1 st)	PEN	5.5625	6					6
T. Peru 4 th Program (13 th -Series A)	PEN	5.5625		17				17
T. Peru 4 th Program (4 th -Series A)	PEN	6.625				18		18
T. Peru 4 th Program (7 th)	PEN	6.1875		12				12
T. Peru 4 th Program (7 th -Series B)	PEN	5.875		4				4
T. Peru 4 th Program (7 th -Series C)	PEN	5.5625			4			4
T. Peru 4 th Program (8 th -Series A)	PEN	7.375			7			7
T. Peru 4 th Program (8 th -Series B)	PEN	6.25			12			12
T. Peru 4 th Program (9 th -Series A)	PEN	6.9375				13		13
T. Peru 4 th Program (9 th -Series B)	PEN	6.375				20		20
T. Peru Senior Notes	PEN	8					171	171
Telefónica del Perú:			20	54	45	33	60	237
T.M. Peru 1 st Program (1 st Series A)	PEN	6.25		11				11
T.M. Peru 1 st Program (2 nd Series A)	PEN	7.0625				11		11
T.M. Peru 1 st Program (2 ^{db} Series B)	PEN	7.5625				6		6
T.M. Peru 1 st Program (2 nd Series C)	PEN	7.5625				10		10
T.M. Peru 1 st Program (3 rd Series A)	PEN	7.4375					8	8
T.M. Peru 1 st Program (3 rd Series B)	PEN	7.6875					5	5
T.M. Peru 1 st Program (8 th Series A)	PEN	6.4375			11			11
Telefónica Móviles Perú				11	11	27		13
Nonconvertible bonds	BRL	1.042 x CDI			153			153
Nonconvertible bonds	BRL	1.033 x CDI		38				38
Nonconvertible bonds	BRL	1.03 x CDI	96					96
Brasilcel Group			96	38	153			287
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Nonconvertible bonds	BRL	1 x CDI + 0.35000%							575	575
Telesp									575	575
Total issues			424	105	1,430	153	871	255		3,247
Total Group issues			1,149	1,935	4,485	3,083	1,667	12,787		25,107

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The detail and main features of outstanding debentures and bonds at December 31, 2006 were as follows (in millions of euros):

	Telefónica and special purpose vehicles	Currency	Interest rate	% Actual rate	2007	2008	2009	2010	2011	Subsequent years	Total
	Debentures and bonds:										
TSA	FEBRUARY 1990 SERIES C	EUR	12.60%	12.60%				4			4
	FEBRUARY 1990 SERIES F	EUR	12.58%	12.58%				10			10
	APRIL 1999	EUR	4.50%	4.50%			500				500
	JUNE 1999	EUR	4.15%	4.15%			300				300
	JULY 1999 zero coupon	EUR	6.37%	6.37%						47	47
	MARCH 2000	EUR	4.64%	4.64%						50	50
	APRIL 2000	EUR	5.63%	5.63%	500						500
	Debentures subtotal:				500		800	14		97	1,411
	MARCH 1998	EUR	4.84%	4.84%		421					421
T.E.BV	GLOBAL BOND	USD	7.75%	7.75%				1,898			1,898
	GLOBAL BOND	USD	8.25%	8.25%						949	949
	EMTN ISSUE (A Tranche)	EUR	5.13%	5.13%						1,500	1,500
	EMTN ISSUE (B Tranche)	EUR	5.88%	5.88%						500	500
EMISIONES	EMTN O2 EUR (I)	EUR	4.38%	4.38%						1,750	1,750
	EMTN O2 EURO (II)	EUR	3.75%	3.75%					2,250	0	2,250
	EMTN O2 GBP (I)	GBP	5.38%	5.38%						1,117	1,117
	EMTN O2 GBP (II)	GBP	5.38%	5.38%						745	745
		3M USD									
	TELEF. EMISIONES JUN 06 TRANCHE	LIBOR USD	+0.3%	5.67%			759			0	759
	TELEF. EMISIONES JUN 06 TRANCHE	USD	5.98%	5.98%					759	0	759
	TELEF. EMISIONES JUN 06 TRANCHE	USD	6.42%	6.42%						949	949
	TELEF. EMISIONES JUN 06 TRANCHE	USD	7.05%	7.05%						1,519	1,519
		3M EURIBOR									
	TELEF. EMISIONES JULY 06	EUR	+0.35%	3.88%				1,250			1,250
	TELEF. EMISIONES SEPTEMBER 06	EUR	4.39%	4.39%						500	500
		3M EURIBOR									
	TELEF. EMISIONES OCTOBER 06	EUR	+0.2%	3.75%		300					300
		GBP	5.89%	5.89%						745	745

TELEF. EMISIONES
DECEMBER 06

Bonds subtotal:		721	759	3,148	3,009	10,273	17,911
Total issues:	500	721	1,559	3,162	3,009	10,370	19,322

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			Maturity (Nominal)					Subsequent years	Total
Foreign operators Debentures and bonds	Currency	% Interest rate	2007	2008	2009	2010	2011		
Series F	UF	6	2	2	2	2	2	8	18
Series L	UF	3.75						78	78
CTC CHILE:			2	2	2	2	2	86	96
T. Peru 2 nd Program (5 th)	PEN	VAC+6.25	3						3
T. Peru 3 rd Program (1 st)	PEN	VAC+5				12			12
T. Peru 3 rd Program (2 nd Series A)	PEN	5.3125	7						7
T. Peru 3 rd Program (3 rd)	PEN	8.125	7						7
T. Peru 3 rd Program (5 th -Series A)	PEN	5.5	16						16
T. Peru 4 th Program (1 st)	PEN	5.5625		6					6
T. Peru 4 th Program (10 th -Series A)	PEN	7.875						7	7
T. Peru 4 th Program (10 th Series B)	PEN	6.4375						12	12
T. Peru 4 th Program (7 th)	PEN	6.1875			12				12
T. Peru 4 th Program (7 th -Series B)	PEN	5.875			4				4
T. Peru 4 th Program (8 th -Series A)	PEN	7.375				7			7
T. Peru 4 th Program (8 th -Series B)	PEN	6.25				12			12
T. Peru 4 th Program (9 th -Series A)	PEN	6.9375					14		14
T. Peru 4 th Program (8 th -Series B)	PEN	6.375					21		21
8 th issue T. Peru bonds	USD	3.8125			13				13
9 th issue T. Peru bonds	USD	3.125	15						15
7 th issue T. Peru bonds	PEN	7.9375		15					15
T. Peru Senior Notes	PEN	8						179	179
T. Peru 1 st Program (2 nd)	PEN	VAC+7			11				11
T. Peru securitized bonds	USD	7.48							
Telefónica del Perú:			48	21	40	31	35	198	372

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T.M. Peru 1 st Program (1 st Series A)	PEN	6.25		12					12
T.M. Peru 1 st Program (2 nd Series A)	PEN	7.0625				12			12
T.M. Peru 1 st Program (2 ^{db} Series B)	PEN	7.5625				6			6
T.M. Peru 1 st Program (2 nd Series C)	PEN	7.5625				11			11
T.M. Peru 1 st Program (3 rd Series A)	PEN	7.4375					8		8
T.M. Peru 1 st Program (3 rd Series B)	PEN	7.6875					5		5
T.M. Peru 1 st Program (8 th Series A)	PEN	6.4375			11				11
4 th issue T.M. Peru bonds	USD	5.25	23						23
5 th issue 1 st Program T.M. Peru	USD	5.3125	23						23
Telefónica Móviles Perú			46	12	11	29	13		111
Marketable debentures	USD	11.875	144						144
Marketable debentures	ARS SURVEY+2.5		12						12
Marketable debentures	USD	9.125		95					95
Marketable debentures	USD	9.125			161				161
Marketable debentures	USD	8.85				102			102
TASA			156	95	161	102			514
Marketable debentures	USD	9.75	6						6
Telefónica Holding Argentina			6						6
Peso bonds, Series A	MXN	91-day CETES+0.61			558				558
Peso bonds, Series B	MXN	9.25					244		244
Telefónica Finanzas México					558		244		802
Nonconvertible bonds Telesp	BRL	103.5% CDI	533						533
TELESP			533						533
Nonconvertible bonds Brasilcel	BRL	104.4% CDI	89						89
Nonconvertible bonds Brasilcel	BRL	104.2% CDI			142				142
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Nonconvertible bonds	BRL	103.3% CDI			36				36
Brasilcel Group			89		36	142			266
O2 euro issue	EUR	6.375	1,000						1,000
O2 sterling issue	GBP	7.625					558		558
MmO2			1,000				558		1,558
3.5% 2008 bond	CZK	3.50		218					218
Cesky Telecom				218					218
Total issues			1,880	336	90	905	168	1,100	4,479
Total Group issues			2,380	1,057	1,648	4,067	3,177	11,470	23,799

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The main features of the bonds and debentures issued in 2007 are as follows:

Telefónica Emisiones, a subsidiary of Telefónica, held the following four issues under its EMTN program registered with the London Stock Exchange on July 8, 2005 and renewed on July 3, 2007:

Item	Date	Nominal value (millions of euros)⁽¹⁾	Currency of issuance	Maturity	Interest rate
EMTN bonds	01/31/2007	55	EUR	12/31/2021	6-month Euribor + 0.83% p.a.
		24	EUR	12/31/2018	3-month Euribor + 0.7% p.a.
EMTN bonds	02/07/2007	1,500	EUR	02/07/2014	4.674%
EMTN bonds	03/30/2007	350	EUR	03/30/2009	3-month Euribor + 0.13% p.a.
EMTN bonds	06/19/2007	98	CZK	06/19/2010	CZK 3-month Pribor + 0.16%
		112	CZK	06/19/2012	4.351%
		90	CZK	06/16/2014	4.623%

⁽¹⁾ Exchange rate at
December 31,
2007.

Bonds issued by Telefónica Emisiones, S.A.U., under the shelf program filed with the Securities Exchange Commission (SEC) in the US on April 12, 2006 and renewed on July 2, 2007:

Item	Date	Nominal value (millions of euros)⁽¹⁾	Currency of issuance	Maturity	Interest rate
Global bond	07/02/2007	509	USD	02/04/2013	5.855%
		577	USD	02/04/2013	3M Libor + 0.33%
		476	USD	07/03/2017	6.221%

- (1) Exchange rate at
December 31,
2007.

Bonds issued by Telefónica Europe, B.V. under its bond issue program registered with the Tokyo Stock Exchange (TSE) on July 11, 2007:

Item	Date	Nominal value (millions of euros)⁽¹⁾	Currency of issuance	Maturity	Interest rate
EMTN bonds	07/19/2007	91	JPY	07/19/2012	2.11%
		91	JPY	07/19/2012	6M Libor + 0.4% p.a.

- (1) Exchange rate at
December 31,
2007.

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Issues by Telefónica del Perú, S.A.A.:

Item	Date	Nominal value (millions of euros)⁽¹⁾	Currency of issuance	Maturity	Interest rate
Bonds	01/11/2007	17	PEN	01/11/2009	5.56%
Bonds	03/12/2007	23	PEN	03/12/2012	6.00%
Bonds	04/13/2007	4	PEN	04/13/2010	5.56%
Bonds	07/13/2007	14	PEN	07/13/2027	VAC+3.625%
Bonds	10/12/2007	18	PEN	10/12/2012	6.63%
Bonds	10/23/2007	34	PEN	10/23/2017	VAC +3.6875%
Bonds	11/20/2007	11	PEN	11/20/2010	6.38%
Bonds	11/30/2007	14	PEN	11/30/2019	VAC +3.6875%

⁽¹⁾ Exchange rate at
December 31,
2007.

The main issues in 2006 were:

Bonds issued by Telefónica Emisiones, S.A.U. under its EMTN program registered with the London Stock Exchange on July 8, 2005, renewed on July 5, 2006 and July 3, 2007:

Item	Date	Nominal value (millions of euros)⁽¹⁾	Currency of issuance	Maturity	Interest rate
EMTN bonds	02/02/2006	2,250	EUR	02/02/2011	3.750%
EMTN bonds	02/02/2006	1,750	EUR	02/02/2016	4.375%
EMTN bonds	02/02/2006	1,117	GBP	02/02/2018	5.375%
EMTN bonds	02/02/2006	745	GBP	02/02/2026	5.375%
EMTN bonds	07/25/2006	1,250	EUR	01/25/2010	3M Euribor + 0.35%
EMTN bonds	10/17/2006	500	EUR	04/17/2012	4.393% 3M Euribor
EMTN bonds	10/30/2006	300	EUR	10/30/2008	+0.20%

EMTN bonds	12/28/2006	745	GBP	01/31/2014	5.888%
(1) Exchange rate at December 31, 2006.					

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Bonds issued by Telefónica Emisiones, S.A.U., under the shelf program filed with the Securities Exchange Commission (SEC) in the US on April 12, 2006:

Item	Date	Nominal value (millions of euros)⁽¹⁾	Currency of issuance	Maturity	Interest rate 3M Libor
Global bond	06/20/2006	759	USD	06/19/2009	+0.30%
Global bond	06/20/2006	759	USD	06/20/2011	5.984%
Global bond	06/20/2006	949	USD	06/20/2016	6.421%
Global bond	06/20/2006	1,519	USD	06/20/2036	7.045%

⁽¹⁾ Exchange rate at December 31, 2006.

Bonds issued by Telefónica del Perú, S.A.A, under its fourth debt program registered with the Lima Stock Exchange on April 12, 2006:

Item	Date	Nominal value (millions of euros)	Currency of issuance	Maturity	Interest rate
T.Peru 4 th Program (8 th -Series A)	07/05/2006	7	PEN	07/05/10	7.3750%
T.Peru 4 th Program (10 th -Series A)	07/05/2006	7	PEN	07/05/12	7.8750%
T.Peru 4 th Program (9 th -Series A)	08/07/2006	14	PEN	08/07/11	6.9375%
T.Peru 4 th Program (7 th -Series A)	09/07/2006	12	PEN	09/04/09	6.1875%
T.Peru 4 th Program (8 th -Series B)	11/03/2006	12	PEN	11/03/10	6.2500%
T.Peru 4 th Program (10 th -Series B)	11/17/2006	12	PEN	11/17/12	6.4375%
T.Peru 4 th Program (1 st -Series A)	11/17/2006	6	PEN	11/17/08	5.5600%
T.Peru 4 th Program (7 th -Series B)	12/06/2006	4	PEN	12/07/09	5.8750%
T.Peru 4 th Program (9 th -Series B)	12/06/2006	21	PEN	12/06/11	6.3750%

⁽¹⁾ Exchange rate at December 31, 2006.

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Bonds issued by Telefónica Móviles Perú, under its first debt program registered with the Lima Stock Exchange on February 1, 2006:

Item	Date	Nominal value (millions of euros)⁽¹⁾	Currency of issuance	Maturity	Interest rate
Móviles Peru 1 st Program (1 st -Series A)	02/07/2006	12	PEN	02/07/2009	6.25%
Móviles Peru 1 st Program (2 nd -Series A)	02/14/2006	12	PEN	02/14/2011	7.0625%
Móviles Peru 1 st Program (5 th -Series A)	02/14/2006	23	USD	08/14/2007	5.3125%
Móviles Peru 1 st Program (3 rd -Series A)	02/22/2006	8	PEN	02/22/2013	7.4375%
Móviles Peru 1 st Program (4 th -Series A)	02/22/2006	23	USD	05/22/2007	5.2500%
Móviles Peru 1 st Program (3 rd -Series B)	03/13/2006	5	PEN	03/13/2013	7.6875%
Móviles Peru 1 st Program (2 nd -Series B)	06/01/2006	6	PEN	06/01/2011	7.5625%
Móviles Peru 1 st Program (2 nd -Series C)	07/19/2006	11	PEN	07/19/2011	7.5625%
Móviles Peru 1 st Program (8 th -Series A)	09/13/2006	11	PEN	09/13/2010	6.4375%

⁽¹⁾ Exchange rate at
December 31,
2006.

Bonds issued by Telefónica Finanzas México, S.A. de C.V., under the peso bond issue program filed with the Mexican securities regulator (CNBV for its initials in Spanish) on December 30, 2004:

Item	Date	Nominal value (millions of euros)⁽¹⁾	Currency of issuance	Maturity	Interest rate
Peso bonds (retapping of the Telfim 05)	02/10/2006	558	MXN	09/24/2010	91-day Cetes + 0.61%
Peso bonds (retapping of the Telfim 05-2)	02/10/2006	244	MXN	09/21/2012	9.25%

⁽¹⁾ Exchange rate at
December 31,
2006.

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Bonds issued by Telefónica Chile, S.A. under the 015 line of trade financing (*efectos de comercio*) registered with the Chilean securities market regulator on May 12, 2004:

Item	Date	Nominal value (millions of euros)⁽¹⁾	Currency of issuance	Maturity	Interest rate
Local bond (Series L)	03/29/2006	78	UF	10/25/12	3.75%

⁽¹⁾ Exchange rate at December 31, 2006.

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The breakdown of financial instruments arranged by the Group (notional amount) by currency and interest rates at December 31, 2007 is as follows:

	Millions of euros						Fair value			
	2008	2009	2010	2011	2012	Subsequent years	Total	Underlying debt	Associated derivatives	Total
EURO	3,256	(17)	1,799	8,610	2,569	11,005	27,222	23,370	3,862	27,232
Floating rate	1,227	(999)	(307)	4,412	(1,488)	5,142	7,987	5,901	1,523	7,424
Spread Ref										
Euribor	(0.28%)	0.13%	(0.68%)	0.21%	0.34%	0.00%	0.10%			
Fixed rate	629	(68)	2,106	2,998	(293)	5,863	11,235	9,339	2,491	11,830
Interest rate	3.79%	(3.93%)	7.14%	3.59%	6.59%	4.56%	4.74%			
Rate cap	1,400	1,050		1,200	4,350		8,000	8,130	(152)	7,978
OTHER										
EUROPEAN										
CURRENCIES	(1,877)	2,102	2,106	845	3,487	2,814	9,477	5,971	3,485	9,456
Instruments in										
CZK	1,669	561	708		113	98	3,149	360	2,772	3,132
Floating rate	(45)		281				236	46	191	237
Spread	(0.06%)	0.00%	0.07%	0.00%	0.00%	0.00%	0.10%			
Fixed rate	1,714	561	427		113	98	2,913	314	2,581	2,895
Interest rate	4.13%	3.15%	3.35%	0.00%	4.35%	4.62%	3.85%			
Rate cap										
Instruments in										
GBP	(3,546)	1,541	1,398	845	3,374	2,716	6,328	5,611	713	6,324
Floating rate	(205)	1,200	1,398	108	2,181	(682)	4,000	469	3,494	3,963
Spread	0.13%	0.02%	(0.01%)	3.35%	0.28%	0.00%	0.19%			
Fixed rate	(3,818)	341		737	511	2,034	(195)	2,585	(2,781)	(196)
Interest rate	6.19%	5.59%	0.00%	5.12%	7.63%	6.06%	8.78%			
Rate cap	477				682	1,364	2,523	2,557		2,557
AMERICA	3,906	957	1,697	448	357	1,414	8,779	13,689	(5,569)	8,120
Instruments in										
USD	(391)	(68)	122	135	40	1,694	1,532	10,726	(9,768)	958
Floating rate	163	(695)	118	(14)	6	672	250	2,367	(2,132)	235
Spread	1.12%	44.69%	(0.00%)	77.37%	(0.25%)	0.00%	(1.03%)			
Fixed rate	(563)	(62)	(5)	140	25	984	519	7,578	(7,635)	(57)
Interest rate	10.28%	5.79%	(119.61%)	9.26%	3.85%	10.95%	12.79%			
Rate cap	9	689	9	9	9	38	763	781	(1)	780
Instruments in										
UYU		2	2	2			6	5		5
Floating rate										
Spread	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%			

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	Millions of euros					Subsequent	Fair value			
	2008	2009	2010	2011	2012	years	Total	Underlying	Associated	Total
								debt	derivatives	
Fixed rate		2	2	2			6	5		5
Interest rate	8.83%	3.75%	3.75%	3.75%	0.00%	0.00%	3.93%			
Rate cap										
Instruments										
in ARS	468	256	153				877	101	774	875
Floating rate	22						22	21		21
Spread	1.15%	0.00%	0.00%	0.00%	0.00%	0.00%	1.15%			
Fixed rate	446	256	153				855	80	774	854
Interest rate	10.20%	9.22%	9.12%	0.00%	0.00%	0.00%	9.71%			
Rate cap										
Instruments										
in BRL	140	208	822	94	92	200	1,556	305	1,134	1,439
Floating rate	(774)	153	794	66	64	151	454	138	375	513
Spread	0.47%	(2.42%)	0.21%	3.59%	3.60%	0.00%	0.98%			
Fixed rate	914	55	28	28	28	49	1,102	167	759	926
Interest rate	9.51%	10.65%	10.17%	10.17%	10.17%	10.15%	9.65%			
Rate cap										
Instruments										
in CLP	53	184	31	181	42		491	12	488	500
Floating rate	(17)	132	31	158	42		346	139	144	283
Spread	0.27%	0.05%	0.38%	0.07%	0.38%	0.00%	0.12%			
Fixed rate	70	52		23			145	(127)	344	217
Interest rate	3.43%	6.63%	0.00%	3.35%	0.00%	0.00%	4.57%			
Rate cap										
Instruments										
in UFC	117	90	98	99	82	7	493	177	326	503
Floating rate			95				95	95		95
Spread	0.00%	0.00%	0.33%	0.00%	0.00%	0.00%	0.33%			
Fixed rate	117	90	3	99	82	7	398	82	326	408
Interest rate	2.55%	3.55%	6.56%	4.28%	3.80%	6.00%	3.55%			
Rate cap										
Instruments										
in PEN	132	136	81	72	80	338	839	639	215	854
Floating rate										
Spread	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%			
Fixed rate	132	136	81	72	80	338	839	639	215	854
Interest rate	8.58%	5.95%	6.42%	6.90%	6.68%	6.81%	6.91%			
Rate cap										
Instruments										
in COP	589	222	36	22	26	29	924	412	472	884
Floating rate	12	17	36	22	26	29	142	104		104
Spread	0.00%	0.00%	1.32%	0.00%	0.00%	0.00%	0.34%			
Fixed rate	577	205					782	308	472	780
Interest rate	11.49%	0.01%	0.00%	0.00%	0.00%	36.00%	7.65%			

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	Millions of euros						Fair value			
	2008	2009	2010	2011	2012	Subsequent years	Total	Underlying debt	Associated derivatives	Total
Rate cap										
Instruments in UVR	3,481	(146)	(151)	(157)	(224)	(854)	1,949	1,949		1,949
Floating rate										
Spread	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%			
Fixed rate	3,481	(146)	(151)	(157)	(224)	(854)	1,949	1,949		1,949
Interest rate	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%			
Rate cap										
Instruments in VEB	(1,341)						(1,341)	(1,341)		(1,341)
Floating rate										
Spread	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%			
Fixed rate	(1,341)						(1,341)	(1,341)		(1,341)
Interest rate	8.16%	0.00%	0.00%	0.00%	0.00%	0.00%	8.16%			
Rate cap										
Instruments in MXN	656	73	503		219		1,451	714	778	1,492
Floating rate	(39)	70	314				345	478	78	556
Spread	0.02%	2.59%	0.61%	0.00%	0.00%	0.00%	1.08%			
Fixed rate	695	3	189		219		1,106	236	700	936
Interest rate	7.81%	8.83%	8.17%	0.00%	9.25%	0.00%	8.16%			
Rate cap										
Instruments in GTQ	2						2	(10)	12	2
Floating rate										
Spread	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%			
Fixed rate	2						2	(10)	12	2
Interest rate	23.70%	0.00%	0.00%	0.00%	0.00%	0.00%	23.70%			
Rate cap										
ASIA								622	(661)	(39)
Instruments in JPY								622	(661)	(39)
Floating rate								151	(152)	(1)
Spread	3.79%	3.79%	3.79%	3.79%	0.00%	0.00%	3.79%			
Fixed rate								471	(509)	(38)
Interest rate	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%			
Rate cap										
AFRICA					88		88		85	85
Instruments in MAD					88		88		85	85
Floating rate										
Spread	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%			
Fixed rate					88		88		85	85
Interest rate	0.00%	0.00%	0.00%	0.00%	4.54%	0.00%	4.54%			

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	Millions of euros						Fair value			
	2008	2009	2010	2011	2012	Subsequent years	Total	Underlying debt	Associated derivatives	Total
Rate cap										
TOTAL	5,285	3,042	5,602	9,903	6,501	15,233	45,566	43,652	1,202	44,854
Floating rate	344	(122)	2,760	4,752	831	5,312	13,877	9,909	3,521	13,430
Fixed rate	3,055	1,425	2,833	3,942	629	8,519	20,403	22,275	(2,166)	20,109
Rate cap	1,886	1,739	9	1,209	5,041	1,402	11,286	11,468	(153)	11,315
Currency options							(52)		(52)	
Other							(230)			

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(Euros)		MATURITIES			
Interest rate options	2008	2009	2010	2011	2012+
Collars					
Notional bought	1,884,741,996	2,522,100,000		900,000,000	1,847,524,908
Strike Cap	4.195%	3.925%		3.944%	4.715%
Strike Floor	3.460%	2.749%		3.189%	3.804%
Notional sold					
Strike Cap					
Strike Floor					
Caps					
Notional bought	5,400,000,000			300,000,000	6,231,756,204
Strike	4.748%			4.070%	4.470%
Notional sold	1,884,741,996	2,522,100,000		1,200,000,000	8,079,281,112
Strike	4.837%	4.847%		4.555%	5.298%
Floors					
Notional bought	477,229,343	2,872,100,000		900,000,000	1,663,512,408
Strike	2.500%	0.013%		1.000%	1.205%
Notional sold	4,000,000,000	350,000,000	518,685,530		700,000,000
Strike	2.750%	2.700%	4.568%		2.146%

(Euros)		MATURITIES			
Currency options	2008	2009	2010	2011	2012+
Call USD/Put BRL					
Notional amount of options bought		135,860,336			
Strike		2.1585			
Notional amount of options sold		196,239,298			
Strike		2.5587			
Put USD / Call BRL					
Notional amount of options sold		135,860,336			
Strike		1.8585			
Call EUR / Put USD					
Notional amount of options bought	27,832,084				
Strike	1.2780				
Put USD / Call EUR					
Notional amount of options bought	438,659,058				1,714,557,435
Strike	1.4454				1.3618
Notional amount of options sold					831,255,453
Strike					1.2030

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The breakdown of financial instruments arranged by the Group by currency and interest rates at December 31, 2006 is as follows:

	Millions of euros						Fair value			
	2007	2008	2009	2010	2011	Subsequent	Total	Underlying	Associated	Total
EURO	691	1,915	3,632	3,342	8,630	years	12,234	30,444	debt	derivatives
Floating rate	(6,808)	(5,472)	2,430	1,236	4,762	4,992	1,140	7,194	(6,500)	694
Spread	(0.00%)	0.00%	0.40%	0.70%	0.30%	0.62%	0.39%			
Fixed rate	7,499	480	(198)	2,106	2,968	6,042	18,897	10,539	9,113	19,652
Interest rate	4.44%	4.24%	0.77%	7.14%	3.66%	4.82%	4.77%			
Rate cap		6,907	1,400		900	1,200	10,407	10,730	(97)	10,633
OTHER										
EUROPEAN										
CURRENCIES	577	612	1,362	2,162	806	7,150	12,669	8,801	4,003	12,804
Instruments in										
CZK	464	107	543	598		256	1,968	119	1,850	1,969
Floating rate	601			272			873		872	872
Spread				0.02%			0.01%			
Fixed rate	(137)	107	543	326		256	1,095	119	978	1,097
Interest rate	3.75%	3.17%	3.15%	3.26%		3.50%	3.19%			
Rate cap										
Instruments in										
GBP	113	505	819	1,564	806	6,894	10,701	8,682	2,153	10,835
Floating rate	453	(439)	819	1,564		3,872	6,269	5,356	979	6,335
Spread	1.56%	(0.04%)	0.24%	0.26%		0.37%	0.76%			
Fixed rate	(340)	423			806	3,022	3,911	2,802	1,178	3,980
Interest rate	4.65%	5.00%			5.12%	5.87%	5.73%			
Rate cap		521					521	524	(4)	520
AMERICA	144	1,372	1,373	1,215	507	4,624	9,235	13,914	(5,074)	8,840
Instruments in										
USD	(970)	209	779	280	143	1,133	1,574	10,753	(9,175)	1,578
Floating rate	(601)	(25)	(53)	130			(549)	2,711	(3,093)	(382)
Spread	(0.30%)	(1.88%)	2.40%	0.09%			(0.20%)			
Fixed rate	(368)	222	63	139	133	1,080	1,269	7,357	(6,067)	1,290
Interest rate	2.47%	7.41%	4.87%	11.03%	11.13%	8.62%	10.53%			
Rate cap		11	770	11	11	51	854	685	(15)	670
Instruments in										
UYU		2	1	1	2		6	6		6
Floating rate										
Spread										
Fixed rate		2	1	1	2		6	6		6
Interest rate	3.75%	3.75%	3.75%	3.75%	3.75%		3.75%			
Rate cap										

Instruments in

ARS	322	251	88	19	0		680	(1)	706	705
Floating rate	79						79		78	78
Spread										
Fixed rate	231	251	88	19	0		589	(13)	628	615
Interest rate	10.76%	11.22%	11.43%	11.10%	10.38%		11.07%			
Rate cap	12						12	12		12

Instruments in

BRL	796	409	112	168	4	4	1,493	397	1,102	1,499
Floating rate	353	115	112	168	4	4	756	397	297	694
Spread	(0.81%)	(2.96%)	(3.06%)	0.08%	1.66%		(1.25)%			
Fixed rate	443	294					737		805	805
Interest rate	15.99%	12.45%					14.58%			
Rate cap										

Instruments in

CLP	(40)	156	101	33	165	44	459	38	431	469
Floating rate	4	17	48	33	165	44	311	153	169	322
Spread		(0.28%)	0.15%	0.38%	0.07%	0.38%	0.14%			
Fixed rate	(44)	138	54				148	(114)	261	147
Interest rate	6.41%	4.80%	5.07%				4.42%			
Rate cap										

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	Millions of euros						Fair value			
	2007	2008	2009	2010	2011	Subsequent years	Total	Underlying debt	Associated derivatives	Total
Instruments in UFC	3	132	171	96	119	86	607	192	424	616
Floating rate				93			93	94		94
Spread				0.45%			0.45%			
Fixed rate	3	132	171	3	119	86	514	98	424	522
Interest rate	6.49%	2.57%	3.46%	6.49%	4.22%	3.97%	3.52%			
Rate cap										
Instruments in PEN	208	89	40	57	67	273	734	546	239	785
Floating rate	6	8					14		14	14
Spread										
Fixed rate	202	81	40	57	67	273	720	546	225	771
Interest rate	6.88%	6.51%	6.40%	6.40%	6.93%	7.81%	7.13%			
Rate cap										
Instruments in COP	445	117			7	414	983	537	446	983
Floating rate	184				3	123	310	127	181	308
Spread	(0.00)%				2.00%	4.45%	1.78%			
Fixed rate	261	117			4	291	673	410	265	675
Interest rate	10.99%	8.04%			9.50%	5.50%	8.10%			
Rate cap										
Instruments in UVR						2,426	2,426	1,896		1,896
Floating rate										
Spread										
Fixed rate						2,426	2,426	1,896		1,896
Interest rate						4.00%	4.00%			
Rate cap										
Instruments in VEB	(1,000)						(1,000)	(1,000)		(1,000)
Floating rate										
Spread										
Fixed rate	(1,000)						(1,000)	(1,000)		(1,000)
Interest rate	5.69%						5.69%			
Rate cap										
Instruments in MXN	379	7	81	561		244	1,272	563	740	1,303
Floating rate	590	4	78	350			1,022	563	461	1,024
Spread	(0.01%)	(0.52%)	2.59%	0.61%			0.40%			
Fixed rate	(211)	3	3	211		244	250		279	279
Interest rate	5.46%	8.83%	8.83%	8.17%		9.25%	11.52%			
Rate cap										
Instruments in GTQ	1						1	(12)	12	
Floating rate	13						13		12	12

Spread										
Fixed rate	(12)					(12)	(12)			(12)
Interest rate	2.00%					2.00%				
Rate cap										
ASIA	1	(3)				(2)	366	(374)		(8)
Instruments										
in JPY	1	(3)				(2)	366	(374)		(8)
Floating rate	1					1	98	(98)		
Spread										
Fixed rate		(3)				(3)	268	(276)		(8)
Interest rate		(0.00%)		2.30%		(0.00)%				
Rate cap										
AFRICA						90	90		90	90
Instruments										
in MAD						90	90		90	90
Floating rate										
Spread										
Fixed rate						90	90		90	90
Interest rate						4.54%	4.54%			
Rate cap										
TOTAL	1,413	3,896	6,367	6,719	9,943	24,097	52,435	51,543	1,162	52,705
Total										
floating rate	(5,126)	(5,793)	3,434	3,846	4,935	9,034	10,330	16,691	(6,626)	10,065
Total fixed										
rate	6,528	2,247	763	2,862	4,098	13,812	30,310	22,902	7,903	30,805
Total rate										
cap	12	7,439	2,170	11	911	1,252	11,795	11,951	(116)	11,835
Currency										
options	(17)						(17)		(17)	
Other							(273)			

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INTEREST RATE OPTIONS (Euros)
MATURITIES

	2007	2008	2009	2010	2011	2012+
Collars						
Notional amount bought	12,399,000	7,439,279,505	2,169,847,296	10,545,853	910,545,853	52,729,267
Strike Cap	12.50%	2.83%	3.72%	4.25%	3.96%	4.25%
Strike Floor	4.50%	2.32%	2.75%	3.00%	3.19%	3.00%
Notional amount sold						1,500,000,000
Strike Cap						6.82%
Strike Floor						4.18%
Caps						
Notional amount sold		7,428,733,651	2,169,847,296		900,000,000	
Strike		4.26%	4.62%		4.55%	
Floors						
Notional amount bought		7,421,221,000	2,169,847,296		900,000,000	
Strike		1.11%	0.01%		1.00%	
Notional amount sold						700,000,000
Strike						2.15%

CURRENCY OPTIONS (Euros)
MATURITIES

	2007	2008	2009	2010	2011	2012+
Call USD / Put ARS						
Notional amount of options bought		148,357,173				
Strike		3.1356				
Notional amount of options sold		18,381,195				
Strike		3.4800				
Call EUR / Put USD						
Notional amount of options bought		212,177,910				
Strike		1.2643				
Notional amount of options sold		176,678,815				
Strike		1.3150				
Put USD / Call EUR						
Notional amount of options bought		602,126,044				

Strike

1.3158

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Table of Contents**APPENDIX IV DETAILS OF SUBSIDIARIES, ASSOCIATES AND INVESTEEES AT DECEMBER 31, 2007**
(millions of euros)

	OWNERSHIP STAKE				
	TELEFÓNICA		INTERIM		
THEIR INVESTMENTS	DIRECT	INDIRECT	GROUP CAPITAL	RESERVE	RESIDUAL
S.A.U. (SPAIN) (*) (**) (1) (6) (9)	100.00%	100.00%	1,024	1,870	
Communications services in Spain					
Madrid					
Telefónica y Comunicaciones de España, S.A.U. (SPAIN) (*) (**) (3)	100.00%	100.00%	6	8	
Systems, networks and infrastructure engineering					
- Pl. 9ª - 28020 Madrid					
Telefonos Chile, S.A.C. (CHILE)	N/D	N/D	N/D	N/D	N/D
Engineering activities					
Providencea Santiago de Chile					
Outsourcing, S.A. (SPAIN) (*) (**) (3)	100.00%	100.00%	1		
and marketing					
Consultoriales, S.A. (SPAIN) (*) (**) (4)	100.00%	100.00%	14	(3)	
business consulting services					
2007					
Telefónica (N) (*) (**) (4)	100.00%	100.00%		1	
Director					
2007					
Telefónica de Servicios de Telecomunicaciones, S.A. (SPAIN)	50.00%	50.00%			
Services, installation and telecommunications services Parque industrial y					
del Aljarafe Sevilla					
Telecomunicaciones, S.A. (SPAIN) (1)	49.00%	49.00%	3		
and telecommunications					
Porto Madrid- Barajas. Ed. Servicios Generales Pl 2 Of. 246. Madrid					
Telefónica, S.L. (SPAIN)	40.00%	40.00%			
Work installation and maintenance					
Ceuta					
Telefónica Usuarios Múltiples, S.A. (SPAIN)	33.33%	33.33%	1	2	
Outsourcing					
2036 Madrid					
Telefónica de Sist. y Servicios Avanzados de Telecom., S.A. (TISSAT) (SPAIN) (2)	30.77%	30.77%	1	2	
Services engineering and marketing					
Valencia, 5 Parque Tecnológico de Paterna- 46980 Paterna, Valencia					
	16.00%	16.00%	1		
Service in Cantabria					
Telefónica					
Telefónica (N) (SPAIN)	5.17%	5.17%	3	(1)	
Telefónica companies					
Telefónica					
Telefónica E.C.R. (SPAIN)	5.17%	5.17%	3		

ial companies

lona

A. (SPAIN)

5.00% 5.00% 6 1

0 - Barcelona

unicaciones, S.A. (TELYCO) (SPAIN) (*) (**) (1)

100.00% 100.00% 3 3

and distribution of telephone and telematic equipment and services

- 28027 Madrid

(MOROCCO) (1)

54.00% 54.00% 1 1

and distribution of telephone services

, 1,B. Sidi Maarouf Casablanca

aciones Públicas, S.A. (SPAIN) (*) (**) (1)

100.00% 100.00% 1 68

ephones

ertrán, 7 - 28020 Madrid

(*) Companies
included in the
2006
consolidated tax
statement.

(**) Companies
included in the
2007
consolidated tax
statement.

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	OWNERSHIP STAKE					
	TELEFÓNICA			INTERIM		
AND THEIR INVESTMENTS	DIRECT	INDIRECT	GROUP	CAPITAL	RESERVE	DEFICIT
A. (SPAIN)	51.00%	51.00%				
ation of telecommunications and public television services						
- Nave Industrial 15 - San Sebastián de los Reyes Madrid						
(SPAIN) (2)	20.00%	20.00%	40.00%	2	5	
Madrid						
	N/A	N/A	N/A	N/A	N/A	N/A
AIN) (5)	51.00%	51.00%	20	(6)		(
unications operator						
B - 28037 Madrid						
s, S.A. (SPAIN)	100.00%	51.00%				
A. (SPAIN) (*) (**) (7)	100.00%	100.00%	3	(29)		
ation services provider						
2 - Ciudad de la Imagen (*) - 28223 Madrid						
norca, S.A. (SPAIN) (*) (**) (1)	100.00%	100.00%	1			
ems and value-added services						
ajal, 13 - Mahón Menorca						
España, S.A.U. (SPAIN) (*) (**) (1)	100.00%	100.00%	423	508		2,4
ations services provider						
lencia, 6 - Pta. 5 - 28001 Madrid						
B.V. (NETHERLANDS) (1)	100.00%	100.00%	39	(38)		
- 1077ZX Amsterdam						
TZERLAND) (9)	100.00%	100.00%				
perator						
Zurich						
A. (SPAIN)	13.36%	13.36%	4			
t services through wireless telephony						
lcobendas Madrid						
omain Ltd. (IRELAND) (7)	6.00%	6.00%	12			
main registration service						
lsfort Terrace Dublin 2						
B.V. (NETHERLANDS) (1)	100.00%	100.00%	881	(1,648)		1
- 1077ZX Amsterdam						
ALY)	39.92%	39.92%	13	(584)		(1,2
ation of 3G wireless communications systems						
ri, 70 - Rome						
(MOROCCO) (1)	32.18%	32.18%	234	(7)		2
tions services provider						
Angle Bd Zertouni et El Massira El Kadra Casablanca						
Ltd. (BRAZIL) (7)	100.00%	100.00%	6	(6)		

<i>ro ou Distrito FLAMENGO, Rio de Janeiro</i>						
ón en Aplicaciones Móviles, S.A. (SPAIN)	43.69%	43.69%	1	(2)		
<i>nt and commercial operation of wireless services and applications.</i>						
<i>o s/n Castelldefels Barcelona</i>						
ional, S.A. (SPAIN) (*) (**) (1) (6) (9)	100.00%	100.00%	2,839	9,339		1,6
<i>ecommunications industry abroad</i>						
<i>013 Madrid</i>						
imiento Holding S.A. (ESPAÑA)	100.00%	100.00%				
unicaciones, S.A. ESP (COLOMBIA) (1)	52.03%	52.03%	307	(528)		(10
<i>ices operator</i>						
icações Holding, Ltda. (BRAZIL) (1)	100.00%	100.00%	1,511	(22)	(33)	8

arvalho, 851 20º andar, parte, Sao Paulo

(*) Companies
included in the
2006
consolidated tax
statement.

(**) Companies
included in the
2007
consolidated tax
statement.

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	OWNERSHIP STAKE							GROSS BONDS CO
	TELEFÓNICA	INTERIM	RESERVE	IDENTITY	RESULTS	SALARY		
COMPANIES AND THEIR INVESTMENTS	DIRECT	INDIRECT	GROUP CAPITAL	SERVICES	IDENTITY	RESULTS	SALARY	
Telefônica de São Paulo, S.A. - TELES P (BRAZIL) (1) (11) <i>telephony operator in Sao Paulo</i>	87.95%	87.95%	2,515	1,522	(1,123)	990		
Telefônica de São Paulo, S.A. (BRAZIL) (1) (11) <i>and fixed telephony operator in Sao Paulo</i>	100.00%	87.95%	159	1		26	N/D	
Telefônica de São Paulo, S.A. (BRAZIL) (1) (11) <i>iniano de Carvalho, 851 20º andar, parte, Sao Paulo</i>								
Telefônica de São Paulo, S.A. (BRAZIL) (1) (11) <i>of commercal underground network</i>	50.00%	43.98%	88			(3)	N/D	
Telefônica de São Paulo, S.A. (BRAZIL) (1) (11) <i>ational</i>	50.00%	43.98%					N/D	
Telefônica de São Paulo, S.A. (BRAZIL) (1) (11) <i>logía de Informaçao, Ltd. (BRAZIL) (1)</i>	100.00%	87.95%	81			(20)		
Telefônica de São Paulo, S.A. (BRAZIL) (1) (11) <i>ce and cataloging</i>	100.00%	87.95%			N/D		N/D	
Telefônica de São Paulo, S.A. (BRAZIL) (1) (11) <i>operator Comercial Cabo TV</i>	100.00%	87.95%	32			(2)	N/D	
Telefônica de São Paulo, S.A. (BRAZIL) (1) (11) <i>unications services</i>	100.00%	80,47%	3					
Telefônica de São Paulo, S.A. (BRAZIL) (1) (11) <i>Interactiva Brasil , Ltda. (BRAZIL) (1) (6)</i>	99.99%	99.98%	N/D	N/D	N/D	N/D		
Telefônica de São Paulo, S.A. (BRAZIL) (1) (11) <i>works Brasil, S.A. and subsidiarias (BRAZIL) (1) (6)</i>	100.00%	99.98%	401	(328)		(7)		
Telefônica de São Paulo, S.A. (BRAZIL) (1) (11) <i>of local, domestic and international long distance telephony</i>	0,15%	98.03%	98.18%	589	85	(15)	1,140	
Telefônica de São Paulo, S.A. (BRAZIL) (1) (11) <i>a Multimedia S.A.C.(PERU) (1)(*)(**)</i>	99.99%	98.17%	37	2		4	N/D	
Telefônica de São Paulo, S.A. (BRAZIL) (1) (11) <i>a Servicios Comerciales S.A.C.(PERU) (5)(*)(**)</i>	99.90%	98.08%				3	N/D	
Telefônica de São Paulo, S.A. (BRAZIL) (1) (11) <i>Editoriales del Perú S.A.C.(PERU) (5)(*)(**)</i>	99.90%	98.08%	7				N/D	
Telefônica de São Paulo, S.A. (BRAZIL) (1) (11) <i>a Servicios Técnicos (PERU) (5)(*)(**)</i>	99.90%	98.08%	1				N/D	
Telefônica de São Paulo, S.A. (BRAZIL) (1) (11) <i>Globales de Telecomunicaciones S.A.C. (PERU) (5)</i>	99.90%	98.08%				(2)	N/D	
Telefônica de São Paulo, S.A. (BRAZIL) (1) (11) <i>a Chile Holding, B.V. (NETHERLANDS) (1)</i>	100.00%	100.00%	372	303		31	417	
Telefônica de São Paulo, S.A. (BRAZIL) (1) (11) <i>a Chile Holding, B.V. (NETHERLANDS) (1)</i>	100.00%	100.00%		23		(1)	108	

Company							
es Telefónica Uno, S.A. (CHILE)	99.99%	99.99%	1	122	(81)	3	
on de toda clase de inversiones.							
e Santiago, Comuna de Providencia							
es Telefónica Dos, S.A.	99.99%	99.99%	125	1		(10)	
on de toda clase de inversiones.							
e Santiago, Comuna de Providencia							
a Internacional de Chile, S.A. (CHILE) (1)	100.00%	100.00%	10	945		17	34
Company							
a de Telecomunicaciones de Chile, S.A. (CHILE) (1) (11)	44.89%	44.89%	1,003	(163)	(15)	47	
of local, long distance and international telephony services in							
Providencia, 127-A Santiago de Chile							
a Gestión de Servicios Compartidos de Chile, S.A. (CHILE)							
	44.89%	44.89%	1				1
of mangement and administration services							
videncia, 111-piso 22. Comuna de Providencia. Santiago de							
ile, S.A. (CHILE) (1) (6)	30.00%						
a Internacional de Telecomunicaciones, S.A. (ARGENTINA)							
	100.00%	99.98%	115	(306)		271	644
Company							
iero Huergo, 723, PB Buenos Aires							
a Holding de Argentina, S.A. (ARGENTINA) (1) (11)	99.96%	99.96%	148	(195)		141	1,476
Company							
1 P-17 Buenos Aires							
a de Argentina, S.A. (ARGENTINA) (1) (11)	98.04%	98.04%	165	(1)		82	
unications service provider							
iero Huergo, 723, PB Buenos Aires							
a Larga Distancia de Puerto Rico, INC. (PUERTO RICO) (1)	98.00%	98.00%	76	4		(57)	107
unications service operator							
edificio n° 8. Metro Office Park. Sector de Buchanan.							
o Puerto Rico							

(*) Companies
included in the
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(**) Companies
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	TELEFÓNICA	INTER	RESER	DESI	
R INVESTMENTS	DIRECT	INDIRECT	GROUP	CAPIT	RESER
ation (Hong Kong) Limited (CHINA) (11)	5.00%	5.00%	N/D	N/D	N
operator					
ing) Comp Ltd (China)	100%	100%			
gía e inform, y comunic, de las telecom, Serv, de consultoría y management,					
a Tower. Beijing kerry Centre. 1, Guanghua Road. Chaoyang District Beijing	N/A	N/A	N/A	N/A	N
	N/A	N/A	N/A	N/A	N
A. (VENEZUELA) (1)	100.00%	100.00%		(3)	
enezuela					
Centro Plaza, Torre A, Piso 11, Los Palos Grandes, Caracas					
ERU) (1)	99.99%	99.99%	2	3	
rovider					
San Borja Lima					
ing, S.A. De C.V. (MEXICO) (1) (6)	100.00%	100.00%	52	(53)	
Col. Santa María, Monterrey, Nuevo León, México					
De C.V. (MEXICO) (1) (6)	99.99%	99.99%	N/D	N/D	N
ncial information services					
Col. Santa María, Monterrey, Nuevo León, México					
g Limitada (CHILE) (1) (6)	99.99%	99.99%	69	(47)	
ndes Santiago de Chile					
CHILE) (1)	99.99%	99.99%	N/D	N/D	N
rovider					
ndes Santiago de Chile					
A. (GUATEMALA) (1) (6)	100.00%	100.00%	12	(12)	
Margaritas II Ciudad de Guatemala					
S.A. (EL SALVADOR) (1)	99.99%	99.99%			
elt, Centro Fin. Gigante Torre de San Salvador					
A. (HONDURAS)	99.99%	99.99%			
A. (COSTA RICA) (1)	99.99%	99.99%			
Plaza, 2ª Planta Oficina 2 - San José					
A. (NICARAGUA)	99.99%	99.99%			
(PANAMA) (1)	99.99%	99.99%			
Edificio El Educador Coopeduc - Bethania					

subsidiaries (USA) (1) (6)	100.00%	100.00%		7
00, Miami Florida 33131				
A. (ARGENTINA) (1)	100.00%	100.00%		1
provider				
17 - Buenos Aires				
A. (La Ciudad.com) (COLOMBIA) (1)	99.99%	99.99%		2
a 402. Bogotá D.C., Colombia				
ANDS) (5)	50.00%	50.00%		6,560
company for wireless communications services				
X Amsterdam				
RAZIL) (5) (14)	100.00%	50.00%	135	(2)
industrial property				
851, 20 andar, Parte, Bela Vista, Sao Paulo.				
a. (BRAZIL) (5) (14)	100.00%	50.00%	740	(117)
851, 20 andar, Parte, Bela Vista, Sao Paulo.				
(*) Companies included in the 2006 consolidated tax statement.				
(**) Companies included in the 2007 consolidated tax statement.				

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	TELEFÓNICA		INTERIM		GROSS VALUE		CONSOLIDATION		CONSOLIDATION	
SUBSIDIARIES AND THEIR INVESTMENTS	DIRECT	INDIRECT	GROUP	CAPITAL	RESERVE	DEFERRED	RESULTS	INVESTMENT	METHOD	(10)
Avista Participações Ltda. (BRAZIL) (5) (14) <i>Holding company</i> <i>Rua da Consolação, 247 - 6º andar / sala 57-F</i> <i>São Paulo SP</i>	100.00%	50.00%	236	(30)	(18)	N/D	P			
Telefónica Brasil Sul Celular Participações, Ltda. (BRAZIL) (5) (14) <i>Holding company</i> <i>Avda. Martiniano de Carvalho, 851, 20 andar,</i> <i>parte São Paulo, São Paulo</i>	1.12%	97.44%	50.43%	224	26	(8)	1	P		
PTelecom Brasil, S.A. (BRAZIL) (5) (14) <i>Holding company</i> <i>Rua Cubatao, 320, 4 andar, São Paulo, São Paulo</i>	100.00%	50.00%	1,013	(618)	(8)	N/D	P			
Portelcom Participações, S.A. (BRAZIL) (5) (14) <i>Holding company</i> <i>Av Brigadeiro Faria Lima, 2277, 15ª andar,</i> <i>Conj1503, Jardim Paulistano, São Paulo</i>	100.00%	50.00%	1,358	(369)	(33)	N/D	P			
Vivo Brasil Comunicações (BRAZIL) (5) (14) <i>Wireless communications services operator</i> <i>Rua José Bonifácio, 245, Bon Fim, Porto Alegre</i> <i>Rio Grande Do Sul</i>	100.00%	50.00%				N/D	P			
Vivo Participações, S.A. (BRAZIL) (5) (11) (14) <i>Holding company</i> <i>Rua Silveria Martins, no. 1036, Cabula, Salvador-Bahia</i>	62.94%	31.49%	2,417	642	(4)	124	N/D	P		
Vivo, S.A. (BRAZIL) (5) (14) <i>Wireless services operator</i> <i>Av. Higienópolis, nº1635, Curitiba Parana</i>	100.00%	31.49%	2,153	992		163	N/D	P		
Tele Centro Oeste IP, S.A. (BRAZIL) (5) (14) <i>Wireless services operator</i> <i>AC/ Sul Quadra 02, Bloco C, nº 256, 3º</i> <i>Pavimento, Ed Toufic, Plano Piloto, Brasília, DF</i>	100.00%	31.49%	4	(4)		N/D	P			
Telefónica Móviles El Salvador Holding, S.A. de C.V. (EL SALVADOR) (1) <i>Holding company</i> <i>Alameda Roosevelt y Avenida Sur. Torre</i> <i>Telefónica nivel 10 - San Salvador</i>	100.00%	100.00%	127	(79)	21	161	F			
Telefónica Móviles El Salvador, S.A. de C.V. (EL SALVADOR) (1) <i>Provision of wireless and international long</i> <i>distance communications services</i> <i>Alameda Roosevelt y Avenida Sur. Torre</i> <i>Telefónica nivel 10 - San Salvador</i>	99.08%	99.08%	29	2	9	N/D	F			
	77.50%	76.79%	6		(3)	N/D	F			

Telefónica Multiservicios, S.A. de C.V. (EL SALVADOR) (1)									
<i>Cable modem services operator</i>									
<i>Alameda Roosevelt y Avenida Sur. Torre</i>									
<i>Telefónica nivel 10 - San Salvador</i>									
Telefónica El Salvador, S.A. de C.V. (EL SALVADOR) (3)	100.00%	76.79%						N/D	F
<i>Operational company</i>									
<i>Alameda Roosevelt y Avenida Sur. Torre</i>									
<i>Telefónica nivel 10 - San Salvador</i>									
Guatemala Cellular Holdings, B.V. (NETHERLANDS) (1)	100.00%	100.00%	19					29	F
<i>Holding company</i>									
<i>Strawinskylaan 3105, Atium 7th, Amsterdam</i>									
TCG Holdings, S.A. (GUATEMALA) (1)	100.00%	100.00%	281	(169)				31	239 F
<i>Holding company</i>									
<i>Bulevar Los Próceres 5-56 Zona 10, Unicentro nivel 10 - Guatemala City</i>									
Telefónica Móviles Guatemala, S.A. (GUATEMALA) (1)	13.60%	86.38%	99.98%	279	12			(178)	38 F
<i>Provision of wireless, wireline and radio paging communications services</i>									
<i>Bulevar Los Próceres 5-56 Zona 10, Unicentro nivel 11 - Guatemala City</i>									
Infraestructura Internacional, S.A. (GUATEMALA)	100.00%	99.98%						N/D	F
<i>Telecommunications and paging service provider</i>									
<i>5ª Avenida 7-76, Zona 10 - Guatemala City</i>									
Simpay, Ltd. (UK) (8)	25.00%	25.00%	N/D	N/D	N/D	N/D	N/D	N/D	I
<i>Payment services through wireless telephony</i>									
<i>62-65 Chandos Place, London WC2N 4LP</i>									
Omicron Ceti, S.L. (SPAIN) (8)	100.00%	100.00%	N/D	N/D	N/D	N/D			I
<i>Dormant company</i>									
<i>José Abascal Madrid</i>									
Telefónica Móviles Puerto Rico, Inc. (PUERTO RICO)	100.00%	100.00%	98	(98)				110	F
<i>Ownership of shareholdings in wireless operators in Puerto Rico</i>									
<i>Metro Office Park Calle Edificio # 17, Suite 600 - 00968 Guaynabo</i>									
Newcomm Wireless Services, Inc. (PUERTO RICO)	1.96%	1.96%	N/D	N/D	N/D	N/D	N/D	N/D	I 43
<i>Wireless operator</i>									
OMTP Limited (Open Mobile Terminal Platform) (UK)	2.04%	2.04%	N/D	N/D	N/D	N/D	N/D	N/D	I
(*) Companies included in the 2006 consolidated tax statement.									

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	OWNERSHIP STAKE							GROSS VALUE CONSOLIDATION		
	TELEFÓNICA	INTERIM CONSOLIDATION	TELEFÓNICA	INTERIM CONSOLIDATION	TELEFÓNICA	INTERIM CONSOLIDATION	TELEFÓNICA	INTERIM CONSOLIDATION	TELEFÓNICA	INTERIM CONSOLIDATION
SUBSIDIARIES AND THEIR INVESTMENTS	DIRECT	INDIRECT	GROUP	CAPITAL	RESERVE	DEFERRED	RESULTS	METHOD	(ID)	
MobiPay Internacional, S.A. (SPAIN)	50.00%		50.00%	12	(9)		(1)	5	P	
<i>Provision of payment services through wireless telephony</i>										
<i>Avenida de Europa 20, Alcobendas, Madrid</i>										
Telefónica de Centroamérica, S.L. (SPAIN) (8)	100.00%		100.00%	N/D	N/D	N/D	N/D	1	I	1
<i>Dormant company</i>										
<i>Gran Vía, n° 28, Madrid</i>										
Telefónica Móviles del Uruguay, S.A. (URUGUAY)	100.00%		100.00%	6	N/D	N/D	N/D	13	F	
<i>Wireless communications services operator</i>										
<i>Plza de la Independencia 8, planta baja, Montevideo</i>										
Telefónica Móviles México, S.A. de C.V. (MEXICO) (1) (6)	100.00%									