TELEFONICA S A
Form 20-F
March 26, 2010

As filed with the Securities and Exchange Commission on March 26, 2010

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 20-F

(Mark One)

o REGISTRATION STATEMENT PURSUANT TO SECTION 12(b) OR (g) OF THE SECURITIES EXCHANGE ACT OF 1934

OR

x ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended December 31, 2009

OR

o TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from _____ to _____

OR

o SHELL COMPANY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

Commission file number: 001-09531

TELEFÓNICA, S.A.
(Exact name of Registrant as specified in its charter)

KINGDOM OF SPAIN
(Jurisdiction of incorporation or organization)

Distrito C, Ronda de la Comunicación, s/n

28050 Madrid, Spain
(Address of principal executive offices)

Lucila Rodriguez Jorge, Securities Legal Department
Distrito C, Ronda de la Comunicación, s/n, 28050 Madrid, Spain
Tel. +34 91 482 3734, Fax. +34 91 482 3768, e-mail: amv@telefonica.es

María García-Legaz Ponce, Head of Investor Relations,
Distrito C, Ronda de la Comunicación, s/n, 28050 Madrid, Spain
Tel. +34 91 482 8700, Fax. +34 91 482 8600, e-mail: ir@telefonica.es
(Name, Telephone, E-Mail and/or Facsimile number and Address of Company Contact Person)

Securities registered or to be registered pursuant to Section 12(b) of the Act:

Title of each class	Name of each exchange on which registered
Ordinary Shares, nominal value €1.00 per share*	New York Stock Exchange
American Depositary Shares, each representing three Ordinary Shares	New York Stock Exchange
Guarantees** by Telefónica, S.A. of the $1,000,000,000 Fixed Rate Guaranteed Senior Notes Due 2011; $750,000,000 Fixed Rate Guaranteed Senior Notes Due 2013; $850,000,000 Floating Rate Guaranteed Senior Notes Due 2013; $1,250,000,000 Fixed Rate Notes Due 2015; $1,250,000,000 Fixed Rate Guaranteed Senior Notes Due 2016; $700,000,000 Fixed Rate Guaranteed Senior Notes Due 2017; $1,000,000,000 Fixed Rate Notes Due 2019; $2,000,000,000 Fixed Rate Guaranteed Senior Notes Due 2036; each of Telefónica Emisiones, S.A.U.	New York Stock Exchange

* Not for trading, but only in connection with the listing of American Depositary Shares, pursuant to the requirements of the New York Stock Exchange.

** Not for trading, but only in connection with the listing of the $1,000,000,000 Fixed Rate Guaranteed Senior Notes Due 2011; $750,000,000 Fixed Rate Guaranteed Senior Notes Due 2013; $850,000,000 Floating Rate Guaranteed Senior Notes Due 2013; $1,250,000,000 Fixed Rate Notes Due 2015; $1,250,000,000 Fixed Rate Guaranteed Senior Notes Due 2016; $700,000,000 Fixed Rate Guaranteed Senior Notes Due 2017; $1,000,000,000 Fixed Rate Notes Due 2019; $2,000,000,000 Fixed Rate Guaranteed Senior Notes Due 2036; each of Telefónica Emisiones, S.A.U. (a wholly-owned subsidiary of Telefónica, S.A.)

Securities registered or to be registered pursuant to Section 12(g) of the Act: None

---

Securities for which there is a reporting obligation pursuant to Section 15(d) of the Act: None

---

The number of outstanding shares of each class of capital stock of Telefónica, S.A. at December 31, 2009 was:

Ordinary Shares, nominal value €1.00 per share: 4,563,996,485

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

Yes x No o

If this report is an annual or transition report, indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934.

Yes o No x

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports) and (2) has been subject to such filing requirements for the past 90 days.

Yes x No o

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (Section 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes o No o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer" and "large accelerated filer" in Rule 12b-2 of the Exchange Act.

Large accelerated filer x Accelerated filer o Non-accelerated filer o

Indicate by check mark which basis of accounting the registrant has used to prepare the financial statements included in this filing:

U.S. GAAP o International Financial Reporting Standards as Issued by the international Accounting Standards Board x Other o

If "Other" has been checked in response to the previous question, indicate by check mark which financial statement item the registrant has elected to follow.

Item 17 o Item 18 o

If this is an annual report indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes o No x

TABLE OF CONTENTS

Table of Contents

CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING STATEMENTS

This Annual Report contains statements that constitute forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, Section 21E of the Securities Exchange Act of 1934, as amended, and the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. The forward-looking statements in this Annual Report can be identified, in some instances, by the use of words such as "will", "expect", "aim", "hope", "anticipate", "intend", "believe" and similar language or the negative thereof or by the forward-looking nature of discussions of strategy, plans or intentions. These statements appear in a number of places in this Annual Report including, without limitation, certain statements made in "Item 3. Key Information—Risk Factors", "Item 4. Information on the Company", "Item 5. Operating and Financial Review and Prospects" and "Item 11. Quantitative and Qualitative Disclosures About Market Risk" and include statements regarding our intent, belief or current expectations with respect to, among other things:

- the effect on our results of operations of competition in telecommunications markets;
- trends affecting our financial condition or results of operations;
- acquisitions or investments which we may make in the future;
- our capital expenditures plan;
- our estimated availability of funds;
- our ability to repay debt with estimated future cash flows;
- our shareholder remuneration policies;
- supervision and regulation of the telecommunications sectors where we have significant operations;
- our strategic partnerships; and
- the potential for growth and competition in current and anticipated areas of our business.

Such forward-looking statements are not guarantees of future performance and involve numerous risks and uncertainties, and actual results may differ materially from those anticipated in the forward-looking statements as a result of various factors. The risks and uncertainties involved in our business that could affect the matters referred to in such forward-looking statements include but are not limited to:

- changes in general economic, business or political conditions in the domestic or international markets (particularly in Latin America) in which we operate or have material investments that may affect demand for our services;
- changes in currency exchange rates, interest rates or in credit risk in our treasury investments or in some of our financial transactions;
- general economic conditions in the countries in which we operate;
- existing or worsening conditions in the international financial markets;
- failure to maintain satisfactory working relationships with our joint venture partners;

- the actions of existing and potential competitors in each of our markets;
- the impact of current, pending or future legislation and regulation in countries where we operate;
- failure to renew or obtain the necessary licenses, authorizations and concessions to carry out our operations;

1

Table of Contents

- the potential effects of technological changes;
- the impact of limitations in spectrum capacity;
- failure of suppliers to provide necessary equipment and services on a timely basis;
- the impact of unanticipated network interruptions;
- the effect of reports suggesting that radio frequency emissions cause health problems;
- the impact of impairment charges on our goodwill and assets as a result of changes in the regulatory, business or political environment; and
- the outcome of pending litigation.

Readers are cautioned not to place undue reliance on those forward-looking statements, which speak only as of the date of this Annual Report. We undertake no obligation to release publicly the result of any revisions to these forward-looking statements which may be made to reflect events or circumstances after the date of this Annual Report including, without limitation, changes in our business or acquisition strategy or planned capital expenditures, or to reflect the occurrence of unanticipated events.

Table of Contents

CERTAIN TERMS AND CONVENTIONS

Our ordinary shares, nominal value €1.00 per share, are currently listed on each of the Madrid, Barcelona, Bilbao and Valencia stock exchanges under the symbol "TEF". They are also listed on various foreign stock exchanges such as the London, Buenos Aires and Tokyo stock exchanges and are quoted through the Automated Quotation System of the Spanish stock exchanges and through the SEAQ International System of the London Stock Exchange. American Depositary Shares ("ADSs"), each representing the right to receive three ordinary shares, are listed on the New York Stock Exchange and on the Lima Stock Exchange. ADSs are evidenced by American Depositary Receipts ("ADRs") issued under a Deposit Agreement with Citibank, N.A., as Depositary. Brazilian Depositary Receipts ("BDRs"), each representing the right to receive one ordinary share, are listed on the São Paulo Stock Exchange and are issued under a Deposit Agreement with Banco Bradesco, S.A., as Depositary.

As used herein, "Telefónica", "Telefónica Group", "Group" and terms such as "we", "us" and "our" mean Telefónica, S.A. and consolidated subsidiaries, unless the context requires otherwise.

As used herein, "Atento" means Atento Holding, Inversiones y Teleservicios, S.A. and its consolidated subsidiaries, unless the context requires otherwise.

Below are definitions of certain technical terms used in this Annual Report:

- "Access" refers to a connection to any of the telecommunications services offered by us. We present our customer base using this model because the integration of telecommunications services in bundled service packages has changed the way residential and corporate customers contract for our services. Because a single customer may contract for multiple services, we believe it is more accurate to count the number of accesses, or services a customer has contracted for, as opposed to only counting the number of our customers. For example, a customer that has fixed line telephony service and broadband service represents two accesses rather than a single customer. In addition, we fully count the accesses of all companies over which we exercise control or joint control. The following are the main categories of accesses:

- Fixed telephony accesses: includes public switched telephone network, or PSTN, lines (including public use telephony), and integrated services digital network, or ISDN, lines and circuits. For purposes of calculating our number of fixed line accesses, we multiply our lines in service as follows: PSTN (x1); basic ISDN (x1); primary ISDN (x30, x20 or x10); 2/6 digital accesses (x30).

    - Internet and data accesses: includes broadband accesses (retail asymmetrical digital subscriber line "ADSL", satellite, fiber optic and circuits over 2 Mbps), narrowband accesses (Internet service through the PSTN lines) and other accesses, including the remaining non-broadband final client circuits. "Naked ADSL" allows customers to subscribe for a broadband connection without a monthly fixed line fee.

    - Pay TV: includes cable TV, direct to home satellite TV, or DTH, and Internet Protocol TV, or IPTV.

- Mobile accesses: includes contract and pre-pay mobile telephony. In 2009 in order to align the criteria for the key performance indicators of our mobile operations, the definition of mobile accesses (and, therefore, of total accesses) was revised to include machine-to-machine accesses. In addition, we revised the accounting criteria for pre-pay mobile accesses at Telefónica O2 Czech Republic and Telefónica O2 Slovakia to conform to the accounting criteria for pre-pay mobile accesses throughout the Group. In order to count a pre-pay mobile access, such access must have been active in the most recent three months prior to counting. As a result of both revisions, we restated 2008 mobile accesses. 2007 information is presented based on our prior classifications.

- Unbundled local loop, or ULL: includes accesses to both ends of the copper local loop leased to other operators to provide voice and DSL services (fully unbundled loop, fully UL) or only DSL service (shared unbundled loop, "shared UL").
- Wholesale ADSL: means wholesale asymmetrical digital subscriber line.
- Other: includes other circuits for other operators.

3

Table of Contents

Certain technical terms used with respect to our business are as follows:

- "ARPU" is the average revenue per user per month. ARPU is calculated by dividing total service revenue (excluding inbound roaming revenue) from sales to customers for the preceding 12 months by the weighted average number of customers for the same period, and then divided by 12 months. ARPU is calculated using gross service revenue before deduction of wholesale discounts.

- "CDMA" means Code Division Multiple Access, which is a type of radio communication technology.

- "Commercial activity" includes the addition of new lines, replacement of handsets and changes in types of contracts.

- "Customer revenue" means service revenue less interconnection revenue.

- "Duo bundle" means broadband plus voice service. We measure "duo bundles" in terms of units, where each bundle of broadband and voice service counts as one unit.

- "Final clients accesses" means accesses provided to residential and corporate clients.

- "Gross adds" means the gross increase in the customer base measured in terms of accesses in a period.

- "HSDPA" means High Speed Downlink Packet Accesses, which is a 3G mobile telephony communications protocol in the High-Speed Packet Access (HSPA) family, which allows networks based on UMTS to have higher data transfers speeds and capacity.

- "Interconnection revenue" means revenues received from other operators which use our networks to connect to our customers.

- "ISP" means Internet service provider.

- "LMDS" means local multipoint distribution service.

- "Local loop" means the physical circuit connecting the network termination point at the subscriber's premises to the main distribution frame or equivalent facility in the fixed public telephone network.

- "MOU", or minutes of use, is calculated by dividing the total number of voice minutes for the preceding 12 months by the weighted average number of mobile accesses for the same period, and then divided by 12 months. Over the past several years, we have experienced strong growth in mobile accesses related primarily to data services (such as accesses related to machine-to-machine and mobile broadband devices). Such growth in mobile accesses related to data services limits the use of MOU as an indicator of usage as it increases the total number of mobile accesses in the relevant period without any corresponding increase in the number of voice minutes related to such accesses for the relevant period. As a result, for 2009 and 2008 we have decided to publish traffic evolution in absolute minutes of use terms rather than MOU.

- "MVNO" means mobile virtual network operator, which is a mobile operator that is not entitled to use spectrum for the provision of mobile services. Consequently, an MVNO must subscribe to an access agreement with a mobile network operator in order to provide mobile access to their customers. An MVNO pays such mobile network operator for using the infrastructure to facilitate coverage to their customers. There are two types of MVNOs: (i) pure MVNOs, which are typically telecommunications companies without licensed frequency allocation and want to complete their telecommunications service portfolio (for example, ONO in Spain); and (ii) reseller MVNOs which are companies that purchase wholesale mobile minutes and resell to end-users, and use their brand and distribution channel (for example, Carrefour in Spain).

- "Net adds" means the difference between the customer base measured in terms of accesses at the end of the period and the beginning of a period.

- "Revenues" means net sales and rendering of services.

Table of Contents

- "Service revenues" means revenues less revenues from handset sales.

- "Traffic" means voice minutes used by our customers over a given period, both outbound and inbound. On-net traffic is only included once (outbound), and promotional traffic (free minutes included in commercial promotions) is included. Traffic not associated with our mobile customers (roaming-in; MVNOs; interconnection of third parties and other business lines) is excluded. To arrive at the aggregate traffic for a given period, the individual components of traffic are not rounded.

- "Trio bundle" means broadband plus voice service plus IPTV. We measure "trio bundles" in terms of units, where each bundle of broadband, voice service and IPTV counts as one unit.

- "UMTS" means Universal Mobile Telecommunications System.

- "VoIP" means voice over Internet protocol.

- "Wholesale accesses" means accesses we provide to our competitors, who then sell such accesses to their residential and corporate clients.

In this Annual Report we make certain comparisons in local currency or on a "constant euro basis" or "excluding foreign exchange rate effects" in order to present an analysis of the development of our results of operations from year-to-year without the effects of currency fluctuations. To make comparisons on a local currency basis, we compare financial items in the relevant local currency for the periods indicated as recorded in the relevant local currency for such periods. To make comparisons on a "constant euro basis" or "excluding foreign exchange rate effects", we convert the relevant financial item into euros using the prior year's average euro to relevant local currency exchange rate. In addition, we present certain financial information excluding the effects of Venezuela being considered a hyperinflationary economy in 2009 by eliminating all of the adjustments made as a result of such consideration.

Table of Contents

PRESENTATION OF CERTAIN FINANCIAL INFORMATION

In this Annual Report, references to “U.S. dollars”, “dollars” or “$”, are to United States dollars, references to “pounds sterling”, “sterling” or “£” are to British pounds sterling, references to “reais” refer to Brazilian reais and references to “euro” or “€” are to the single currency of the participating member states in the Third Stage of the European Economic and Monetary Union pursuant to the treaty establishing the European Community, as amended from time to time.

Our consolidated financial statements as of December 31, 2008 and 2009, and for the years ended December 31, 2007, 2008 and 2009 included elsewhere in this Annual Report including the notes thereto (the “Consolidated Financial Statements”), are prepared in conformity with International Financial Reporting Standards (“IFRS”) as issued by the International Accounting Standards Board (“IASB”), which do not differ for the purposes of the Telefónica Group from IFRS as adopted by the European Union.

Table of Contents

PART I

Item 1. Identity of Directors, Senior Management and Advisors

A. Directors and Senior Management

Not applicable.

B. Advisers

Not applicable.

C. Auditors

Not applicable.

Item 2. Offer Statistics and Expected Timetable

Not applicable.

Item 3. Key Information

A. Selected Financial Data

The following table presents our selected consolidated financial data. It is to be read in conjunction with "Item 5. Operating and Financial Review and Prospects" and the Consolidated Financial Statements. The consolidated income statement and cash flow data for the years ended December 31, 2007, 2008 and 2009 and the consolidated statement of financial position data as of December 31, 2008 and 2009 set forth below are derived from, and are qualified in their entirety by reference to, the Consolidated Financial Statements. The consolidated income statement and cash flow data for the years ended December 31, 2005 and 2006 and the consolidated statement of financial position data as of December 31, 2005, 2006 and 2007 set forth below are derived from Telefónica, S.A.'s consolidated financial statements for such years, which are not included herein.

Our Consolidated Financial Statements have been prepared in accordance with IFRS as issued by the IASB.

Table of Contents

The basis of presentation and principles of consolidation are described in detail in Notes 2 and 3.q., respectively, to our Consolidated Financial Statements.

	As of or for the year ended December 31,				
	2005(1)	2006(1)	2007	2008	2009
	(in millions of euros, except share data)				
Revenues	37,383	52,901	56,441	57,946	56,731
Other income	1,416	1,571	4,264	1,865	1,645
Supplies	(9,999)	(16,629)	(17,907)	(17,818)	(16,717)
Personnel expenses	(5,532)	(7,622)	(7,893)	(6,762)	(6,775)
Other expenses	(8,212)	(11,095)	(12,081)	(12,312)	(12,281)
Depreciation and amortization	(6,693)	(9,704)	(9,436)	(9,046)	(8,956)
Operating income	8,363	9,422	13,388	13,873	13,647
Share of profit (loss) of associates	(128)	76	140	(161)	47
Net financial expenses	(1,790)	(2,795)	(2,851)	(2,821)	(2,767)
Net exchange differences	162	61	7	24	(540)
Net financial income (expense)	(1,628)	(2,734)	(2,844)	(2,797)	(3,307)
Profit before taxes from continuing operations	6,607	6,764	10,684	10,915	10,387
Corporate income tax	(1,904)	(1,781)	(1,565)	(3,089)	(2,450)
Profit for the year from continuing operations	4,703	4,983	9,119	7,826	7,937
Profit from discontinued operations after taxes	124	1,596	—	—	—
Profit for the year	4,827	6,579	9,119	7,826	7,937
Non-controlling interests	(381)	(346)	(213)	(234)	(161)
Profit for the year attributable to equity holders of the parent	4,446	6,233	8,906	7,592	7,776
Weighted average number of shares (thousands)	4,870,852	4,778,999	4,758,707	4,645,852	4,552,656
Basic and diluted earnings per share from continuing operations attributable to equity holders (euros)(2)	0.90	0.97	1.87	1.63	1.71
Basic and diluted earnings per share attributable to equity holders of the parent (euros)(2)	0.91	1.30	1.87	1.63	1.71
Earnings per ADS (euros)(2)(3)	2.74	3.91	5.62	4.90	5.12
Weighted average number of ADS (thousands)	1,623,617	1,592,999	1,586,236	1,548,617	1,517,552
Cash dividends per ordinary share (euros)	0.50	0.55	0.65	0.90	1.00
Consolidated Statement of Financial Position Data					
Cash and cash equivalents	2,213	3,792	5,065	4,277	9,113
Property, plant and equipment	27,993	33,887	32,460	30,545	31,999
Total assets	73,174	108,982	105,873	99,896	108,141
Non-current liabilities	35,126	62,645	58,044	55,202	56,931

Equity (net)	16,158	20,001	22,855	19,562	24,274
Capital stock	4,921	4,921	4,773	4,705	4,564
Consolidated Cash Flow Data					
Net cash from operating activities	11,139	15,414	15,551	16,366	16,148
Net cash used in investing activities	(9,592)	(28,052)	(4,592)	(9,101)	(9,300)
Net cash (used in) from financing activities	(435)	14,572	(9,425)	(7,765)	(2,281)

(1) Telefónica Publicidad e Información, S.A. (TPI) was sold in 2006 and its results of operations for 2006 and the gain we recorded on its sale are included under "Profit from discontinued operations after taxes" for 2006. Figures for 2005 have been restated to present TPI's results under the same caption.

(2) The per share and per ADS computations for all periods presented have been presented using the weighted average number of shares and ADSs, respectively, outstanding for each period, and have been adjusted to reflect the stock dividends which occurred during the periods presented, as if these had occurred at the beginning of the earliest period presented.

(3) Each ADS represents the right to receive three ordinary shares. Figures do not include any charges of the Depositary.

Table of Contents

Exchange Rate Information

As used in this Annual Report, the term "Noon Buying Rate" refers to the rate of exchange for euros, expressed in U.S. dollars per euro, in the City of New York for cable transfers payable in foreign currencies as certified by the Federal Reserve Bank of New York for customs purposes. The Noon Buying Rate certified by the New York Federal Reserve Bank for the euro on March 19, 2010 was $1.3530 = €1.00. The following tables describe, for the periods and dates indicated, information concerning the Noon Buying Rate for the euro. Amounts are expressed in U.S. dollars per €1.00.

	Noon Buying Rate			
Year ended December 31,	Period end	Average(1)	High	Low
2005	1.1842	1.2400	1.3476	1.1667
2006	1.3197	1.2661	1.3327	1.1860
2007	1.4603	1.3797	1.4862	1.2904
2008	1.3919	1.4698	1.6010	1.2446
2009	1.4332	1.3955	1.5100	1.2547
2010 (through March 19, 2010)	1.3530	1.3687	1.4536	1.3476

Source: Federal Reserve Bank of New York.

(1) The average of the Noon Buying Rates for the euro on the last day reported of each month during the relevant period.

	Noon Buying Rate	
Month ended	High	Low
October 31, 2009	1.5029	1.4532
November 30, 2009	1.5085	1.4658
December 31, 2009	1.5100	1.4243
January 31, 2010	1.4536	1.3870
February 28, 2010	1.3955	1.3476
March 31, 2010 (through March 19, 2010)	1.3758	1.3516

Source: Federal Reserve Bank of New York.

Monetary policy within the member states of the euro zone is set by the European Central Bank. The European Central Bank has set the objective of containing inflation and will adjust interest rates in line with this policy without taking account of other economic variables such as the rate of unemployment. It has further declared that it will not set an exchange rate target for the euro.

Our ordinary shares are quoted on the Spanish stock exchanges in euro. Currency fluctuations may affect the dollar equivalent of the euro price of our shares listed on the Spanish stock exchanges and, as a result, the market price of our ADSs, which are listed on the New York Stock Exchange. Currency fluctuations may also affect the dollar amounts received by holders of ADSs on conversion by the depositary of any cash dividends paid in euro on the underlying shares.

Our consolidated results are affected by fluctuations between the euro and the currencies in which the revenues and expenses of some of our consolidated subsidiaries are denominated (principally the Brazilian real, the Venezuelan

Bolivar fuerte (see "Item 5. Operating and Financial Review and Prospects—A. Operating Results—Significant Factors Affecting the Comparability of our Results of Operations in the Periods Under Review—Classification of Venezuela as a hyperinflationary economy"), pounds sterling, the Czech koruna (crown), the Argentine peso, the Chilean peso, the Peruvian nuevo sol, the Mexican peso and the Colombian peso).

B. Capitalization and Indebtedness

Not applicable.

Table of Contents

C. Reasons for the Offer and Use of Proceeds

Not applicable.

D. Risk Factors

In addition to the other information contained in this Annual Report, prospective investors should carefully consider the risks described below before making any investment decision. The risks described below are not the only ones that we face. Additional risks not currently known to us or that we currently deem immaterial may also impair our business and results of operations. Our business, financial condition, results of operations and cash flow could be materially adversely affected by any of these risks, and investors could lose all or part of their investment.

Risks Relating to Our Business

A material portion of our operations and investments are located in Latin America, and we are therefore exposed to risks inherent in operating and investing in Latin America.

At December 31, 2009, approximately 35.7% of our assets were located in Latin America. In addition, approximately 40.6% of our revenues for 2009 were derived from our Latin American operations. Our operations and investments in Latin America (including the revenues generated by these operations, their market value and the dividends and management fees expected to be received therefrom) are subject to various risks linked to the economic, political and social conditions of these countries, including risks related to the following:

- government regulation or administrative polices may change unexpectedly and negatively affect our interests in such countries;
- currencies may be devalued or may depreciate or currency restrictions and other restraints on transfer of funds may be imposed;
- the effects of inflation or currency depreciation may result in certain of our subsidiaries having negative equity, which would require them to undertake a mandatory recapitalization or commence dissolution proceedings;
- governments may expropriate or nationalize assets or increase their participation in the economy and companies;
- governments may impose burdensome taxes or tariffs;
- political changes may lead to changes in the economic conditions and business environment in which we operate; and
- economic downturns, political instability and civil disturbances may negatively affect our operations.

For instance, throughout 2009 and in the early part of 2010, certain factors affecting the Venezuelan economy have had an impact on the accounting treatment applied with respect to our subsidiaries in that country, notably the level of inflation reached in 2009, the cumulative inflation rate over the last three years, restrictions placed on the official foreign exchange market and the devaluation of the Venezuelan Bolivar fuerte on January 8, 2010. As a result, in accordance with IFRS, Venezuela was considered a hyperinflationary economy in 2009, which has had a series of effects on our consolidated financial statements as of and for the year ended December 31, 2009 and will have additional effects on our consolidated financial statements as of and for the year ended December 31, 2010. A more detailed description of these effects is included in "Item 5. Operating and Financial Review and Prospects—A. Operating

Results—Significant Factors Affecting the Comparability of our Results of Operations in the Periods Under Review—Classification of Venezuela as a hyperinflationary economy" and Note 2 to our Consolidated Financial Statements.

In addition, our operations are dependent, in many cases, on concessions and other agreements with existing governments in the countries in which we operate. These concessions and agreements, including their renewal, could be directly affected by economic and political instability, altering the terms and conditions under which we operate.

Our financial condition and results of operations may be adversely affected if we do not effectively manage our exposure to foreign currency exchange rate, interest rate or financial investment risks.

We are exposed to various types of market risk in the normal course of our business, including the impact of changes in foreign currency exchange rates and the impact of changes in interest rates, as well as the impact of changes of credit risk in our treasury investments (in cash and cash equivalents) or in some of our financial transactions. We employ risk management strategies to manage this exposure, in part through the use of financial derivatives such as foreign currency forwards, currency swap agreements and interest rate swap agreements. If the financial derivatives market is not sufficiently liquid for our risk management purposes, or if we cannot enter into arrangements of the type and for the amounts necessary to limit our exposure to currency exchange rate fluctuations and interest rate fluctuations or if our counterparties fail to deliver on their commitments due to lack of solvency or otherwise, such failure could adversely affect our financial condition, results of operations and cash flow. Also, our other risk management strategies may not be successful, which could adversely affect our financial condition, results of operations and cash flow. Finally, if the rating of our counterparties in treasury investments or in our structured financial transactions deteriorates significantly or if any of such counterparties were to fail in its obligations to us, we may suffer a loss of value in our investments, incur unexpected losses and assume additional financial obligations under these transactions, and such failure could adversely affect our business, financial condition, results of operations and cash flow.

For a more detailed description of our financial derivatives transactions, see "Item 11. Quantitative and Qualitative Disclosures about Market Risk" and Note 16 to our Consolidated Financial Statements.

Adverse economic conditions could reduce purchases of our products and services.

Our business is impacted by general economic conditions and other similar factors in each of the countries in which we operate. The current adverse global economic environment and uncertainty about an economic recovery may negatively affect the level of demand of existing and prospective customers, as our services may not be deemed critical for these customers. Other factors that could influence customer demand include access to credit, unemployment rates, consumer confidence and other general macroeconomic factors. Spanish gross domestic product, or GDP, contracted by 3.6% in 2009 and, according to the Stability Program 2009-2013 forecasts from the Spanish Ministry of Economy, the Spanish economy is expected to remain in recession in 2010, which could have a material adverse effect on our business, financial condition, results of operations and cash flow.

In addition, there could be other possible follow-on effects from the financial crisis on our business, including insolvency of key suppliers or customers. A loss of customers or a reduction in purchases by our current customers could have a material adverse effect on our business, financial condition, results of operations and cash flow and may therefore negatively affect our ability to meet our growth targets.

Existing or worsening conditions in the international financial markets may limit our ability to carry out our business plan.

The development and distribution of our services as well as the operation, expansion and upgrading of our networks, require substantial financing. Moreover, our liquidity and capital resource requirements may increase if we participate in other fixed line or mobile license award processes or make acquisitions. We also have major capital resource requirements relating to, among other things, the development of distribution channels in new countries of operations and the development and implementation of new technologies.

If our ability to generate cash flow were to decrease, whether due to the current worldwide financial and economic crisis or otherwise, we may need to incur additional debt or raise other forms of capital to support our liquidity and capital resource requirements for the ongoing development and expansion of our business.

Table of Contents

The current state of the financial markets in terms of liquidity, cost of credit and volatility has improved compared to the situation in the second half of 2008 and during most of 2009. Nevertheless, there remain several factors that could affect the ordinary performance of financial markets, such as uncertainty about an economic recovery, reorganization of the international banking system, and growing concern over increases in government deficits, among other factors. Worsening conditions in the international credit markets due to any of these factors may make it more difficult and more expensive to refinance our financial debt (of which €8,647 million matures in 2010) or to incur additional debt.

In addition, our capacity to raise capital in the international capital markets would be impaired if our credit ratings were downgraded, whether due to decreases in our cash flow or otherwise. Further, current market conditions may make it more difficult to renew our unused bilateral credit facilities scheduled to expire prior to December 31, 2010 (for an aggregate amount of €2,779 million). The current financial situation may also make it more difficult and costly for us to launch a rights issue to our current shareholders or to raise additional equity capital if further funds were needed for pursuing our business plans.

The successful implementation of our strategy for our mobile operations in Brazil depends on the development of our joint venture company with Portugal Telecom, SGPS, S.A.

Our mobile business in Brazil is conducted through a 50/50 joint venture company, Brasilcel, N.V., or Brasilcel, which is jointly controlled by us and Portugal Telecom SGPS, S.A., or Portugal Telecom. As a result of our less than controlling interest in this joint venture, we do not have absolute control over the operations of the venture. As a result, there is an inherent risk for management or operational disruptions whenever a disagreement between us and our partner arises. Therefore, we must cooperate with Portugal Telecom in order to implement and expand upon our business strategies and to finance and manage the operations of the joint venture. If we do not manage to obtain the cooperation of Portugal Telecom or if a disagreement or deadlock arises we may not achieve the expected benefits from this joint venture, including economies of scale and opportunities to achieve potential synergies and cost savings.

Risks Relating to Our Industry

We face intense competition in most of our markets, which could result in decreases in current and potential customers, revenues and profitability.

We face significant competition in all of the markets in which we operate, and we are therefore subject to the effects of actions by our competitors in these markets. Our competitors could:

- offer lower prices, more attractive discount plans or better services and features;
- develop and deploy more rapidly new or improved technologies, services and products;
- launch bundle offerings of one type of service with others;
- in the case of the mobile industry, subsidize handset procurement; or
- expand and enhance their networks more rapidly.

Furthermore, some of our competitors in certain markets have, and some potential competitors may enjoy, in certain markets, competitive advantages, including the following:

- greater brand name recognition;

- greater financial, technical, marketing and other resources;
- dominant position or significant market power;
- better strategic alliances;

Table of Contents

- larger customer bases; and
- well-established relationships with current and potential customers.

To compete effectively with our competitors, we need to successfully market our products and services and to anticipate and respond to various competitive factors affecting the relevant markets, such as the introduction of new products and services by our competitors, pricing strategies adopted by our competitors and changes in consumer preferences and in general economic, political and social conditions. If we are unable to effectively compete, it could result in price reductions, lower revenues, under-utilization of our services, reduced operating margins and loss of market share, any of which could have a material adverse effect on our business, financial condition, results of operations and cash flow.

We operate in a highly regulated industry, which could adversely affect our businesses.

As a multinational telecommunications company that operates in regulated markets, we are subject to different laws and regulations in each of the jurisdictions in which we provide services. Such laws and regulations are promulgated and enforced to varying degrees by supranational regulators such as the European Union and national, state, regional and local authorities. Regulation may be especially strict in the markets of those countries in which we hold a significant market position. In this respect, regulatory authorities regularly intervene in the retail and wholesale offering and pricing of our products and services. Furthermore, such authorities may also adopt further regulations or take additional actions that could adversely affect us, including revocation of or failure to renew any of our licenses, authorizations or concessions, implementation of changes to the spectrum allocated to us or the granting or new licenses, authorizations or concessions to our competitors to offer services in the relevant markets. Furthermore, regulations could require us to reduce roaming prices and termination rates in mobile and fixed line networks, require us to offer access to our network to other operators, and result in the imposition of fines if we fail to fulfill our service commitments. Such regulations and regulatory actions could place significant competitive and pricing pressure on our operations, and could have a material adverse effect on our business, financial condition, results of operations and cash flow.

In addition, since we hold a leading market share in many of the counties where we operate, we could face regulatory actions by antitrust or competition authorities designed to enhance competition in the relevant markets. These authorities could prohibit us from taking further actions such as making further acquisitions or continuing to engage in particular practices or impose fines or other penalties on us, which, if significant, could result in loss of market share and harm to our financial performance and future growth.

The regulatory landscape in the European Union will change as a consequence of the recent passage of a new common regulatory framework that is to be implemented by Member States before June 2011. We believe based on the principles set forth in such regulatory framework that the regulations adopted by Member States may result in an increased focus on the development and maintenance of competitive markets. This regulatory framework proposes the adoption of measures, under exceptional circumstances and in specific situations, by national authorities to establish functional separation between the retail and wholesale operations of vertically integrated operators with significant market power, by requiring them to offer equal wholesale conditions to related and third party operators. The adoption of such regulatory framework in Spain and the other European Union Members States where we operate could result in requirements to modify our internal organization in the relevant markets, which could result in additional costs to us. Additionally, our industry may face new regulatory initiatives regarding lowering mobile termination rates and the provision of data and audiovisual services.

In addition, we may also face pressure from regulatory initiatives in some European countries in order to reallocate spectrum rights of use and to modify spectrum allocation policies that may result, among other matters, in new tender processes for spectrum allocation in the European Union.

Finally, the recommendation that is being drafted by the European Commission on the implementation of European regulation of new generation broadband networks may reduce the incentives for operators to invest in broadband networks over the short and medium term because operators that invest in broadband networks could be required to provide access to such networks to third parties. This could affect competition and business performance and future growth in such services.

Table of Contents

For further information regarding the matters discussed above and other aspects of the regulatory environments in which our businesses operate, see "Item 4. Information on the Company—Business Overview—Regulation".

We operate under licenses, authorizations and concessions granted by government authorities.

Most of our operating companies require licenses, authorizations or concessions from the governmental authorities of the countries in which they operate. These licenses, authorizations and concessions specify the types of services permitted to be offered by the operating company holding such license, authorization or concession. The continued existence and terms of our licenses, authorizations and concessions are subject to review by regulatory authorities in each country and to interpretation, modification or termination by these authorities. Moreover, authorizations, licenses and concessions as well as their renewal terms and conditions may be affected by political and regulatory factors.

The terms of these licenses, authorizations and concessions granted to our operating companies and conditions of the renewals of such licenses, authorizations and concessions vary from country to country. Although license, authorization and concession renewal is not usually guaranteed, most licenses, authorizations and concessions do address the renewal process and terms, which is usually related to the fulfillment of the commitments that were assumed by the grantee. As licenses, authorizations and concessions approach the end of their terms, we intend to pursue their renewal to the extent provided by the relevant licenses, authorizations or concessions and, under certain circumstances, we will operate under technically expired licenses, authorizations or concessions under preexisting terms during the renewal process. Failure to complete the renewal process successfully could adversely affect our business, financial condition, results of operations and cash flow.

Many of our licenses, authorizations and concessions are revocable for public interest reasons. The rules of some of the regulatory authorities with jurisdiction over our operating companies require us to meet specified network build-out requirements and schedules. In particular, our existing licenses, authorizations and concessions typically require us to satisfy certain obligations, including, amongst others, minimum specified quality standards, service and coverage conditions and capital investment. Failure to comply with these obligations could result in the imposition of fines or revocation or forfeiture of the license, authorization or concession for the relevant area. In addition, the need to meet scheduled deadlines may require our companies to expend more resources than otherwise budgeted for a particular network build-out.

For further information regarding the licenses and concessions of our operating companies, see "Item 4. Information on the Company—Business Overview—Regulation".

The industry in which we operate is subject to rapid technological changes, which requires us to continuously adapt to such changes and to upgrade our existing networks. If we are unable to adapt to such changes, our ability to provide competitive services could be materially adversely affected.

Our future success depends, in part, on our ability to anticipate and adapt in a timely manner to technological changes. We expect that new products and technologies will emerge on a continuous basis and that existing products and technologies will further develop. These new products and technologies may reduce the prices for our existing services or may be superior to, and render obsolete, the products and services we offer and the technologies we use and may consequently reduce the revenues generated by our products and services and require investment in new technology. In addition, we may be subject to competition in the future from other companies that are not subject to regulation as a result of the convergence of telecommunications technologies. As a result, it may be very expensive for us to upgrade our products and technology in order to continue to compete effectively with new or existing competitors. Such increased costs could adversely affect our business, financial condition, results of operations and cash flow.

In particular, we must continue to upgrade our existing mobile and fixed line telephony networks in a timely and satisfactory manner in order to retain and expand our customer base in each of our markets, to enhance our financial performance and to satisfy regulatory requirements. Among other things, we could be required to upgrade the functionality of our networks to accommodate increased customization of services, to increase coverage in some of our markets, or to expand and maintain customer service, network management and administrative systems.

Table of Contents

Many of these tasks are not entirely under our control and may be affected by applicable regulations. If we fail to execute these tasks successfully, our services and products may be less attractive to new customers and we may lose existing customers to our competitors, which would adversely affect our business, financial condition, results of operations and cash flow.

Spectrum capacity may become a limiting factor.

Our mobile operations in a number of countries may rely on spectrum availability. Failure to obtain sufficient or adequate spectrum coverage and, to a lesser extent, the costs related to obtaining this capacity could have a material adverse impact on the quality of our services and on our ability to provide new services, adversely affecting our business, financial condition, results of operations and cash flow.

Our business could be adversely affected if our suppliers fail to provide necessary equipment and services on a timely basis.

We depend upon a small number of major suppliers for essential products and services, mainly network infrastructure and mobile handsets. These suppliers may, among other things, extend delivery times, raise prices and limit supply due to their own shortages and business requirements. Furthermore, these suppliers may be adversely affected by current economic conditions. If these suppliers fail to deliver products and services on a timely basis, our business and results of operations could be adversely affected. Similarly, interruptions in the supply of telecommunications equipment for our networks could impede network development and expansion, which in some cases could adversely affect our ability to satisfy our license terms and requirements.

We may be adversely affected by unanticipated network interruptions.

Unanticipated network interruptions as a result of system failures whether accidental or otherwise, including due to network, hardware or software failures, which affect the quality of or cause an interruption in our service, could result in customer dissatisfaction, reduced revenues and traffic and costly repairs, penalties or other measures imposed by regulatory authorities, and could harm our reputation. We attempt to mitigate these risks through a number of measures, including backup systems and protective systems such as firewalls, virus scanners and building security. However, these measures are not effective under all circumstances and cannot avert every action or event that could damage or disrupt our technical infrastructure. Although we carry business interruption insurance, our insurance policy may not provide coverage in amounts sufficient to compensate us for any losses we may incur.

The mobile industry may be harmed by reports suggesting that radio frequency emissions cause health problems.

Over the last few years, the debate about the alleged potential effects of radio frequency emissions on human health has increased significantly. In many cases, this has hindered the deployment of the infrastructures necessary to ensure quality of service.

Institutions and organizations, such as the World Health Organization (WHO), have stated that exposure to radio frequency emissions generated by mobile telephony, within the limits established, has no adverse effects on health. In fact, a number of European countries, including Spain among others, have drawn up complete regulations reflecting the Recommendation of the Council of the European Union dated July 12, 1999. These add planning criteria for new networks, thus ensuring compliance with the limits on exposure to radio frequency emissions.

Whether or not other research or studies conclude there is a link between radio frequency emissions and health, popular concerns about radio frequency emissions may discourage the use of mobile communication devices and may result in significant restrictions on both the location and operation of cell sites, either or both of which could have a detrimental impact on our mobile companies and consequently on our financial condition, results of operations and cash flow. While we are not aware of any evidence confirming a link between radio frequency emissions and health problems and we continue to comply with good practices codes and relevant regulations, there can be no assurance of what future medical research may suggest.

Table of Contents

Developments in the telecommunications sector have resulted, and may in the future result, in substantial write-downs of the carrying value of certain of our assets.

We review on an annual basis or more frequently where the circumstances require, the value of each of our assets and subsidiaries to assess whether the carrying values of such assets and subsidiaries can be supported by the future cash flows expected to be derived from such assets and subsidiaries, including in some cases synergies included in their acquisition costs. The current economic environment and changes in the short and medium term, as well as changes in the regulatory, business or political environment may result in the necessity of recognizing impairment charges on our goodwill, intangible assets or fixed assets.

Although the recognition of impairments of tangible, intangible and financial assets result in a non-cash charge on the income statement, such charge would adversely affect our results of operations and consequently, our ability to achieve our growth targets.

Other Risks

We are involved in disputes and litigation with regulators, competitors and third parties.

We are party to lawsuits and other legal, regulatory and antitrust proceedings in the ordinary course of our business, the final outcome of which is generally uncertain. Litigation and regulatory proceedings are inherently unpredictable. An adverse outcome in, or any settlement of, these or other proceedings (including any that may be asserted in the future) may have a material adverse effect on our business, financial condition, results of operations and cash flow.

For a more detailed description of current legal proceedings, see "Item 8. Financial Information—Legal Proceedings".

Item 4. Information on the Company

A. History and Development of the Company

Overview

Telefónica, S.A., is a corporation duly organized and existing under the laws of the Kingdom of Spain, incorporated on April 19, 1924. We are:

- a diversified telecommunications group which provides a comprehensive range of services through one of the world's largest and most modern telecommunications networks;
- mainly focused on providing fixed and mobile telephony services; and
- present principally in Spain, Europe and Latin America.

The following significant events occurred in 2009:

- On June 23, 2009, our Board of Directors agreed to initiate a process for the purchase of the Telefónica de Argentina S.A. ("Telefónica de Argentina") shares held by unaffiliated parties, which amounted to 1.8% of Telefónica de Argentina's share capital. After following the procedures set forth in Argentine Presidential Decree No. 677/01, Chapter VII, on December 3, 2009, the Argentine securities regulator approved the transaction, resulting in our acquisition on January 25, 2010 of these shares for approximately €23 million. As a result of such acquisition we beneficially own 100% of the share capital of Telefónica de Argentina, and we delisted Telefónica de Argentina's shares and ADSs from the Buenos Aires and New York stock exchanges, respectively.

- On August 31, 2009, we agreed to sell our 32.18% stake in Medi Telecom S.A., or Medi Telecom, together with its outstanding shareholder loans to our local partners for total cash consideration of €400 million. This transaction closed on December 31, 2009.

Table of Contents

- On September 6, 2009 we entered into a strategic alliance with China Unicom (Hong Kong) Limited, or China Unicom, which provides for, among other areas for cooperation, joint procurement of infrastructure and client equipment, common development of mobile service platforms, joint provisions of service to multinational customers, roaming, research and development, sharing of best practices and technical, operational and management know-how, joint development of strategic initiatives in the area of network evolution, joint participation in international alliances and exchanges of senior management. In furtherance of this strategic alliance, on this same date, we entered into a mutual share exchange agreement with China Unicom pursuant to which we agreed to invest the equivalent of $1,000 million in the shares of China Unicom and China Unicom agreed to invest the equivalent of $1,000 million in our shares.

On October 21, 2009, we exchanged 40,730,735 of our shares for 693,912,264 newly issued shares of China Unicom in satisfaction of the mutual share exchange agreement described above. As a result of this exchange, our voting interest in the share capital of China Unicom increased from 5.38% to 8.06%, and China Unicom has a 0.87% voting interest in our share capital at that date. As of the date of this Annual Report, and after the capital reduction carried out by China Unicom, we hold shares representing 8.37% of China Unicom's voting share capital and the right to appoint a member to its board of directors.

- On November 25, 2009, we agreed with Promotora de Informaciones, or Prisa, and Sogecable, S.A., or Sogecable, to acquire a 21% stake in DTS Distribuidora de Televisión Digital, S.A., or DTS, which includes the pay TV services (DIGITAL +) of the Prisa Group for a firm value of €2,350 million. After deduction of net debt, we expect that our total investment will be approximately €470 million. In addition, on this same date we entered into a shareholders' agreement with Prisa and Sogecable to govern the management of DTS. The acquisition is subject, among other conditions, to obtaining regulatory authorizations.

- On December 3, 2009, a subsidiary of Telefónica O2 Germany, Telefónica Deutschland GmbH, signed an agreement to acquire all of the shares of German company HanseNet Telekommunikation GmbH, or HanseNet. The purchase price agreed by the parties was based on a firm value of HanseNet of €900 million, subject to a series of adjustments upon completion of the transaction. On February 16, 2010, having complied with the terms established in the agreement, we completed the acquisition of 100% of the shares of HanseNet. The final amount paid out by us was approximately €912 million.

Business areas

We have implemented a regional, integrated management model based on three business areas, with each area in charge of the fixed and mobile telephone and other businesses within its borders:

- Telefónica Spain: oversees the fixed and mobile telephone, broadband, Internet, pay TV and valued added services and data businesses in Spain.

- Telefónica Europe: oversees the fixed and mobile telephone, broadband, Internet, pay TV and value added services and data businesses in the United Kingdom, Germany, Ireland, the Czech Republic, Slovakia and the Isle of Man.

- Telefónica Latin America: oversees the fixed and mobile telephone, broadband, Internet, pay TV and value added services and data businesses in Latin America.

We are also involved in the media and contact center segments through Telefónica de Contenidos and Atento, respectively.

17

Table of Contents

The following chart shows the organizational structure of the principal subsidiaries of the Telefónica Group at December 31, 2009, including their jurisdictions of incorporation and our ownership interest. For further detail, see Exhibit 8.1 to this Annual Report.

---

(1) Ownership in Telefónica Móviles España, S.A.U. is held directly by Telefónica, S.A.

(2) 85.5% representing voting interest.

(3) Ownership in Telefónica International Wholesale Services. S.L. (Spain) is held 92.51% by Telefónica, S.A. (Spain) and 7.49% by Telefónica Datacorp, S.A.U. (Spain).

(4) Ownership in O2 (Europe) Ltd. is held directly by Telefónica, S.A.

(5) Companies held indirectly by Telefónica, S.A.

Table of Contents

Telefónica, S.A., the parent company of the Telefónica Group, also operates as a holding company with the following objectives:

- coordinate the Group's activities;
- allocate resources efficiently among the Group;
- provide managerial guidelines for the Group;
- manage the Group's portfolio of businesses;
- foster cohesion within the Group; and
- foster synergies among the Group's subsidiaries.

Our principal executive offices are located at Distrito C, Ronda de la Comunicación, s/n, Las Tablas, 28050 Madrid, Spain, and our registered offices are located at Gran Vía, 28, 28013 Madrid, Spain. Our telephone number is +34 900 111 004.

Capital Expenditures and Divestitures

Our principal capital expenditures excluding acquisitions during the three years ended December 31, 2009 consisted of additions to property, plant and equipment and additions to intangible assets. In 2009, 2008 and 2007, we made capital expenditures of €7,257 million, €8,401 million and €8,027 million, respectively.

Year ended December 31, 2009

Our capital expenditures decreased 13.6% to €7,257 million in 2009 compared to €8,401 million in 2008, mainly as a result of investment containment in our three regions of activity. Our investments in Spain were directed toward further developing the broadband business and expanding mobile third generation, or 3G. In Latin America capital expenditures were directed toward satisfying increased customer demand in broadband and pay TV and increasing coverage and capacity of our second generation, or GSM, and mobile 3G networks. In Europe capital expenditures were directed toward expanding the mobile 3G network coverage, developing the broadband business and undertaking IT projects.

Year ended December 31, 2008

Our capital expenditures increased 4.7% to €8,401 million in 2008 compared to €8,027 million in 2007, mainly as a result of investments made to support the growth in Telefónica Latin America's broadband and pay TV businesses and to further develop ADSL and adapt existing loops to FTTx (fiber optic) technology in order to enhance coverage for new services in Spain and expand the coverage and capacity of our mobile networks in all regions.

Year ended December 31, 2007

Capital expenditures increased 0.2% to €8,027 million in 2007 from €8,010 million in 2006 principally related to our investments in Spain in our growing Internet and broadband businesses, with significant investments related to ADSL and IP services, such as Imagenio, our IPTV business. In Latin America capital expenditures were directed toward satisfying increased customer demand in our fixed line business (particularly in broadband and pay TV) and increasing coverage and capacity of our second generation, or GSM, networks and acquiring spectrum in Venezuela, Brazil and Panama to expand coverage and guarantee service quality in areas where traffic is heaviest. In 2007, capital expenditures in Europe decreased primarily as a result of Telefónica O2 Germany bringing forward capital investment from 2007 into 2006 as part of our build-out of our mobile third generation, or 3G, network.

Table of Contents

Financial Investments and Divestitures

Our principal financial investment in 2009 was the acquisition of an additional stake in China Unicom (approximately $1,000 million as a consequence of a mutual share exchange). Our principal divestiture in 2009 was the sale of Medi Telecom (€400 million) as described above.

Our principal financial investments in 2008 were made by Inversiones Telefónica Internacional Holding, Ltda., which invested €640 million for the acquisition of the additional 51.85% of CTC, and Vivo, which invested Brazilian reais 1,163 million (equivalent to approximately €429 million at the transaction date) for the acquisition of 53.90% of the voting stock and 4.27% of the preferred stock of Telemig Celular Participaçoes, S.A.

Our principal financial investments in 2007 were made by Telefónica (€2,314 million for the acquisition of indirect shareholding in Telecom Italia). Our principal financial divestitures in 2007 were the sale of Airwave and Endemol N.V., or Endemol, for £1,932 million (equivalent to approximately €2,841 million at the transaction date) and €2,629 million, respectively.

Public Takeover Offers

The principal public takeover offer which occurred in 2009 and in 2010 through the date of this Annual Report was the following:

- On September 17, 2008, we launched a tender offer through our Inversiones Telefónica Internacional Holding, Ltda. subsidiary to acquire all the outstanding shares of Compañía de Telecomunicaciones de Chile, S.A., or CTC, that we did not already control directly or indirectly, amounting to 55.1% of CTC's share capital. This included all CTC shares listed on the Santiago de Chile and New York Stock Exchanges (represented by American Depositary Shares). In January 2009, upon completion of the transaction, our indirect ownership in CTC had increased to 97.89% of the total outstanding shares, representing a total investment by us of approximately €658 million.

Recent Developments

The principal events that have occurred since December 31, 2009 are set forth below:

- On January 11, 2010, Telco, S.p.A., or Telco, arranged a €1,300 million loan with Intesa Sanpaolo, S.p.A., Mediobanca, S.p.A., Société Générale, S.p.A. and Unicredito, S.p.A. maturing on May 31, 2012, part of which is secured with the Telecom Italia, S.p.A., or Telecom Italia, shares held by Telco. The rest of Telco's financing needs with respect to debt maturities were met with a bridge loan granted by shareholders that was repaid with the proceeds of a bond issuance subscribed by Telco's shareholders, on a pro rata basis in accordance with their interests in Telco, on February 26, 2010 for an aggregate principal amount of €1,300 million. Our subscription amounted to an aggregate principal amount of €600 million.

- On February 16, 2010, having complied with the terms established in the agreement dated December 3, 2009 by the parties, we completed the acquisition of 100% of the shares of HanseNet. The final amount paid was approximately €912 million.

- Following the agreement between Prisa and Gestevisión Telecinco, S.A., or Telecinco, for the sale by Prisa to Telecinco of a 22% stake in DIGITAL+, on January 29, 2010, we signed a new agreement with Prisa raising the percentage stake to be acquired by us in DTS from 21% to 22%. Furthermore, we have undertaken to renegotiate the terms of the shareholders' agreement to reflect the new shareholder structure of DTS.

The estimated total investment to be made by us for the 22% stake in DTS, after deduction of net debt, is expected to be around €495 million, of which approximately €230 million will be covered by the subordinated loan agreement that currently exists between Telefónica de Contenidos, S.A.U. (creditor) and Sogecable (debtor).

Table of Contents

For information related to our significant financing transactions completed in 2009 and through the date of this Annual Report, see “Item 5. Operating and Financial Review and Prospects – Liquidity and Capital Resources – Anticipated Sources of Liquidity”.

B. Business Overview

We increased our customer base, measured in terms of total accesses, by 2.1% to 264.6 million accesses at December 31, 2009 from 259.1 million accesses at December 31, 2008, which was a 13.3% increase from the 228.7 million accesses we had at December 31, 2007. This growth from December 31, 2008 to December 31, 2009 was primarily driven by a 3.3% increase in mobile accesses, a 8.2% increase in broadband accesses and a 9.8% increase in pay TV accesses, which more than offset our 5.4% loss of fixed telephony accesses and 28.5% loss of narrowband accesses as these technologies continue to be substituted by customers for mobile and broadband technologies, respectively. Growth in our total number of accesses from December 31, 2007 to December 31, 2008 was primarily driven by strong growth in mobile and broadband accesses.

The following table shows our total accesses at the dates indicated. The classifications and explanatory notes below also apply, to the extent applicable, to the tables detailing our accesses by business area and country elsewhere in this section.

	At December 31,		
	2007	2008(1)	2009(1)
	(in thousands)		
Fixed telephony accesses(2)	43,433.6	42,930.8	40,606.0
Internet and data accesses	13,156.6	14,654.3	15,082.5
Narrowband accesses	2,678.7	1,997.2	1,427.5
Broadband accesses(3)	10,320.2	12,472.1	13,492.6
Other accesses(4)	157.7	185.0	162.4
Mobile accesses(5)(6)	167,781.1	195,818.6	202,332.5
Pay TV accesses	1,748.1	2,267.5	2,489.2
Final clients accesses	226,119.4	255,671.1	260,510.2
Unbundled local loop accesses	1,396.5	1,748.1	2,206.0
Shared UL accesses	776.4	602.3	447.7
Full UL accesses	620.1	1,145.8	1,758.3
Wholesale ADSL accesses(7)	571.7	534.7	463.4
Other accesses(8)	656.0	1,150.1	1,426.0
Wholesale accesses	2,624.2	3,433.0	4,095.3
Total accesses	228,743.6	259,104.1	264,605.5

(1) From January 1, 2008, fixed wireless public use telephony accesses are included under the caption “fixed telephony accesses”.

(2) PSTN (including public use telephony) x1; ISDN basic access x1; ISDN primary access; 2/6 access x30. Includes our accesses for internal use. It also includes VOIP and naked ADSL accesses.

(3) Includes ADSL, satellite, fiber optic, cable modem and broadband circuits and naked ADSL accesses.

(4) Includes remaining non-broadband final client circuits.

(5) Includes accesses of Telemig at December 31, 2008 and going forward. Medi Telecom accesses are excluded at December 31, 2009.

(6) In 2009 in order to align the criteria for the key performance indicators of our mobile operations, the definition of mobile accesses (and, therefore, of total accesses) was revised to include machine-to-machine accesses. In addition, we revised the accounting criteria for pre-pay mobile accesses at Telefónica O2 Czech Republic and Telefónica O2 Slovakia to conform to the accounting criteria for pre-pay mobile accesses throughout the Group. In order to count a pre-pay mobile access, such access must have been active in the most recent three months prior to counting. As a result of both revisions, we restated 2008 mobile accesses, adding 0.2 million accesses in the aggregate. Our 2007 information is presented based on our prior classifications.

(7) Includes unbundled lines by Telefónica O2 Germany.

(8) Includes circuits for other operators.

Table of Contents

Our Services and Products

Fixed business

The principal services we offer in our fixed businesses in Spain, Europe and Latin America are:

- Traditional fixed telecommunication services. Our principal traditional fixed telecommunication services include PSTN lines; ISDN accesses; public telephone services; local, domestic and international long distance and fixed-to-mobile communications services; corporate communications services; supplementary value-added services (including call waiting, call forwarding, voice and text messaging, advanced voicemail services and conference-call facilities); video telephony; business-oriented value-added services; intelligent network services; leasing and sale of terminal equipment; and telephony information services.

- Internet and broadband multimedia services. Our principal Internet and broadband multimedia services include Internet service provider service; portal and network services; retail and wholesale broadband access through ADSL; naked ADSL (a broadband connection without the monthly fixed line fee); narrowband switched access to Internet for universal service, and other technologies; residential-oriented value-added services (including instant messaging, concerts and video clips by streaming video, e-learning, parental control, firewall protection, anti-virus protection, content delivery and personal computer sales); television services such as Imagenio, our IPTV business, cable television and satellite television; companies-oriented value-added services, like puesto integral o puesto informático, which includes ADSL, computer and maintenance for a fixed price and VoIP services. Telefónica Spain is also providing services based on Fiber to the Home (FTTH), including a new range of products and services named “FUTURA”. This line of products includes high speed Internet access (currently up to 30 Mb), which allows Telefónica Spain to provide its customers with advanced IPTV services such as High Definition (HDTV) channels, Multiroom (allowing clients to watch different TV channels in different rooms) and Digital Video Recording (DVR).

- Data and business-solutions services. Our data and business-solutions services principally include leased lines; virtual private network, or VPN, services; fiber optics services; the provision of hosting and application, or ASP, service, including web hosting, managed hosting, content delivery and application, and security services; outsourcing and consultancy services, including network management, or CGP; and desktop services and system integration and professional services.

- Wholesale services for telecommunication operators. Our wholesale services for telecommunication operators principally include domestic interconnection services; international wholesale services; leased lines for other operators’ network deployment; and local loop leasing under the unbundled local loop regulation framework. It also includes bit stream services, bit stream naked, wholesale line rental accesses and leased ducts for other operators’ fiber deployment.

Mobile business

We offer a wide variety of mobile and related services and products to personal and business customers. Although the services and products available vary from country to country, the following are our principal services and products:

- Mobile voice services. Our principal service in all of our markets is mobile voice telephony.

- Value added services. Customers in most of our markets have access to a range of enhanced mobile calling features, including voice mail, call hold, call waiting, call forwarding and three-way calling.

- Mobile data and Internet services. Current data services offered include Short Messaging Services, or SMS, and Multimedia Messaging Services, or MMS, which allow customers to send messages with images, photographs and sounds. Customers may also receive selected information, such as news, sports scores and stock quotes. We also provide mobile broadband connectivity and Internet access. Through mobile Internet access, our customers are able to send and receive e-mail, browse the Internet, download games, purchase goods and services in m-commerce transactions and use our other data services.

Table of Contents

- Wholesale services. We have signed network usage agreements with several MVNOs in different countries.

- Corporate services. We provide business solutions, including mobile infrastructure in offices, private networking and portals for corporate customers that provide flexible on line billing. Telefónica Móviles España, S.A.U., or Telefónica Móviles España, offers corporate services through MoviStar Corporativo, and other advanced solutions for data developed for specific sectors.

- Roaming. We have roaming agreements that allow our customers to use their mobile handsets when they are outside of our service territories, including on an international basis.

- Fixed wireless. We provide fixed voice telephony services through mobile networks in Venezuela, Argentina, Peru, Mexico, Ecuador, El Salvador, Guatemala and Nicaragua.

- Trunking and paging. In Spain and Guatemala, we provide digital mobile services for closed user groups of clients and paging services.

The following sections provide a description of the main markets in which we operate. Customer information on the markets in which we operate, including our market share based on accesses, are estimates that we have made based on annual reports and press releases made public by our competitors or information from local regulators in the respective markets.

Telefónica Spain Operations

Telefónica Spain provides fixed and mobile telephony services, Internet and data and pay TV services in Spain.

Telefónica Spain's total accesses decreased 1.2% to 46.8 million accesses at December 31, 2009 from 47.3 million accesses at December 31, 2008. Total accesses at December 31, 2009 included 23.5 million mobile accesses, 14.2 million fixed telephony accesses, 5.7 million Internet and data accesses and 0.7 million pay TV accesses. Additionally, it included 2.2 million unbundled local loop accesses and 0.4 million of wholesale ADSL accesses.

The following table presents, at the dates indicated, selected statistical data relating to our operations in Spain.

	At December 31,		
	2007	2008	2009
		(in thousands)	
Fixed telephony accesses	15,918.8	15,326.3	14,200.1
Internet and data accesses	5,321.8	5,670.0	5,722.5
Narrowband accesses	660.8	388.0	219.5
Broadband accesses	4,614.0	5,246.4	5,476.8
Other accesses	47.0	35.6	26.2
Mobile accesses	22,826.6	23,604.8	23,538.6
Pre-pay accesses	9,181.8	9,037.0	8,204.5
Pay TV accesses	511.1	612.5	703.0
Final clients accesses	44,578.2	45,213.6	44,164.2
Wholesale accesses	1,855.5	2,136.1	2,614.0
Total accesses	46,433.6	47,349.7	46,778.2

Telefónica Spain - Fixed business

Telefónica Spain provides fixed telephony services in Spain through the operator Telefónica de España, S.A., or Telefónica de España.

Table of Contents

Operations

The following table presents, at the dates indicated, selected statistical data relating to the operations of Telefónica de España:

	At December 31,		
	2007	2008	2009
	(in thousands)		
Fixed telephony accesses	15,918.8	15,326.3	14,200.1
Internet and data accesses	5,321.8	5,670.0	5,722.5
Narrowband accesses	660.8	388.0	219.5
Broadband accesses	4,614.0	5,246.4	5,476.8
Other accesses	47.0	35.6	26.2
Pay TV accesses	511.1	612.5	703.0
Final clients accesses	21,751.6	21,608.8	20,625.6
Wholesale line rental accesses	–	9.5	97.4
Unbundled local loop accesses	1,353.9	1,698.0	2,153.8
Shared UL accesses	776.4	602.3	447.7
Full UL accesses	577.6	1,095.7	1,706.1
Wholesale ADSL accesses	495.5	423.8	359.0
Other accesses	6.0	4.7	3.7
Wholesale accesses	1,855.5	2,136.1	2,614.0
Total accesses	23,607.1	23,744.8	23,239.6

In 2009, the Spanish market for fixed telephony accesses was affected by an unfavorable economic environment and showed an estimated decrease of 0.8% year-on-year based on number of accesses. During the same period, Telefónica Spain's fixed telephony accesses decreased by 7.3% to 14.2 million accesses at December 31, 2009, from 15.3 million accesses at December 31, 2008, outpacing the total market decline as a result of fierce competition. Telefónica Spain had net fixed telephony accesses losses of 1.1 million in 2009, higher than the 0.6 million net fixed telephony accesses losses recorded in 2008.

Estimated net adds in the total Spanish broadband market decreased 47.9% to 0.6 million in 2009 from 1.1 million in 2008. The total estimated Spanish broadband access market was approximately 9.9 million accesses at December 31, 2009. Telefónica Spain's broadband accesses increased 4.4% to 5.5 million at December 31, 2009 from 5.2 million accesses at December 31, 2008.

Unbundled local loops made up approximately 21.1% of the broadband access market in Spain at December 31, 2009 up from approximately 18.3% at December 31, 2008. Unbundled local loops at December 31, 2009 amounted to 2.2 million accesses, of which nearly 21% were shared access loops.

Telefónica Spain's total wholesale ADSL accesses were 0.4 million accesses at December 31, 2009, a decrease of 15.3% compared to the accesses at December 31, 2008, mainly because of the migration to unbundled local loops.

In 2009, Telefónica Spain continued to increase its presence in the pay TV market, achieving a customer base of 0.7 million accesses at December 31, 2009 from 0.6 million accesses at December 31, 2008.

Since 2005 Telefónica Spain has bundled ADSL products with other products in Duo bundles, which include voice and broadband services, and Trio bundles, which include voice, broadband and pay TV services. The total number of Duo and Trio bundles increased by 7.2% to 4.9 million units at December 31, 2009 from 4.5 million units at

December 31, 2008. At December 31, 2009, 88% of Telefónica Spain's broadband accesses were included in Duo or Trio bundles compared to 85% at December 31, 2008.

Table of Contents

Sales and marketing

One of our main priorities has been to satisfy customer needs and increase customer loyalty by improving the quality of our customer service and offering a wide range of integrated telecommunications services. We have reinforced our strategy of customer segmentation in order to tailor our services to best meet the specific needs of each customer segment.

In 2009 we marketed new products and promotions to strengthen our position in the market for fixed-mobile convergence, both for residential and business customers.

In 2009 we were also very active in capturing new fixed telephony customers (which, in many cases, included broadband customers as well) through “free-connection fee” campaigns. These campaigns stimulated new adds. At the same time, we improved the value of fixed lines creating, for example, Línea 3, a new product that offers our customers free national calls to their three most called numbers.

During 2009 Telefónica Spain continued marketing bundled ADSL products, which included voice and pay TV services, and Quadruple bundles, which include fixed telephony, mobile telephony, broadband access and pay TV services, some of these new bundles include:

- Banda ancha total: bundle of fixed and mobile broadband; and
- ADSL + voz móvil: bundle of fixed broadband and free mobile traffic during the weekends.

In September 2009, the CMT modified the regulatory framework for retail offers allowing Telefónica Spain to carry out promotions to its clients under certain conditions and simplifying the replicability analysis of the quadruple play.

In October 2009 Telefónica Spain launched ADSL Libre, a new product that allows customers to subscribe for a broadband connection without the monthly fixed line fee (naked ADSL).

ADSL commercial campaigns carried out to capture new broadband customers were very intense during 2009. In particular, the Semana Loca campaigns introduced new promotions with more attractive prices that allowed Telefónica Spain to better defend its market share.

In the business segment, we continued to promote our Puesto de Trabajo services, which is a package of services designed to meet the voice, data and IT needs for small- and medium-sized businesses.

The customer service model employed by Telefónica Spain, which is focused on achieving the highest degree of efficiency in customer service, has the following features:

- a 24-hour personal customer service line for purchasing any type of product and service and handling customer queries;

- Telefónica stores (Tiendas Telefónica) where customers can test and buy the products we market, including the opening in 2008 of our flagship store at the historic Telefónica headquarters building on the Gran Vía (Madrid), which is the largest telecommunications store in Spain;

- the Telefónica On Line Store, accessible by Internet (www.telefonica.es), which offers customers the ability to order and purchase online the majority of services and products we offer; and

- a customer service system for corporate customers, with a dedicated sales force.

Competition

Telefónica Spain’s main competitors in the fixed telephony market fall within three main categories:

- cable operators, such as Spanish nationwide cable operator ONO, which offers bundles of voice, broadband and pay TV services, and regional cable operators (Euskaltel, Telecable and Grupo R);

Table of Contents

- ULL operators, such as Orange, Jazztel and Vodafone; and
- large-business oriented operators, such as British Telecom and Colt, which offer voice and data virtual private networks (VPNs).

Telefónica Spain’s estimated market share at December 31, 2009 was as follows:

- fixed telephony accesses market share amounted to approximately 72% of retail accesses (down from approximately 77% at December 31, 2008);
- broadband market share amounted to approximately 56% of retail accesses (down from approximately 57% at December 31, 2008); and
- pay TV market share amounted to approximately 17% of the market in terms of accesses (up from approximately 14% at December 31, 2008).

In November 2008, the CMT approved “Wholesale Access for Telephone Lines”, or AMLT, a new product that allows operators to resell telephone lines to their final customers. During 2009 this product has shown a very slow growth.

Network and technology

Telefónica Spain has made significant investments to develop its broadband access business through broadband technology, as well as in capacity and security of its aggregation, transport and data network.

Telefónica Spain - Mobile business (Spain)

Telefónica Spain provides mobile services in Spain through the operator Telefónica Móviles España.

Operations

The Spanish mobile market exceeded 55.6 million accesses at December 31, 2009, which represented a penetration rate of 121%, an increase of more than 5 percentage points from December 31, 2008. The Spanish mobile market showed growth as a result of data services development.

The following table presents, at the dates or for the periods indicated, selected statistical data relating to Telefónica Spain’s mobile business.

	At or for the year ended December 31,		
	2007	2008	2009
Total mobile accesses (in thousands)	22,826.6	23,604.8	23,538.6
Pre-pay accesses (in thousands)	9,181.8	9,037.0	8,204.5
MOU (minutes)	161	156	n.a.
Traffic (millions of minutes)	n.a.	43,568	42,039
ARPU (in euros)	32.3	30.4	27.5

Our mobile customer base in Spain, measured in terms of accesses, stood at 23.5 million accesses at December 31, 2009, a decrease of 0.3% from 23.6 million at December 31, 2008. This evolution was primarily driven by a 9.2% decrease in accesses in the pre-pay segment, which was primarily driven by our decision in December 2009 to disconnect 715 thousand pre-pay mobile accesses from the customer base as a consequence of lower activity levels.

In the context of an increasingly competitive market, with strong competition in number portability and pressure on pricing, Telefónica Móviles España's main commercial objective was to maintain its market leadership in revenue share, based on its competitive tariff scheme, strong focus on high value customers and effective marketing and advertising strategies. Telefónica Spain's mobile business achieved negative net adds of 66 thousand accesses in 2009, compared to positive net adds of 0.8 million accesses in 2008, with a noteworthy number of net accesses gains in the contract segment, 0.8 million accesses in 2009, down from 0.9 million in 2008.

Table of Contents

In terms of portability, which is customers transferring their number to Telefónica Móviles España from a competitor, Telefónica Móviles España's total net adds was a negative figure of 0.2 million lines in 2009. However, by continuing to focus on the higher value customer segments, net portability adds of contract lines was a positive, though significantly smaller, figure of 8.1 thousand lines in 2009.

At December 31, 2009, approximately 65% of our mobile accesses in Spain were contract, which represents an increase of 3.4 percentage points from December 31, 2008.

ARPU for Telefónica Spain's mobile business decreased 9.7% to €27.5 in 2009 from €30.4 in 2008. The decrease was primarily driven by a decrease in voice ARPU of 12.4% to €22.1 in 2009 from €25.2 in 2008 as a result of increased competition, interconnection price cuts, roaming-out regulation and less usage. Outgoing voice ARPU also decreased 10.3% to €19.0 in 2009 from €21.2 in 2008. These decreases were partially offset by an increase in data ARPU of 3.0% to €5.4 in 2009 from €5.2 in 2008, with outgoing data ARPU growing 3.4% to €4.8 in 2009 from €4.7 in 2008.

Traffic for 2009 decreased 3.5% to 42,039 million minutes compared to 43,568 million minutes in 2008 mainly due to a lower voice usage as customers optimized their consumption.

At December 31, 2009, Telefónica Spain's customers held more than 8.9 million UMTS/HSDPA handsets, an increase of 12 percentage points from December 31, 2008.

Sales and marketing

Telefónica Spain is focused on key initiatives to preserve its position as a leading mobile operator in the market, leading it to increase commercial efforts with measures including:

- in-depth market segmentation, with a focus on customer value;
- programs to promote customer loyalty; and
- pricing policies to stimulate usage, including launching segmented packages and innovative tariff options.

Since Telefónica Spain began providing mobile services in Spain, its sales and marketing strategy has been to generate increased brand awareness and customer satisfaction to achieve customer growth and increased revenues. Telefónica Spain utilizes several types of marketing channels, including television, radio, exterior billboards, telemarketing, direct mail and Internet advertising. Telefónica Spain also sponsors several cultural and sporting events in order to increase its brand recognition.

During 2009 Telefónica Spain's main marketing campaigns focused on boosting demand for mobile broadband, with the launch of data flat rates for browsing the web by a handset or small screen (to access contents, music, television, etc.) as well as browsing the web with laptops or big screen, developing new concepts and campaigns such as "try and buy". In addition, Telefónica Spain offers access to mobile broadband services with HSPA technology. These favorable data rates and mobile broadband capable devices have been bundled by Telefónica Spain in order to promote an increase in the number of accesses and level of use of mobile broadband services in Spain. In order to help achieve this goal:

- In June 2009, Telefónica launched mobile broadband services for pre-pay customers.
-

In September 2009, Telefónica launched “mstore” with a catalogue of more than 1,000 mobile telephony applications and services, available to all Movistar customers, and ready to download to mobile phones and computers.

- Also, in November 2009, Telefónica launched HSPA+ services and tariffs which allow downloading at peak speeds of 21 Mbs.

27

Table of Contents

Competition

Telefónica Spain's main competitors in the Spanish market for mobile communications service are: Vodafone España, a subsidiary of Vodafone plc, Orange, which is the trade name of France Telecom España S.A., Yoigo, whose principal shareholder is TeliaSonera, and other MVNO operators.

Telefónica Spain's estimated market share in Spain in terms of mobile accesses was approximately 42% at December 31, 2009 (down from approximately 44% at December 31, 2008).

Network and technology

Telefónica Spain's digital network in Spain is based upon the GSM/UMTS standard. The prevalence of the GSM standard, together with Telefónica Spain's international roaming agreements, enable its mobile customers to make and receive calls in more than 200 countries worldwide. Telefónica Spain's GSM/UMTS based network provides its customers with access to many of the most advanced mobile handsets and a full range of services and products.

In 2009, Telefónica Spain invested in building out and enhancing its networks in Spain and developing its technological platforms and information systems. At December 31, 2009, Telefónica Spain's GSM/GPRS digital network in Spain consisted of approximately 22,293 base stations of 2G. In 2009, Telefónica Spain accelerated the expansion of its UMTS network with 1,547 new base stations with a total of more than 10,820 UMTS base stations installed at the end of the year.

Telefónica Europe

Telefónica Europe's principal activities are the provision of fixed and mobile telephony services, Internet and data services in the United Kingdom, Germany, the Czech Republic and the Isle of Man, mobile telecommunications services in Ireland and Slovakia and pay TV in Czech Republic.

The following table presents, at the dates indicated, selected statistical data relating to our operations in Europe.

	At December 31,		
	2007	2008	2009
		(in thousands)	
Fixed telephony accesses	2,130.0	1,952.7	1,827.5
Internet and data accesses	880.0	1,354.5	1,754.7
Narrowband accesses	202.4	163.4	137.3
Broadband accesses	670.3	1,158.7	1,589.1
Other accesses	7.3	32.4	28.3
Mobile accesses	38,263.8	41,401.8	44,095.0
Pay TV accesses	73.2	114.5	137.6
Final clients accesses	41,347.0	44,823.5	47,814.9
Wholesale accesses	706.2	1,237.9	1,425.2
Total accesses	42,053.2	46,061.4	49,240.1

Telefónica Europe's total accesses increased 6.9% to 49.2 million accesses at December 31, 2009 from 46.1 million accesses at December 31, 2008. Total accesses at December 31, 2009 included 44.1 million mobile accesses, 1.8 million fixed telephony accesses, 1.8 million Internet and data accesses and 0.1 million pay TV accesses. Additionally, it included 1.4 million ADSL wholesale accesses.

Table of Contents

United Kingdom – Telefónica O2 UK

Operations

The following tables present, at the dates or for the periods indicated, selected statistical data relating to our operations in the United Kingdom.

	At December 31,		
	2007	2008	2009
	(in thousands)		
Internet and data accesses	70.7	340.9	591.5
Broadband accesses	70.7	340.9	591.5
Mobile accesses	18,382.1	20,274.7	21,299.3
Pre-pay accesses	11,573.4	11,862.5	11,740.3
Final clients accesses	18,452.8	20,615.6	21,890.8
Total accesses	18,452.8	20,615.6	21,890.8

	Year ended December 31,		
	2007	2008	2009
MOU (minutes)	190	207	n.a.
Traffic (millions of minutes)	n.a.	46,585	53,856
ARPU (in euros)	34.4	29.0	24.7

The mobile penetration rate in the United Kingdom was approximately 126% at December 31, 2009, an increase of approximately 3 percentage points compared to the penetration rate at December 31, 2008.

Total accesses for Telefónica O2 UK, Telefónica Europe’s operating company in the United Kingdom, increased 6.2% to 21.9 million accesses at December 31, 2009 compared to 20.6 million accesses at December 31, 2008 (excluding the Tesco mobile customer base, which is the result of a joint venture in which Telefónica O2 UK holds a 50% stake and whose customers use the Telefónica O2 UK network). Telefónica O2 UK, had net adds of 1.3 million accesses in 2009, 41.0% less than its net additions in 2008.

Telefónica O2 UK added 1.1 million mobile contract accesses in 2009, bringing the total at December 31, 2009 to 9.6 million mobile contract accesses, an increase of 13.6% from December 31, 2008. Pre-pay mobile accesses decreased from 11.9 million accesses from December 31, 2008 to 11.7 million accesses at December 31, 2009. At December 31, 2009 mobile contract accesses made up 44.9% of Telefónica O2 UK’s mobile customer base, compared to 41.5% at December 31, 2008. At December 31, 2009 Telefónica O2 UK had 0.6 million broadband accesses compared to 0.3 million broadband accesses at December 31, 2008.

Contract ARPU decreased to €40.8 in 2009 from €48.6 in 2008 (a decrease of 5.9% in local currency). Pre-pay ARPU decreased to €12.3 in 2009 from €15.5 in 2008 (a decrease of 11.0% in local currency). ARPU was €24.7 in 2009 down from €29.0 in 2008 (a decrease of 4.4% in local currency). This decrease in local currency ARPU was caused by MTR regulation (which resulted in an average rate decrease of approximately 11% year-on-year) and customers’ usage optimization. Traffic in 2009 increased 15.6% to 53,856 million minutes compared to 46,585 million minutes in 2008.

Sales and marketing

In the United Kingdom, we use a broad range of marketing channels, including television, radio, billboards, telemarketing, direct mail, internet advertising and sponsorship to market Telefónica O2 UK's products and services.

In 2009, Telefónica O2 UK continued its focus on high-value customers across various segments and offered a wide range of smart phones such as the iPhone 3GS and the Palm Pre, in addition to mobile and fixed broadband representing one of the key drivers of revenue growth in 2009.

Table of Contents

In 2009 Telefónica O2 UK was voted “Best Network” for the second consecutive year at Mobile Awards 2009.

Competition

Telefónica O2 UK’s estimated market share was approximately 26.2% at December 31, 2009 compared with approximately 25.9% at December 31, 2008, based on the number of mobile accesses.

In addition to Telefónica O2 UK, there are currently four other network operators in the UK mobile telecommunications market: Vodafone UK, a subsidiary of Vodafone plc, T-Mobile UK, a subsidiary of Deutsche Telecom AG, Orange, owned by France Telecom, and 3, owned by Hutchison Whampoa. MVNOs operating in the UK market include Virgin Mobile and Talk-Talk, owned by Virgin Media and The Carphone Warehouse Group, respectively, which respectively use the T-Mobile UK and Vodafone network, and Tesco Mobile, a joint venture in which Telefónica O2 UK holds a 50% stake, and which uses the Telefónica O2 UK network.

We understand that a proposed joint venture between France Telecom and Deutsche Telekom’s UK operators (Orange UK and T-Mobile UK, respectively) is currently being analyzed by regulators.

At December 31, 2009, Telefónica O2 UK also provides the network infrastructure for LycaMobile, a mobile virtual network operator (MVNO) who competes with us and pays Telefónica O2 UK to use its network.

Network and technology

Telefónica O2 UK’s digital network in the United Kingdom is based upon the GSM/UMTS standard. The prevalence of the GSM standard, together with Telefónica O2 UK’s international roaming agreements, enables Telefónica O2 UK’s customers to make and receive calls in more than 200 countries worldwide. At December 31, 2009, Telefónica O2 UK’s GSM/UMTS digital network consisted of approximately 11,817 base stations.

Telefónica O2 UK had rolled out ULL capabilities to 1,245 exchanges by the end of 2009, giving its broadband network population coverage of 67.2% in terms of the UK population.

Germany – Telefónica O2 Germany

Operations

The following tables present, at the dates or for the periods indicated, selected statistical data relating to our operations in Germany.

	At December 31,		
	2007	2008	2009
	(in thousands)		
Internet and data accesses	74.7	214.8	285.1
Broadband accesses	74.7	214.8	285.1
Mobile accesses	12,471.5	14,198.5	15,507.4
Pre-pay accesses	6,235.0	7,231.5	7,807.0
Final clients accesses	12,546.2	14,413.3	15,792.5
Wholesale accesses	596.0	1,128.4	1,316.8
Total accesses	13,142.3	15,541.7	17,109.3

	Year ended December 31,		
	2007	2008	2009
MOU (minutes)	131	138	n.a.
Traffic (millions of minutes)	n.a.	22,313	23,257
ARPU (in euros)	20.4	17.4	15.6

The mobile penetration rate in Germany was approximately 132% at December 31, 2009, similar to the penetration rate at December 31, 2008.

Table of Contents

The total customer base of Telefónica O2 Germany, Telefónica Europe's operating company in Germany, increased by 1.6 million accesses from December 31, 2008 to 17.1 million accesses at December 31, 2009. Telefónica O2 Germany's joint venture with Tchibo Mobile was responsible for 0.1 million of this increase in accesses from December 31, 2008 to 1.4 million accesses at December 31, 2009, while Telefónica O2 Germany's "Fonic" low-cost brand, added 0.6 million accesses from December 31, 2008, giving it a customer base of 1.3 million accesses at December 31, 2009.

Telefónica O2 Germany had net adds of 0.7 million mobile contract accesses and 0.6 million mobile pre-pay accesses in 2009, bringing the contract and pre-pay customer base at December 31, 2009 to 7.7 million accesses and 7.8 million accesses respectively.

At December 31, 2009, Telefónica O2 Germany had a customer base of 0.3 million broadband accesses. Telefónica O2 Germany reported 1.3 million ULL lines at December 31, 2009, an increase of 16.7% from 1.1 million ULL lines at December 31, 2008.

ARPU continued to decline in 2009, decreasing 9.9% to €15.6 in 2009 from €17.4 in 2008, partly as a result of an approximately 14% regulated cut in MTRs in April 2009 and the fierce level of competition in the German market. Contract ARPU decreased 10.0% to €26.1 in 2009 from €29.0 in 2008. Pre-pay ARPU decreased 4.4% to €5.7 in 2009 from €5.9 in 2008. Traffic in 2009 increased 4.2% to 23,257 million minutes compared to 22,313 million minutes in 2008.

Sales and marketing

During 2009 Telefónica O2 Germany revised its commercial model, replacing existing tariffs such as "Genion S/M/L/XL", with the new and innovative "O2 o" proposition, where customers have contracts with no minimum spend, and a monthly cap for voice and SMS. As a result of this new commercial proposition "My Handy" has been introduced which separates the handset from the traditional subsidized mobile phone contract, with customers acquiring a separate contract for a handset. The "Inklusivpaket" plan continues to be marketed as a data tariff.

Telefónica O2 Germany continued to build on its core strategy of increasing its distribution network, which was broadly in line with target at 940 shops at year end.

Competition

Telefónica O2 Germany's estimated market share in Germany was approximately 14.3% at December 31, 2009 compared to approximately 13.5% at December 31, 2008, based on number of mobile accesses.

Telefónica O2 Germany competes primarily with three other companies in the German market for mobile telecommunications. These are T-Mobile, which is owned by Deutsche Telecom AG, Vodafone Germany, a subsidiary of Vodafone plc, and E-Plus, which is owned by KPN. Telefónica O2 Germany also competes with several MVNOs.

Network and technology

Telefónica O2 Germany's digital network in Germany is based upon the GSM/UMTS standard. The prevalence of the GSM standard, together with Telefónica O2 Germany's international roaming agreements, enables Telefónica O2 Germany customers to make and receive calls in more than 200 countries worldwide.

At December 31, 2009, Telefónica O2 Germany's GSM/UMTS digital network consisted of approximately 17,210 base stations.

Table of Contents

Czech Republic and Slovakia – Telefónica O2 Czech Republic and Telefónica O2 Slovakia

Telefónica Europe provides fixed line, pay TV, and mobile services in the Czech Republic and mobile services in Slovakia, where it launched operations during the first quarter of 2007.

Operations

The following tables present, at the dates or for the periods indicated, selected statistical data relating to our operations in the Czech Republic (data excludes Slovakia).

	At December 31,		
	2007	2008	2009
	(in thousands)		
Fixed telephony accesses	2,069.2	1,893.4	1,770.6
Internet and data accesses	719.1	779.5	848.7
Narrowband accesses	202.4	163.4	137.6
Broadband accesses	509.4	583.7	683.2
Other accesses	7.3	32.4	28.3
Mobile accesses	5,125.4	4,802.1	4,944.6
Pre-pay accesses	2,881.5	2,282.8	2,130.2
Pay TV accesses	73.2	114.5	137.6
Final clients accesses	7,986.8	7,589.5	7,701.5
Wholesale accesses	110.2	109.5	108.4
Total accesses	8,097.0	7,698.9	7,810.0

	Year ended December 31,		
	2007	2008	2009
MOU (minutes)	117	121	n.a.
Traffic (millions of minutes)	n.a.	7,420	8,232
ARPU (in euros)	18.9	22.8	19.3

The mobile penetration rate in the Czech Republic was approximately 134% at December 31, 2009, approximately 3 percentage points higher than the penetration rate at December 31, 2008.

Fixed telephony accesses for Telefónica O2 Czech Republic, Telefónica Europe’s operating company in the Czech Republic, decreased by 6.5% to 1.8 million accesses at December 31, 2009 from 1.9 million accesses at December 31, 2008, mainly as the result of fixed-to-mobile substitution.

Telefónica O2 Czech Republic’s broadband accesses increased 17.0% compared to December 31, 2008 to 0.7 million accesses at December 31, 2009. The pay TV customer base increased 20.2% to 0.1 million accesses at December 31, 2009. These increases are primarily as a result of increased demand for these services in the Czech Republic.

Telefónica O2 Czech Republic’s mobile accesses increased 3.0% to 4.9 million accesses at December 31, 2009, from 4.8 million accesses at December 31, 2008. Contract mobile accesses accounted for 56.9% of these accesses at December 31, 2009, up from 52.5% at December 31, 2008. The number of pre-pay mobile accesses decreased 43.1%, to 2.1 million accesses at December 31, 2009 from 2.3 million accesses at December 31, 2008.

ARPU decreased to €19.3 in 2009 from €22.8 in 2008 (a reduction of 10.5% in local currency). Pre-pay ARPU decreased to €8.5 in 2009 from €11.4 in 2008 (a reduction of 21.9% in local currency), primarily due to customers optimizing their tariffs and calling patterns. Contract ARPU decreased to €28.2 in 2009 from €33.5 in 2008 (a decrease of 12.0% in local currency), primarily due to regulated MTR cuts (approximately 22.7% year-on-year) and customers optimizing their spending. Traffic in 2009 increased 11.0% to 8,232 million minutes compared to 7,420 million minutes in 2008.

Table of Contents

Sales and marketing

During 2009 the dominant mobile proposition of Telefónica O2 Czech Republic remained the "O2 Neon" tariffs launched in 2008, which are designed to stimulate traffic through a simplified, flat tariff structure. In 2009 a new concept was launched in fixed segment, called "O2 Home", where subscribers can purchase DSL packages without the need to have a fixed line. Within the O2 Home offering are options to subscribe for bundled products, including mobile broadband, mobile tariffs and IPTV at more advantageous prices.

Competition

There are currently two other primary competitors in the Czech Republic mobile telecommunications market, Vodafone Czech Republic, which is owned by Vodafone plc., and T-Mobile, which is part of Deutsche Telecom AG.

Telefónica O2 Czech Republic had an estimated mobile market share of approximately 39.2% at December 31, 2009 compared to approximately 38.6% at December 31, 2008, based on number of mobile accesses.

The fixed telephony market in the Czech Republic consists of six large operators and a number of other smaller providers. In voice the major competitors are U:fon, UPC and other cable operators which also provide integrated voice, Internet and pay TV offers. Internet service is offered by all major mobile operators as well as a large volume of WiFi providers. Pay TV is dominated by a number of cable and satellite companies, the biggest being UPC.

Network and technology

Telefónica O2 Czech Republic's digital network in the Czech Republic is based upon the GSM/UMTS standard. The prevalence of the GSM standard, together with Telefónica O2 Czech Republic's international roaming agreements, enables its customers to make and receive calls in more than 200 countries worldwide.

At December 31, 2009, Telefónica O2 Czech Republic's GSM/UMTS digital network consisted of 4,786 base stations.

Slovakia

At December 31, 2009, Telefónica O2 Slovakia's total number of mobile accesses amounted to 0.6 million accesses, an increase of 69.9% compared to December 31, 2008. Contract mobile accesses accounted for 35.4% of these accesses at December 31, 2009 compared to 30.4% at December 31, 2008. Throughout 2009, Telefónica O2 Slovakia continued with "O2 Fér" plan, a simple tariff which unifies pre-pay and contract mobile rates and offers SIM-only products without a handset subsidy.

In 2009, Telefónica O2 Slovakia continued to roll out its own network infrastructure, and by December 31, 2009 the company had 917 base stations, which fulfilled its license conditions.

Table of Contents

Ireland – Telefónica O2 Ireland

Operations

The following tables present, at the dates or for the periods indicated, selected statistical data relating to our operations in Ireland:

	At December 31,		
	2007	2008	2009
	(in thousands)		
Total mobile accesses	1,646.1	1,727.7	1,714.3
Pre-pay accesses	1,090.9	1,084.6	1,022.5

	Year ended December 31,		
	2007	2008	2009
MOU (minutes)	248	245	n.a.
Traffic (millions of minutes)	n.a.	4,867	4,672
ARPU (in euros)	45.9	43.2	39.6

The mobile penetration rate in Ireland was approximately 120% at December 31, 2009, approximately 1 percentage point lower than the penetration rate at December 31, 2008.

Telefónica O2 Ireland had net losses of 13 thousand mobile accesses in 2009. Telefónica O2 Ireland's customer base, in terms of mobile accesses, decreased 0.8% from December 31, 2008 to 1.7 million mobile accesses at December 31, 2009.

Telefónica O2 Ireland had net adds of 49 thousand contract mobile accesses in its mobile business in 2009, a decrease of 44.6% on December 31, 2008.

ARPU decreased by 8.3% in 2009 to €39.6 from €43.2 in 2008. Contract ARPU decreased 14.6% to €62.0 in 2009 from €72.5 in 2008 due to a different price plan mix. Pre-pay ARPU decreased by 5.7% in 2009 to €25.5 in 2009 from €27.0 in 2008. Traffic in 2009 decreased 4.0% to 4,672 million minutes compared to 4,867 million minutes in 2008 primarily due to voice to text substitution.

Sales and marketing

During 2009, Telefónica O2 Ireland continued to be the exclusive provider of the iPhone, with the new version 3GS having been launched in June. The second half of the year saw the launch of the new O2 exclusive Palm Pre phone, and pre-pay mobile internet.

Competition

There are currently three other primary competitors in the Irish mobile telecommunications market: Vodafone Ireland, which is part of Vodafone plc, Meteor, which is part of Eircom, and 3 Ireland, which is part of Hutchison Wampoa.

Telefónica O2 Ireland had an estimated market share of the Irish mobile market of approximately 32.3% at December 31, 2009 compared to approximately 32.5% at December 31, 2008, based on number of mobile accesses.

Network and technology

Telefónica O2 Ireland's digital network in Ireland is based upon the GSM/UMTS standard. The prevalence of the GSM standard, together with Telefónica O2 Ireland's international roaming agreements, enables Telefónica O2 Ireland customers to make and receive calls in more than 200 countries worldwide.

At December 31, 2009, Telefónica O2 Ireland's GSM/UMTS digital network consisted of approximately 1,692 base stations.

Table of Contents

Telefónica Latin America

Telefónica Latin America provides fixed and mobile telephony, Internet and data services and pay TV services through the operators described in the following sections in the main Latin American markets. In addition, Telefónica Latin America's other members include: Telefónica Empresas, Telefónica International Wholesale Services (TIWS), the business unit responsible for other telecommunications operators and for managing our international services and the network which supports these services, and Terra Networks Latin América.

The following table presents statistical data relating to our operations in Latin America:

	At December 31,		
	2007	2008	2009
	(in thousands)		
Fixed telephony accesses	25,381.0	25,644.5	24,578.3
Internet and data accesses	6,954.8	7,629.8	7,605.2
Narrowband accesses	1,815.6	1,445.8	1,070.6
Broadband accesses	5,035.9	6,067.0	6,426.8
Other accesses	103.4	117.0	107.8
Mobile accesses	100,542.2	123,385.2	134,698.9
Pay TV accesses	1,163.8	1,540.5	1,648.6
Final clients accesses	134,041.8	158,200.1	168,531.1
Wholesale accesses	62.6	59.0	56.1
Total accesses	134,104.4	158,259.0	168,587.2

Telefónica Latin America's total accesses increased 6.5% to 168.6 million accesses at December 31, 2009 from 158.3 million accesses at December 31, 2008. Total accesses at December 31, 2009 include 134.7 million mobile accesses, 24.6 million fixed telephony accesses, 7.6 million Internet and data accesses and 1.6 million pay TV accesses. Additionally, it includes 56 thousand wholesale accesses.

The following table sets forth certain information at December 31, 2009 regarding the principal Latin American operating companies of Telefónica Latin America.

Country	Company	Population (in millions)	Interest (%)
Brazil	Telecomunicações de São Paulo, S.A.—Telesp	41.26(*)	87.95
	Brasilcel, N.V.(1)	192.3	50.00
Mexico	Telefónica Móviles México, S.A. de C.V.	110.6	100.00
Panama	Telefónica Móviles Panamá, S.A.	3.5	100.00
Nicaragua	Telefónica Móviles Nicaragua, S.A.	5.5	100.00
Guatemala	Telefónica Móviles Guatemala, S.A.	13.7	99.98
El Salvador	Telefónica Móviles El Salvador, S.A. de C.V.	5.9	99.08
Venezuela	Telcel, S.A.	28.4	100.00
Colombia	Colombia Telecomunicaciones, S.A. ESP.	45.2	52.03
	Telefónica Móviles Colombia, S.A.		100.00
Peru	Telefónica del Perú, S.A.A.	28.2	98.34
	Telefónica Móviles Perú, S.A.C.		100.00
Ecuador	Otecel, S.A.	14.1	100.00

Argentina	Telefónica de Argentina, S.A.	40.1	100.00
	Telefónica Móviles Argentina S.A.		100.00
Chile	Telefónica Chile, S.A.	16.7	97.89
	Telefónica Móviles Chile, S.A.		100.00
Uruguay	Telefónica Móviles Uruguay, S.A.	3.4	100.00

(*) Concession area only.

(1) Jointly controlled and managed by Telefónica and Portugal Telecom. Brasilcel is the holding company which controls the mobile operating company Vivo.

Table of Contents

Brazil

The following table presents, at the dates indicated, selected statistical data relating to our operations in Brazil.

	At December 31,		
	2007	2008	2009
	(in thousands)		
Fixed telephony accesses	11,960.0	11,661.9	11,253.8
Internet and data accesses	3,288.6	3,625.8	3,440.2
Narrowband accesses	1,155.9	996.4	723.1
Broadband accesses	2,069.6	2,557.8	2,638.4
Other accesses	63.1	71.6	78.7
Mobile accesses	33,483.5	44,945.0	51,744.4
Pre-pay accesses	27,236.4	36,384.0	41,960.7
Pay TV accesses	230.9	472.2	487.2
Final clients accesses	48,963.1	60,704.9	66,925.7
Wholesale accesses	37.4	34.1	34.2
Total accesses	49,000.5	60,739.1	66,959.8

Telefónica Latin America’s accesses in Brazil increased 10.2% to 67.0 million accesses at December 31, 2009 from 60.7 million accesses at December 31, 2008. This growth reflects a 15.1% year-on-year increase in Vivo’s (Telefónica Latin America’s jointly-controlled Brazilian mobile business) customer base and, to a lesser extent, the expansion of Telecomunicações de São Paulo, S.A.’s, or Telesp’s, (Telefónica Latin America’s Brazilian fixed line business) broadband and pay TV businesses. These increases were offset by a reduction in the number of fixed telephony accesses at Telesp and a decrease in narrowband Internet accesses primarily as a result of a modest migration to broadband accesses.

Brazil Fixed Business – Telecomunicações de São Paulo, S.A. – Telesp

Operations

Telesp provides fixed telephony and other telecommunications services in the Brazilian state of São Paulo under concessions and licenses from Brazil’s federal government.

Telesp’s fixed telephony, Internet and data and pay TV accesses decreased 3.7% to 15.2 million accesses at December 31, 2009 from 15.8 million accesses at December 31, 2008, primarily due to the reduction in the number of fixed telephony accesses, within the context of increased fixed-to-mobile substitution as a result of the growth in Brazil’s mobile sector, and a decrease in narrowband Internet accesses, as a result of migration to broadband solutions, that was not compensated by broadband accesses increase. Telesp’s fixed telephony accesses decreased 3.5% to 11.3 million accesses at December 31, 2009 from 11.7 million accesses at December 31, 2008. Of these, 25.8% were pre-pay accesses or accesses with consumption limits.

The Brazilian broadband market continued to grow in 2009. Telesp increased its broadband customer base by 3.2% to 2.6 million accesses at December 31, 2009. This moderate increase was affected by the decision of ANATEL, the Brazilian telecommunications regulator, to suspend the sale of Telesp’s broadband products from June 22, 2009 to August 27, 2009 as a result of several technical problems on our network. Telesp offers pay TV mainly through a DTH solution and, since the fourth quarter of 2007 after the acquisition of Navy Tree, also offers MMDS technology, reaching 0.5 million accesses at December 31, 2009, 15 thousand accesses more than at December 31, 2008.

Telesp's voice traffic, measured in minutes, decreased by 5.0% in 2009 compared to 2008, mainly due to lower local and long distance traffic that was not compensated by higher interconnection traffic coming primarily from mobile networks. Fixed local traffic, measured in minutes, decreased 7.4% due to lower fixed telephony accesses, and the implementation of flat rates and minutes bundles. Fixed-to-mobile traffic, measured in minutes, fell 7.9% in 2009 compared to 2008 as a result of a migration of traffic to mobile networks.

Sales and marketing

In Brazil, we employ a differentiated approach to marketing whereby we use a mix of human and technological resources (a specialized team and business intelligence tools, respectively), in addition to specific studies that allow us to target various market segments according to the relevant needs of the customers in each segment. We continuously monitor market trends in an effort to develop new products and services that may address the future needs of our customers.

Telefónica Latin America employs the following strategies to deliver fixed telephony and other telecommunications solutions to residential, small and medium enterprises, or SMEs, and corporate customers in Brazil:

- person-to-person sales: customized sales services to achieve and preserve customer loyalty, customized consulting telecommunication services and technical and commercial support;
- telesales: a telemarketing channel;
- indirect channels: outsourced sales by certified companies in the telecommunications and data processing segments to provide an adequately sized network for our products and services;
- Internet: the Telefónica website;
- virtual shop for corporate clients: a “gateway” for our corporate customers to acquaint themselves with our portfolio through the Internet; and
- door-to-door: door-to-door sales of services by consultants in the State of São Paulo in order to approach more SMEs to convert them into Telefónica Negocios clients.

We offer bundled products, which include both local and long-distance traffic and minutes bundled with broadband. We believe that the trend towards bundled offers in Brazil will continue to grow, and that further developing such offers will be important to maintaining our competitiveness in the market. Also, in 2009 Telesp launched its “X-treme” products, based on FTTX technology, and its IPTV services as well.

Competition

Our fixed telephony business in Brazil currently faces strong competition in the corporate and premium residential segments in respect of several types of services. In the corporate segment, there is strong competition in both voice services (local and long distance) and data transmission, resulting in greater retention costs to maintain client relationships.

Our main competitors in the corporate fixed telephony line segment are Oi, Intelig and Embratel, a subsidiary of Telmex International. In the high-income residential service segment, we compete for long-distance customers with Embratel and for broadband customers with cable TV providers, mainly NET Serviços de Comunicação S.A., or Net. For the local voice and high-income segments, we also face increasing competition from mobile telecommunications services, which have lower rates for certain types of calls, such as mobile-to-mobile calls. Such competition increases our advertising and marketing costs. We are taking several steps to defend ourselves from increasing competition. We are focused on improving our broadband products, by offering bundled services that include voice, broadband and television, and by increasing the access speed offered to our clients. In addition, we are improving our market segmentation and developing more competitive products intended to defend our client base from our competitors' product offerings and to defend our market share.

In the low-income, local fixed telecommunications segment, we face less direct competition due to the low profitability of this market. The most significant competition is from pre-pay mobile telecommunications providers.

Telesp had an estimated market share in the fixed telephony market in the State of São Paulo of approximately 74.4% at December 31, 2009 based on the number of fixed telephony accesses, down from approximately 83.5%

Table of Contents

at December 31, 2008. This decrease is mainly due to intense competition from Net, which offers its “Net Phone” service as part of its offer of pay TV and broadband.

Network and technology

During the first half of 2009, Telesp had some problems with its network that affected the quality of the service of some products, particularly broadband. In order to guarantee the stability of the service, ANATEL suspended the sale of “Speedy”, our broadband product, on June, 22, 2009. That suspension was temporary and subject to the implementation by Telesp of an action plan to improve the service. Telesp presented its action plan that included capital expenditures and customer care and network expenses. As a result of this, the suspension was revoked on August, 27, 2009. In addition, Telesp continued through 2009 to develop its ADSL network as long as the deployment of the fiber access network.

Brazil mobile business – Brasilcel (Vivo)

Operations

With approximately 174 million mobile accesses, Brazil ranked first in Latin America in terms of number of mobile accesses at December 31, 2009. At December 31, 2009, Brazil had an estimated mobile market penetration rate of approximately 90.5%, compared to approximately 79% at December 31, 2008.

Telefónica and Portugal Telecom are 50:50 shareholders in Brasilcel, a joint venture which combines Telefónica’s and Portugal Telecom’s mobile businesses in Brazil. This joint venture is the leading mobile operator in Brazil in terms of number of mobile accesses at December 31, 2009. All of the operating companies participating in the joint venture have been operating under the brand name “Vivo” since April 2003. The licensed areas of Brasilcel include 20 states in Brazil with an aggregate population of approximately 192.3 million people.

Vivo’s customer base, in terms of number of accesses, increased 15.1% to 51.7 million accesses at December 31, 2009 from 44.9 million accesses at December 31, 2008. Of these, 9.8 million were mobile contract accesses. The primary factors contributing to this growth include the increasing importance of the new mobile broadband accesses, the wider range of handsets available, Vivo’s leadership in terms of brand and distribution chain, ongoing marketing campaigns for pre-pay mobile traffic and an improved capacity to attract contract mobile accesses first with Vivo Escolha plans and with Vivo Voçe. Vivo Voçe, launched to improve Vivo Escolha plans, started to be commercialized at the end of November 2009. These plans are customized plans that allow customers to choose the mix of services with an extra bunch of free voice minutes, messaging, or mobile Internet access. Vivo Voçe also helped to increase customer loyalty by encouraging increased minute consumption and maintaining the perception on the market of Vivo’s lower prices than its competitors. These plans are divided into different categories depending on the number of minutes included as well as additional upgrade features, such as extra SMS, extra minutes of long distance calls and extra MMS, with the improvement of being able to choose two of these upgrades instead of one as in the previous plans and include a 3G Internet upgrade option.

	Year ended December 31,		
	2007	2008	2009
Traffic (millions of minutes)	n.a.	40,547	52,134
ARPU (in euros)	11.9	11.2	9.9

Traffic in 2009 increased 28.6% to 52,134 million minutes compared to 40,547 million minutes in 2008 due to the characteristics of the promotions offered by Vivo in 2009, which focused on the pre-pay mobile segment and control lines, which require minimum consumption and a prepaid "recharge" when such consumption is complete.

ARPU was €9.9 in 2009 compared to €11.2 in 2008 (a decrease of 8.6% in local currency). The decrease in local currency reflected the increased proportion of "SIM only" accesses in the pre-pay customer base and control accesses in the contract customer base, despite the growth in data consumption.

Table of Contents

Sales and marketing

Vivo actively manages its distribution channels, which consisted of approximately 12,070 points of sale at December 31, 2009. Also, pre-pay mobile customers have access to a wide range of "recharge" points. Credit recharges can also be made by electronic transfers through the commercial banking network. At December 31, 2009, approximately 18.9% of Vivo's customer base were contract mobile accesses and the remaining 81.1% were pre-pay mobile accesses. Contract mobile accesses growth was driven by customer acquisition and retention campaigns focused on high-value customers, with an emphasis on the Vivo Escolha and Vivo Voçe plans.

Competition

Vivo was the leading mobile operator in Brazil in terms of number of accesses at December 31, 2009. The growth of the Brazilian market was considerable during the past years while being accompanied by an increase in competition due to the introduction of new competitors in the regions in which Vivo operates. Vivo's major competitors are subsidiaries of Telecom Italia, America Móvil and Oi.

Vivo's estimated market share in terms of mobile accesses in the Brazilian mobile markets in which it operates was approximately 29.7% at December 31, 2009, down from approximately 30.0% market share at December 31, 2008.

Network and technology

The licenses granted to the companies integrated under the Vivo brand allow operations over the WCDMA, GSM, CDMA, CDMA 1XRTT, CDMA EVDO and TDMA systems. Vivo offers both analog and digital services in the bands of 800 MHz, 1900 MHz and 2100 MHz. In 2009 migration from the CDMA to the GSM network continued. Vivo's GSM customer base at December 31, 2009 amounted to 40.7 million accesses, 78.7% of its total customer base.

Venezuela

Venezuela mobile business – Telcel, S.A. – Telcel

Operations

The following table presents, at the dates indicated, selected statistical data relating to our operations in Venezuela.

	At December 31,		
	2007	2008	2009
	(in thousands)		
Total mobile accesses	9,434.0	10,584.0	10,531.4
Pre-pay accesses	8,900.3	9,970.7	9,891.1
Fixed wireless accesses	995.9	1,312.8	1,214.3
Pay TV	—	8.5	62.8
Total accesses	10,429.9	11,905.3	11,808.5

The mobile penetration rate in Venezuela stood at an estimated 100.6% at December 31, 2009, an increase of approximately 0.5 percentage points from December 31, 2008.

Table of Contents

Telefónica Latin America operates in Venezuela through Telcel, S.A., or Telcel, whose accesses decreased 0.8% to 11.8 million accesses at December 31, 2009 from 12.0 million accesses at December 31, 2008, mainly due to intense competition.

	Year ended December 31,		
	2007	2008	2009
Traffic (millions of minutes)	n.a.	14,993	14,951
ARPU (in euros)	16.3	16.9	21.2

Traffic in 2009 decreased 0.3% to 14,951 million minutes from 14,993 million minutes in 2008, due to lower quality pre-pay mobile accesses and lower contract mobile accesses usage.

ARPU for 2009 was €21.2 compared to €16.9 in 2008 (an increase of 19.2% in local currency and excluding the effects of Venezuela being considered a hyperinflationary economy in 2009). The increase in local currency and excluding the effects of Venezuela being considered a hyperinflationary economy in 2009 reflected the increase in tariffs, the increased proportion of contract mobile accesses in the customer base and the continued growth in data revenues.

Sales and marketing

In Venezuela, we use a broad range of marketing channels, including television, radio, billboards, telemarketing, direct mail and Internet advertising to market our products. At December 31, 2009, 6.1% of our mobile accesses in Venezuela were contract mobile accesses, while approximately 93.9% were pre-pay mobile accesses.

In 2009 the company continued implementing its strategy of offering a wider range of exclusive handsets, including the launch of several Blackberry models.

Competition

The major competitors in the Venezuela mobile business are Movilnet and Digitel. Movilnet is a mobile services communication provider owned by the public operator CANTV. Movilnet currently uses CDMA and GSM technologies. In late December, it launched 3.5G service. Digitel is a mobile communications provider that uses GSM technology and focuses its strategy on mobile internet services based on 3G.

According to the Comisión Nacional de Telecomunicaciones de la República Bolivariana de Venezuela, or CONATEL, CANTV is the incumbent operator in Venezuela with a 46% share of the mobile market (through Movilnet) as of December 31, 2009. CANTV is controlled by the government of Venezuela.

Telefónica's estimated market share in the Venezuelan mobile market, in terms of mobile accesses, was approximately 36.9% at December 31, 2009, down from approximately 37.8% at December 31, 2008.

Network and technology

In Venezuela, we operate a digital network based on the CDMA and GSM standard. In 2009, we deployed an overlay based on UMTS /HSDPA. At December 31, 2009, approximately 66.2% of Telcel's accesses in Venezuela were based on the GSM network. Also, we offer HSUPA technology that offers higher speed to upload data to the web, especially while loading images, e-mails, videos, etc.

Argentina

The following table presents, at the dates indicated, selected statistical data relating to our operations in Argentina.

	At December 31, 2007	2008	2009
	(in thousands)		
Fixed telephony accesses	4,682.5	4,603.1	4,607.7
Fixed wireless accesses	104.3	22.4	36.2
Internet and data accesses	1,149.9	1,284.3	1,351.0
Narrowband accesses	312.2	182.8	112.7
Broadband accesses	819.3	1,082.0	1,238.3
Other accesses	18.4	19.5	—
Mobile accesses	13,629.7	14,829.6	15,931.9
Pre-pay accesses	8,836.0	9,687.6	10,736.8
Final clients accesses	19,462.1	20,717.0	21,890.7
Wholesale accesses	9.3	10.0	9.3
Total accesses	19,471.4	20,726.9	21,900.0

Telefónica Latin America managed a total of 21.9 million accesses in Argentina at December 31, 2009, an increase of 5.7% from December 31, 2008. This increase was underpinned by growth in mobile accesses, which increased by 7.4% to 15.9 million accesses at December 31, 2009 from 14.8 million accesses at December 31, 2008, and in the number of broadband accesses, which increased by 14.4% to 1.2 million accesses at December 31, 2009 from 1.1 million accesses at December 31, 2008.

Argentina fixed business – Telefónica de Argentina S.A.

Operations

Telefónica Latin America conducts its Argentine fixed business through Telefónica de Argentina, the leading provider of fixed telephony services in Argentina in 2009 based on number of accesses, according to information provided by its competitors and regulatory authorities.

Telefónica de Argentina's accesses increased 1.2% to 6.0 million accesses at December 31, 2009 from 5.9 million accesses at December 31, 2008. This modest growth was primarily driven by a 14.4% increase in broadband accesses to 1.2 million accesses at December 31, 2009 from 1.1 million accesses at December 31, 2008. The growth in broadband accesses was accompanied by a slight increase in fixed telephony accesses of 0.1% to 4.6 million accesses at December 31, 2009 from December 31, 2008.

Total voice traffic (measured in minutes) declined 5.6% during 2009 as compared to 2008 despite the sharp growth of mobile-to-fixed traffic. Local and interconnection fixed-to-fixed traffic (measured in minutes) decreased 5.9% and 4.5%, respectively, in the year ended December 31, 2009 compared to the year ended December 31, 2008. Public use telephony traffic (measured in minutes) in 2009 decreased by 18.4% compared to the year ended December 31, 2008.

Sales and marketing

In Argentina, Telefónica de Argentina uses a broad range of marketing channels, including television, radio, billboards, telemarketing, direct mail and Internet advertising to market its fixed telephony products and services. Telefónica de Argentina continued answering customers' needs through the development of its broadband business and by providing them new value added services. Telefónica de Argentina also focused its product strategy on bundles and packages supported by commercial offerings like flat-rate plans (tarifa plana). In 2009, we continued commercializing long distance flat-rate plans. The flat-rate plan was primarily sold with the bundling of broadband access together with a local traffic plan. At December 31, 2009 approximately 67.0% of the broadband customer base subscribed to broadband through a bundled package.

Competition

Telefónica de Argentina is the incumbent provider of fixed telephony services in the southern region of Argentina. However, other licensees currently providing fixed telephony services include Telecom Argentina S.A., Telmex Argentina S.A., Impsat S.A. (acquired by Global Crossing in May 2007) and Port-Hable (Hutchison Telecommunications Argentina S.A.). Claro, a mobile phone company owned by America Móvil, also competes in the fixed telephony market.

Telefónica de Argentina is using its expanded fiber-optic network in the northern region of Argentina to carry long-distance traffic and a multiservice network to provide local service in the three most important cities in the northern region of Argentina where Telecom Argentina, S.A. is the incumbent provider. Telefónica de Argentina expanded and improved its network capacity by the construction of fixed wireless networks and the activation of new lines.

Telefónica de Argentina also competes with Grupo Clarín, a company with a growing broadband and TV businesses as a result of the merger of its affiliate Cablevisión with Multicanal in 2007.

Telefónica had an estimated market share in the Argentine fixed telephony market of approximately 47.8% at December 31, 2009 based on number of fixed telephony accesses, down from approximately 48.1% at December 31, 2008.

Network and technology

Telefónica de Argentina invested in 2009 to develop its broadband access business through ADSL technology, increasing the network coverage and capacity.

Argentina mobile business – Telefónica Móviles Argentina S.A.

Operations

The Argentine mobile market continued to grow at a strong pace in 2009, with an increase in its penetration to approximately 120.3% at December 31, 2009, from approximately 109.8% at December 31, 2008, based on number of mobile accesses.

Telefónica Latin America conducts its Argentine mobile business through Telefónica Móviles Argentina S.A., or Telefónica Móviles Argentina, whose accesses increased 7.4% to 15.9 million accesses at December 31, 2009 from 14.8 million accesses at December 31, 2008. Telefónica Móviles Argentina also increased its number of contract mobile accesses by 1.0% to 5.2 million accesses at December 31, 2009 from 5.1 million accesses at December 31, 2008.

	Year ended December 31,		
	2007	2008	2009
Traffic (millions of minutes)	n.a.	12,941	15,562
ARPU (in euros)	8.5	8.7	8.6

Traffic reached 15,562 million minutes in 2009, an increase of 20.2% compared to 12,941 million minutes in 2008, mainly driven by the growth in on-net traffic.

ARPU was €8.6 in 2009 compared to €8.7 in 2008 (an increase of 10.7% in local currency). The increase in local currency reflected customer adoption of new products and services (upgrades and more consumption), tariff increases and the continued growth in data revenues.

Sales and marketing

In Argentina, Telefónica Móviles Argentina uses a broad range of marketing channels, including television, radio, billboards, telemarketing, direct mail and Internet advertising to market its products. At December 31, 2009, approximately 32.6% of our accesses in Argentina were contract mobile accesses. During 2009, Telefónica Móviles Argentina offered Internet mobile service with plans with limited or unlimited usage.

Competition

We currently have three competitors in the Argentine market for mobile communications services, each of which provides services on a nationwide basis: Telecom Personal, which is controlled by Telecom Italia through Telecom Argentina; Claro, controlled by América Móvil; and Nextel, owned by NII Holdings Inc.

Telefónica Móviles Argentina's estimated market share in the Argentine mobile market in terms of mobile accesses was approximately 33.0% at December 31, 2009, down from approximately 34.0% at December 31, 2008.

Network and technology

In Argentina we operate on digital networks based upon GSM and UMTS technology. At December 31, 2009, GSM accesses represented 98.6% of Telefónica Móviles Argentina's accesses. Also, Telefónica Móviles Argentina developed its mobile broadband business through UMTS technology by increasing coverage.

Chile

The following table presents, at the dates indicated, selected statistical data relating to our operations in Chile.

	At December 31,		
	2007	2008	2009
	(in thousands)		
Fixed telephony accesses	2,172.4	2,121.0	2,028.0
Internet and data accesses	686.8	743.8	807.2
Narrowband accesses	31.8	18.7	15.9
Broadband accesses	646.0	716.6	783.2
Other accesses	8.9	8.6	8.1
Mobile accesses	6,282.7	6,875.0	7,524.7
Pre-pay accesses	4,742.2	4,956.0	5,435.9
Pay TV accesses	219.9	263.0	285.1
Final clients accesses	9,361.7	10,002.7	10,645.0
Wholesale accesses	15.4	11.5	8.9
Total accesses	9,377.2	10,014.3	10,653.8

At December 31, 2009 Telefónica Latin America managed a total of 10.7 million accesses in Chile, 6.4% more than at December 31, 2008, underpinned by growth in mobile accesses, which increased by 9.5% to 7.5 million accesses at December 31, 2009 from 6.9 million accesses at December 31, 2008. Growth was also driven, by a 9.3% increase in broadband accesses to 0.8 million accesses at December 31, 2009 and an 8.4% increase in pay TV accesses to 0.3 million accesses at December 31, 2009. Fixed telephony accesses decreased 4.4% to 2.0 million accesses at December 31, 2009 from 2.1 million accesses at December 31, 2008.

Chilean fixed business – Telefónica Chile S.A.

Operations

Telefónica Latin America conducts its Chilean fixed business through Telefónica Chile S.A., or Telefónica Chile (formerly Compañía de Telecomunicaciones de Chile, or CTC Chile), the leading fixed line telecommunications operator in Chile based on number of accesses, according to information provided by its competitors and regulatory authorities. Telefónica Chile's accesses decreased 0.3% to 3.1 million accesses at December 31, 2009. Telefónica Chile's fixed telephony accesses decreased by 4.4% from December 31, 2008 to 2.0 million accesses at December 31, 2009. Broadband and pay TV accesses continued to grow in 2009, and Telefónica Chile managed 0.8 million broadband accesses at December 31, 2009 compared to 0.7 million at December 31, 2008.

Table of Contents

Telefónica Chile's pay TV business grew to 0.3 million accesses at December 31, 2009. Telefónica Chile established itself as the third pay TV operator in Chile, by number of accesses in 2009.

Sales and marketing

One of our main priorities is to satisfy customer needs by improving the quality of our customer service. We continued our strategy of segmenting our customers in order to tailor our services to best meet the specific needs of each customer segment. With respect to broadband, Telefónica Chile launched bundle services of broadband and voice to satisfy customer demand. Also double and triple play bundles represented one of the drivers of revenue growth.

The customer service model developed by Telefónica Chile, which is aimed at achieving the highest degree of efficiency in customer service, features the following:

- personal customer service lines for purchasing any type of product and service and handling customer queries;
- Telefónica stores (Tiendas Telefónica) where customers can test and buy products marketed by Telefónica;
- Telefónica's "virtual" store, accessible by Internet, which offers customers the ability to order and purchase online the majority of services and products offered by Telefónica; and
- a sophisticated customer service system for corporate clients, ranging from a telephone help line for small and medium-sized businesses to the assignment of sales managers to address the needs of larger corporate clients.

From October 25, 2009, all fixed and/or mobile businesses products and services are marketed under the brand "Movistar", formerly used exclusively by the mobile business.

Competition

The competitive landscape in fixed telephony in Chile is marked by a significant fixed-to-mobile substitution effect. The increased sales of Duo and Trio bundles is the cornerstone of Telefónica Chile's strategic focus, which aims to increase the number of revenue generating units per customer and, accordingly, revenue per customer. VTR is our principal competitor in the Chilean fixed telephony market,

Telefónica Chile's estimated market share at December 31, 2009 was as follows:

- approximately 47.1% of retail broadband accesses, down from approximately 49.4% at December 31, 2008;
- fixed telephony accesses market share amounted to approximately 58.4% of retail fixed telephony accesses, down from approximately 62.1% at December 31, 2008; and
- pay TV market share amounted to approximately 16.6% of the market by number of pay TV accesses, down from 17.5% at December 31, 2008.

Network and technology

Telefónica Chile made improvements on its network to support broadband and TV accesses growth, while updating it, as to be ready for the development of the fiber access network, or FTTX.

Table of Contents

Chilean mobile business – Telefónica Móviles Chile, S.A.

Operations

The mobile penetration rate in Chile stood at an estimated 105.6% at December 31, 2009, an increase of approximately 9.0 percentage points from December 31, 2008.

Telefónica Latin America conducts its Chilean mobile business through Telefónica Móviles Chile, S.A., or Telefónica Móviles Chile, whose customer base increased 9.5% to 7.5 million accesses at December 31, 2009. The number of contract mobile accesses rose by 8.8% to 2.1 million mobile contract accesses at December 31, 2009 from 1.9 million contract mobile accesses at December 31, 2008.

	Year ended December 31,		
	2007	2008	2009
Traffic (millions of minutes)	n.a.	9,703	10,521
ARPU (in euros)	12.0	12.3	10.7

Traffic in 2009 increased 8.4% to 10,521 million minutes at December 31, 2009 from 9,703 million minutes at December 31, 2008, mainly driven by outgoing traffic, primarily on-net.

ARPU was €10.7 in 2009 compared to €12.3 in 2008 (a decrease of 10.7% in local currency). The decrease in local currency was largely due to the reduction of tariffs as a consequence of a regulatory decree mandating lower interconnection rates, which went into effect at January 23, 2009 for mobile termination and resulted in an average tariff decrease of approximately 44.6%.

Sales and marketing

Telefónica Móviles Chile offered promotional campaigns associated with recharges for pre-pay mobile users while developing mobile broadband service.

Competition

We currently have three primary competitors in the Chilean market for mobile telephony, each of which provides services on a nationwide basis: Entel, Claro and Nextel.

Telefónica Móviles Chile's estimated market share in the Chilean mobile sector in terms of mobile accesses was approximately 42.8% at December 31, 2009, down from approximately 43.3% at December 31, 2008.

Network and technology

In Chile, Telefónica Móviles Chile operates with GSM and 3G network, launched in December 2007.

Mexico

Mexico mobile business – Telefónica Móviles México, S.A. de C.V.

Operations

The following table presents, at the dates indicated, selected statistical data relating to our operations in Mexico.

	At December 31,		
	2007	2008	2009
		(in thousands)	
Total mobile accesses	12,534.1	15,330.6	17,400.5
Pre-pay accesses	11,833.7	14,432.4	16,328.3
Fixed wireless accesses	3.6	133.6	334.3
Total accesses	12,537.6	15,464.2	17,734.8

The mobile penetration rate in Mexico was approximately 75.2% at December 31, 2009, an increase of approximately 3.6 percentage points from December 31, 2008.

Telefónica Latin America conducts its Mexican mobile business through Telefónica Móviles México, S.A. de C.V., or Telefónica Móviles México. Telefónica Móviles Mexico's customer base increased 14.7% to 17.7 million accesses at December 31, 2009 from 15.5 million accesses at December 31, 2008. This increase was mainly the result of a 13.1% increase of pre-pay mobile accesses in 2009 compared to 2008. At December 31, 2009, approximately 93.8% of our mobile customers in Mexico were pre-pay mobile accesses while 6.2% were contract mobile accesses.

	Year ended December 31,		
	2007	2008	2009
Traffic (millions of minutes)	n.a.	22,431	23,186
ARPU (in euros)	9.3	8.2	6.9

Traffic for 2009 increased 3.4% to 23,186 million minutes compared to 22,431 million minutes in 2008. This increase was mainly due to commercial promotions focusing on fee-per call (tariff per call rather than per minutes used) that improved usage.

ARPU declined to €6.9 in 2009 compared to €8.2 in 2008 (a decrease of 3.3% in local currency). The decrease in local currency was largely due to the fact that the increase of the customer base was motivated by lower tariff plans, which had the effect of reducing the average consumption.

Sales and marketing

During 2009, Telefónica Móviles México launched innovative products to maintain current customers and attract additional ones. In addition, Telefónica Móviles México focused on commercial activity and profitability while improving the quality of its network, which enabled the company to maintain robust customer growth during that year.

In Mexico, we use a broad range of marketing channels, including television, radio, billboards, telemarketing, direct mail and Internet advertising to market our products and services.

Telefónica Móviles México's offer was completed with "Plan paga menos Xtra" in the pre-pay segment, based on a price-per-call offer. This plan has lower prices but generates consumption.

Competition

Telefónica Móviles México is the second largest mobile operator in Mexico based on the number of mobile accesses, and competes with various mobile operators at the national level. Telefónica Móviles México's principal competitor is Telcel, a subsidiary of América Móvil. Other significant competitors are Nextel and Iusacell.

Telefónica Móviles México's estimated market share in the Mexican mobile market in terms of mobile accesses was approximately 20.8% at December 31, 2009, up from approximately 19.5% at December 31, 2008.

Network and technology

Telefónica Móviles México has 100% of its accesses on its GSM network. Also, Telefónica Móviles México provides UMTS services but spectrum constraints their expansion.

Peru

The following table presents, at the dates indicated, selected statistical data relating to our operations in Peru.

	At December 31,		
	2007	2008	2009
	(in thousands)		
Fixed telephony accesses	2,843.4	2,986.5	2,971.2
Fixed wireless accesses	290.0	485.5	582.7
Internet and data accesses	623.1	728.9	800.6
Narrowband accesses	40.3	17.7	16.9
Broadband accesses	572.1	698.4	768.0
Other accesses	10.7	12.8	15.6
Mobile accesses	8,067.3	10,612.7	11,458.2
Pre-pay accesses	7,238.1	9,575.2	10,214.2
Pay TV accesses	640.0	654.5	686.3
Final clients accesses	12,173.8	14,982.6	15,916.3
Wholesale accesses	0.5	0.4	0.5
Total accesses	12,174.3	14,983,0	15,916.8

At December 31, 2009, Telefónica Latin America had 15.9 million accesses in Peru, which represents an increase of 6.2% from December 31, 2008. This growth in accesses was primarily driven by an 8.0% increase in mobile accesses from December 31, 2008 to 11.5 million mobile accesses at December 31, 2009, mostly in the pre-pay mobile segment. The IRIS project, a collaboration between fixed telephony operators and mobile operators in Peru, which was launched in March 2007 with the aim of increasing fixed telephony and broadband penetration, also contributed to the overall growth in accesses.

Peruvian fixed business – Telefónica del Perú, S.A.A.

Operations

Telefónica Latin America conducts its Peruvian fixed telephony business through Telefónica del Perú, S.A.A., or Telefónica del Perú, which at December 31, 2009 was the leading fixed line telecommunications operator in Peru based on number of fixed telephony accesses.

Telefónica del Perú had total accesses of 4.5 million at December 31, 2009, an increase of 2.0% from December 31, 2008, due primarily to increases in fixed wireless telephony and broadband accesses. Fixed telephony accesses decreased 0.5% from December 31, 2008 to 3.0 million accesses at December 31, 2009. Broadband accesses grew by 10.0% from December 31, 2008 to 0.8 million at December 31, 2009. In addition, pay TV accesses totaled 0.7 million accesses at December 31, 2009 recording growth of 4.9% from December 31, 2008 primarily due to increased cable pay TV subscriptions.

Table of Contents

Sales and marketing

Telefónica del Perú's commercial strategy is based on achieving and maintaining high levels of market penetration by offering customized services to different customer segments, with marketing campaigns focused on maintaining customer loyalty and increasing the options available to potential customers. The primary products offered by Telefónica del Perú include fixed telephony, broadband, pay TV, data and IT services.

Telefónica del Perú focuses its commercial strategy on penetration by targeting specific market segments, commercializing Duos and Trios and leveraging on its customer retention campaign.

Competition

In 2009, Telmex and Americatel, Telefónica del Perú's two primary competitors, focused on offering bundled products (local and long distance telephony together with broadband).

Telmex implemented an aggressive strategy to enter the residential market by offering a "triple play" service. The response from Telefónica del Perú consisted of increasing Trio bundle options at lower prices.

Telefónica del Perú had an estimated market share in the Peruvian fixed telephony market of approximately 93.8% at December 31, 2009, based on number of fixed telephony accesses, down from approximately 94.0% at December 31, 2008.

Network and technology

Telefónica del Peru invested to develop its broadband business through ADSL technology by increasing coverage and speed. Additionally, it began deploying a new fiber access network, called FTTX, which currently is offered on a limited basis to large customers.

Peruvian mobile business – Telefónica Móviles Perú, S.A.C.

Operations

The estimated Peruvian mobile penetration rate reached approximately 64.5% at December 31, 2009, an increase of approximately 3.9 percentage points compared to December 31, 2008.

Telefónica Latin America conducts its Peruvian mobile business through Telefónica Móviles Perú, S.A.C., or Telefónica Móviles Perú, whose customer base increased 8.0% from December 31, 2008 to 11.5 million accesses at December 31, 2009. This increase was primarily driven by a 6.7 % increase in the number of pre-pay mobile accesses from December 31, 2008 to December 31, 2009.

	Year ended December 31,		
	2007	2008	2009
Traffic (millions of minutes)	n.a.	10,039	11,460
ARPU (in euros)	7.3	6.0	5.5

Traffic carried in 2009 increased 14.1% to 11,460 million minutes compared to 10,039 million minutes in 2008, primarily due to increases in on-net traffic, in line with the strategy of offering better tariffs to this type of traffic as a benefit of belonging to the largest mobile network of the country.

ARPU was €5.5 in 2009 compared to €6.0 in 2008 (a decrease of 11.5% in local currency). The decrease in local currency was largely a consequence of reductions in both contract and pre-pay tariffs.

Telefónica Móviles Perú uses a broad range of marketing channels, including television, radio, billboards, telemarketing, direct mail and Internet advertising to market its products. At December 31, 2009, approximately 89.1% of Telefónica Móviles Perú's mobile accesses were pre-pay mobile accesses, while approximately 10.9% were contract mobile accesses.

Sales and marketing

Telefónica Móviles Perú focused its marketing efforts on encouraging migrations from pre-pay to contract services. In May 2009, it started to market mobile broadband and in September 2009 launched the promotion “push to talk”, which allows instant communications from a mobile device. Since November 2009, we changed our marketing focus for the pre-pay segment to better target each of the pre-pay clusters (defined by recharge frequency and money spent) in order to avoid revenue cannibalization.

Competition

Telefónica Móviles Perú currently has two primary competitors in the Peruvian market for mobile telephony services: Claro, owned by América Móvil, and Nextel Perú.

Telefónica’s estimated market share in the Peruvian mobile market in terms of mobile accesses was approximately 62.9% at December 31, 2009, up from approximately 62.6% at December 31, 2008.

Network and technology

At December 31, 2009, Telefónica Móviles Perú operated both GSM and CDMA technology. Its digital network is based upon the CDMA/CDMA 1XRTT standard. Telefónica Móviles Perú continued the migration to GSM technology, and at December 31, 2009, GSM accesses accounted for 93.4 % of its total customer base, which represents an increase of 3.8 percentage points from December 31, 2008.

Colombia

The following table presents, at the dates indicated, selected statistical data related to our operations in Colombia.

	At December 31,		
	2007	2008	2009
		(in thousands)	
Fixed telephony accesses	2,328.5	2,299.2	1,639.8
Internet and data accesses	200.3	395.9	428.4
Narrowband accesses	0.0	0.3	5.9
Broadband accesses	200.3	393.9	420.3
Other accesses		1.7	2.2
Mobile accesses	8,372.1	9,963.1	8,964.6
Pre-pay accesses	6,612.9	8,327.3	7,203.2
Pay TV accesses	72.9	142.3	127.2
Final clients accesses	10,973.8	12,800.5	11,159.9
Wholesale accesses		2.9	3.3
Total accesses	10,973.8	12,803.4	11,163.2

Telefónica Latin America managed a total of 11.2 million accesses in Colombia at December 31, 2009, a decrease of 12.8% from December 31, 2008. This decrease was due to the drop in mobile accesses, which decreased 10.0% to 9.0 million accesses at December 31, 2009 from 10.0 million accesses at December 31, 2008, and by the 28.7% decrease in fixed telephony accesses from December 31, 2009 to December 31, 2008. These decreases were not offset by the 6.7% increase of broadband accesses to reach 0.4 million accesses at December 31, 2009 from 0.4 million accesses at

December 31, 2008.

Colombian fixed business - Colombia Telecomunicaciones, S.A. ESP

Operations

Telefónica Latin America conducts its Colombian fixed telephony business through Colombia Telecomunicaciones, S.A. ESP, or Colombia Telecom, which is present in approximately 1,000 municipalities in Colombia.

Table of Contents

Colombia Telecom had 2.2 million accesses at December 31, 2009, which represents a decrease of 22.6% from 2.8 million accesses at December 31, 2008, primarily due to the decrease of 28.7% in fixed telephony accesses from December 31, 2008 to 1.6 million accesses at December 31, 2009, as a consequence of intense competition and our decision to inactive certain dormant accounts from our customer base. Broadband accesses increased 6.7% to 0.4 million accesses at December 31, 2009 from December 31, 2008.

Colombia Telecom also launched a pay TV product using satellite technology at the beginning of 2007, allowing it to begin offering Trio bundles (voice, broadband and pay TV). As of December 31, 2009, Colombia Telecom had 0.1 million pay TV accesses, a 10.6% decrease compared to December 31, 2008.

Colombia Telecom has a finance lease agreement with PARAPAT. PARAPAT is the consortium which owns the telecommunications assets and manages the pension funds for the entities which were predecessors to Colombia Telecom and regulates the operation of assets, goods and rights relating to the provision of telecommunications services by Colombia Telecom. This finance lease agreement includes the lease of the telecommunications assets and the transfer of these assets to Colombia Telecom once the last installment of the lease has been paid which, in accordance with the payment schedule, is expected to be in 2022.

Sales and marketing

In Colombia, Colombia Telecom uses a broad range of marketing channels, including television, radio, billboards, telemarketing, direct mail and Internet advertising to market its products. Additionally, Colombia Telecom is currently pursuing a strategy to increase market penetration, by restructuring distribution and communication channels, and by offering bundled products such as “Trio Telefónica”. Also, it restructured the commercial offer to strengthen the quality and quantity of television channels and improving broadband capability.

Competition

Colombia Telecom’s principal competitors in the Colombian market are Telmex and ETB. Colombia Telecom had an estimated market share in the Colombian fixed telephony market of approximately 22.4% at December 31, 2009 based on number of fixed telephony accesses, down from approximately 29.2% at December 31, 2008. This decrease was mainly driven by a loss of customers as a result of intense competition and our decision to inactivate certain dormant accounts from our customer base.

Network and technology

Colombia Telecom continued expanding and upgrading the network to support a broader range of product and services in 2009.

Colombian mobile business – Telefónica Móviles Colombia, S.A.

Operations

At December 31, 2009 the Colombian mobile market had an estimated penetration rate of approximately 92.9%, an increase of 1.8 percentage points from December 31, 2008.

Telefónica Latin America conducts its Colombian mobile business through Telefónica Móviles Colombia, S.A., or Telefónica Móviles Colombia, whose customer base decreased by 10.0% from 10.0 million accesses at December 31, 2008 to 9.0 million accesses at December 31, 2009. At December 31, 2009, approximately 19.6% of our mobile accesses in Colombia were contract mobile accesses, compared to 16.4% at December 31, 2008.

	Year ended December 31,		
	2007	2008	2009
Traffic (millions of minutes)	n.a.	13,568	13,665
ARPU (in euros)	8.8	6.8	5.9

Traffic for 2009 increased 0.7% to 13,665 million minutes compared to 2008.

Table of Contents

ARPU was €5.9 in 2009 compared to €6.8 in 2008 (a decrease of 10.2% in local currency). The decrease in local currency was largely due to a reduction in interconnection tariffs and competitive pressure on tariffs.

Sales and marketing

Telefónica Móviles Colombia uses a broad range of marketing channels, including television, radio, billboards, telemarketing, direct mail and Internet advertising to market its products.

In 2009, Telefónica Móviles Colombia implemented, in the contract segment, commercial promotions to increase customer loyalty, and launched new tariff plans focused on a single tariff to any destination with lower basic charges and other tariff plans with preferential on net prices to attract customers. Additionally, it launched the project "Tecnoferias" (specific sales in strategic areas of major cities) to improve commercial activity and to re-position the "Movistar" brand.

Competition

Telefónica Móviles Colombia currently has two primary competitors in the Colombian market for mobile communications services: Comcel, which is owned by América Móvil, and Colombia Móvil, who operates under the brand "Tigo" and is owned by Millicom.

Telefónica Móviles Colombia's estimated market share in the Colombian mobile market in terms of mobile accesses was approximately 21.3% at December 31, 2009, down from approximately 24.5% at December 31, 2008.

Network and technology

TDMA was switched off during 2008 and our CDMA network was working in 2009. The UMTS network experienced an increase in terms of coverage by installing 504 new GSM sites, accounting for a total of 2,573 sites installed and representing a coverage of 83% of the Colombian municipalities.

Central America

Telefónica Central America includes Panama, Guatemala, El Salvador and Nicaragua. At the end of 2009, the mobile penetration rate of the Central American market, where we operate, was approximately 89.7%, which represents an increase of approximately 9.3 percentage points from December 31, 2008.

The following table presents, at the dates indicated, selected statistical data related to our operations in Central America.

	At December 31,		
	2007	2008	2009
	(in thousands)		
Fixed telephony accesses	393.4	437.2	444.5
Internet and data accesses	22.0	18.4	14.7
Broadband accesses	19.8	16.5	12.6
Pay TV accesses	—	—	
Mobile accesses	5,009.9	5,702.0	5,806.5
Total accesses	5,425.3	6,157.6	6,265.8

Table of Contents

Telefónica Central América's customer base increased by 1.8% from December 31, 2008 to 6.3 million accesses at December 31, 2009, mainly due to an increase in mobile accesses in 2009 compared to 2008.

	Year ended December 31,		
	2007	2008	2009
Traffic (millions of minutes)	n.a.	7,174	6,868
ARPU (in euros)	9.7	7.4	6.9

Traffic decreased by 4.3% compared to 2008 to 6,868 million minutes in 2009. This decrease was due primarily to lower voice usage as customers optimized their consumption.

ARPU was €6.9 in 2009 compared to €7.4 in 2008 (a decrease of 8.7% on a constant euro basis). The decrease on a constant euro basis was largely due to lower consumption.

Ecuador

Ecuadorian mobile business – Otecel, S.A.

Operations

The Ecuadorian mobile penetration rate reached approximately 92.8% at December 31, 2009, an increase of approximately 12.2 percentage points from December 31, 2008.

The following table presents, at the dates indicated, selected statistical data relating to our operations in Ecuador.

	At December 31,		
	2007	2008	2009
	(in thousands)		
Total mobile accesses	2,581.1	3,122.5	3,721.8
Pre-pay accesses	2,177.5	2,650.5	3,193.9
Fixed wireless accesses	1.3	89.4	84.7
Total accesses	2,582.4	3,211.9	3,806.4

Telefónica Latin America conducts its Ecuadorian mobile business through Otecel, S.A., or Otecel, which had a customer base of 3.8 million accesses at December 31, 2009, an increase of 18.5% from 3.2 million accesses at December 31, 2008. At December 31, 2009, approximately 85.8% of our mobile accesses in Ecuador were pre-pay mobile accesses, while approximately 14.2% were contract mobile accesses.

	Year ended December 31,		
	2007	2008	2009
Traffic (millions of minutes)	n.a.	2,800	3,744
ARPU (in euros)	6.6	6.7	6.8

Traffic carried in 2009 increased by 33.7% to 3,744 million minutes compared to 2008 mainly due to the increase in the number of both pre-pay and contract accesses.

ARPU was €6.8 in 2009 compared to €6.7 in 2008 (a decrease of 3.8% in local currency). The decrease in local currency was largely due to lower consumption.

Sales and marketing

In Ecuador, Otecel uses a broad range of marketing channels, including television, radio, billboards, telemarketing, direct mail and Internet advertising to market their products. In April 2009, Otecel launched “Total Plan” for on-net calls for the contract segment. In the pre-pay segment, Otecel continued with doubled and tripled recharges, along with the campaign “Multicolor” for off-net calls. The marketing of mobile broadband and the service “push to talk” (Movitalk) were launched in June 2009 and September 2009 respectively.

Competition

Otecel currently has two primary competitors in market for mobile communications services in Ecuador, Porta (América Móvil) and Alegro.

Telefónica’s estimated market share in the Ecuadorian mobile market in terms of mobile accesses was approximately 28.4% at December 31, 2009, up from approximately 26.6% at December 31, 2008.

Network and technology

Otecel operates both analog and digital networks. Its digital network is based upon the GSM standard and CDMA standard. GSM accesses reached 91.8% of the total customer base, representing an increase of 8.7 percentage points from December 31, 2008.

Atento—Call Center Business

Atento offers integrated telephone assistance services as well as sophisticated customer relationship management services, such as the development and implementation of customer loyalty programs, telemarketing services and market research. In addition, Atento rents call centers and provides staff for such centers to third parties. Atento has sought to diversify its client base and serves companies in the financial, consumer and energy sectors, as well as public institutions. At December 31, 2009, Atento operated more than 100 call centers and had 132,256 call center personnel in 15 countries on three continents, including Europe (Spain and Czech Republic), America (Latin America) and Africa (Morocco).

Strategic Partnerships

China Unicom

Since 2005, we have had a stake in China Unicom and its predecessor company. On September 6, 2009 we entered into a strategic alliance agreement with China Unicom, which provides for, among other areas for cooperation, joint procurement of infrastructure and client equipment, common development of mobile service platforms, joint provisions of service to multinational customers, roaming, research and development, sharing of best practices and technical, operational and management know-how, joint development of strategic initiatives in the area of network evolution, joint participation in international alliances and exchanges of senior management. In furtherance of this strategic alliance we entered into a subscription agreement with China Unicom, pursuant to which we increased our voting interest in the share capital of China Unicom to 8.06% and China Unicom obtained 0.87% voting interest in our share capital in October 2009.

Pursuant to the strategic alliance agreement mentioned above, China Unicom has agreed to use its best endeavors to maintain a listing of all the issued ordinary shares of China Unicom on the Hong Kong Stock Exchange. For so long as the strategic alliance agreement with us is in effect, China Unicom shall not (i) offer, issue or sell any significant number of its ordinary shares (including treasury shares), or any securities convertible into or other rights to subscribe for or purchase a significant number of China Unicom’s ordinary shares (including treasury shares), to any current major competitor of Telefónica or (ii) make any significant investment, directly or indirectly, in any current major competitor of Telefónica. We have made similar undertakings.

The strategic alliance agreement between us and China Unicom terminates on September 6, 2012 subject to automatic annual renewal, subject to either party's right to terminate on six months' notice. Also, the strategic alliance agreement may be terminated by China Unicom if our shareholding in China Unicom drops below 5% of its issued share capital or if China Unicom's shareholding in us drops below 0.5% of our issued share capital. In addition, the strategic alliance agreement is subject to termination in the event either party is in default and automatically terminates on a change in control of China Unicom.

Table of Contents

As of the date of this Annual Report, and after the capital reduction carried out by China Unicom, we hold shares representing 8.37% of China Unicom's voting share capital and the right to appoint a member to its board of directors.

Portugal Telecom

At December 31, 2007, we held an 8.32% effective interest in Portugal Telecom (or 9.16% if shares held by Portugal Telecom in treasury are not counted as outstanding), our joint venture partner in Brazil.

In December 2008, Portugal Telecom bought back and cancelled 46,082,677 shares in line with its share buyback program. This raised our direct and indirect ownership interest to 10.48%. In accordance with Portuguese securities regulation, which require us to dispose of any shares which bring our ownership stake over 10%, we sold 4,264,394 shares of Portugal Telecom, thereby lowering our stake to 10%. Our effective shareholding in Portugal Telecom at December 31, 2009 was 9.86%.

Within the framework of our business cooperation with Portugal Telecom, we provide mobile services in Brazil (through Brasilcel, in which we hold a 50% interest and share management responsibilities with Portugal Telecom, under the brand name "Vivo").

For more information on these joint ventures, please see "—Telefónica Latin America—Brazil—Brazil mobile business" abov

In addition, Telefónica Spain provided mobile services in Morocco through Medi Telecom, a Moroccan company in which Telefónica Móviles España held a 32.18% interest and shared management responsibilities with Portugal Telecom. On August 31, 2009, we agreed to sell our 32.18% stake in Medi Telecom, together with its outstanding shareholder loans, to our local partners for total cash consideration of €400 million. This transaction closed on December 31, 2009.

Telecom Italia

Through a series of transactions from 2007 through 2009, we acquired an indirect holding of 10.49% in the voting shares of Telecom Italia (7.21% of the dividend rights) through our holdings in Telco. The Telecom Italia group is principally engaged in the communications sector and, particularly, in telephone and data services on fixed lines for final and wholesale customers, in the development of fiber optic networks for wholesale customers in the provision of broadband services and Internet services, in domestic and international mobile telecommunications (especially in Brazil), in the television sector using both analog and digital terrestrial technology and in the office products sector. Telecom Italia operates primarily in Europe, the Mediterranean basin and in South America.

For more information, please see "Item 4. Information on the Company —History and Development of the Company—Recent Developments", "Item 5. Operating and Financial Review and Prospects —Operating Results—Significant Factors Affecting the Comparability of our Results of Operations in the Period Under Review" and "Item 10. Additional Information—Material Contracts". Telco, through which we hold our stake in Telecom Italia, is included in our consolidated financial statements using the equity method.

Regulation

As a telecommunications operator, we are subject to sector-specific telecommunications regulations, general competition law and a variety of other regulations. The extent to which telecommunications regulations apply to us depends largely on the nature of our activities in a particular country, with traditional fixed telephony services usually subject to more extensive regulations, which can have a direct and material effect on our business areas, particularly in countries that favor regulatory intervention.

To operate our networks, we must obtain general authorizations, concessions or licenses from national regulatory authorities, or NRAs, in those countries in which we operate. Licensing procedures also apply to our mobile operations with respect to radio frequencies. The duration of any particular license or spectrum right depends on the legal framework in the relevant country.

Table of Contents

Electronic Communication Regulation in the EU

The EU legal framework for electronic communications services has been developed with the aim of reinforcing the liberalization of the market and improving the functioning of the EU internal market for telecommunications networks and services, which culminated in the adoption of the 2002 EU regulatory framework for electronic communications sector (the "EU Framework"). Such regulatory framework has been subsequently modified in order to take into account technological changes through the adoption of certain new rules by the European Parliament and the Council during the end of 2009. On December 18, 2009 Regulation 1211/2009/EC was published, establishing the framework for the creation of a European regulatory body for the telecommunications industry. The Directive of Better Regulation (Directive 2009/136/EC), which was also published on the same date, modifies the following directives: (i) Directive 2002/21/EC of 7 March 2002 on a common regulatory framework for electronic communications networks and service ("Framework Directive"); (ii) Directive 2002/20/EC of the European Parliament and of the Council of 7 March 2002 on the authorization of electronic communications networks and services ("Authorization Directive"); (iii) Directive 2002/19/EC of the European Parliament and of the Council of 7 March 2002 on access to, and interconnection of, electronic communications networks and associated facilities ("Access Directive").

The passage and subsequent publication on December 18, 2009 of Directive 2009/140/EC, on citizens' rights ("Citizens' Rights Directive") modifies Directive 2002/22/EC of the European Parliament and of the Council of 7 March 2002 on universal service and users' rights relating to electronic communications networks and services ("Universal Service Directive") and the e-Privacy Directive (2002/58/EC) (the "e-Privacy Directive") complements and supplements the more general provisions of the Data Protection Directive in the area of electronic communications. It provides for basic obligations to ensure the security and confidentiality of communications over EU electronic communications networks and gives consumers a set of tools to protect their privacy and personal data. These Directives set forth the main principles and procedures that NRAs should follow with respect to regulation for the provision of electronic communications services. The EU Framework establishes an authorization regime containing measures to ensure the universal provision of basic services to consumers and sets out the terms on which providers may access each other's networks and services.

In 2006, the European Union established a new regulation regarding retention of electronic communications data in order to ensure that electronic communication data are available for the purpose of the investigation, detection and prosecution of serious crimes. These data retention rules set minimum standards for the type of data to be retained and the retention period. The initial impact of this new regulation is estimated to be significant, although it will depend on the requirements established at the national level and the extent to which operators will be compensated for the costs associated with its implementation. Some European countries, such as Spain and Germany, have already adopted the new regulation at the national level. In Spain, operators shall retain data from their pre-pay customers and extend the data retention period. In Germany the implementation of such regulations has been legally challenged for constitutional reasons and until a decision is made, it will not be applicable. For further information regarding the matters discussed above and other aspects of the regulatory risks derived from the new regulation, see "Item 3. Key Information—Risk Factors—Risks related to our business".

Notably, the EU Framework also harmonizes the rules for deciding when regulation may be imposed on electronic communications providers. In particular, it provides that electronic communications providers can generally only be subject to specific regulation in markets in which they have "significant market power", or SMP. The concept of SMP, for these purposes, has been aligned to the competition law concept of dominance, which essentially means a market position which allows a company to act independently of customers, suppliers and competitors.

Accordingly, the European Commission has identified in a Recommendation a list of relevant markets whose conditions may justify the application of ex ante specific regulation. The Recommendation was published on February 2003 and it has been modified by another Recommendation published in December 2007, which reduces the relevant markets from 18 to seven. In order to determine whether a company has SMP in any of the markets identified in the Recommendations, NRAs must conduct a market analysis for the relevant market. When an NRA determines a company has SMP in a relevant market, that NRA must impose at least one obligation relating to price control, transparency, non-discrimination, accounting separation or access obligations.

Table of Contents

Regulation with respect to voice roaming tariffs in the EU entered into force on June 30, 2007. The regulation introduces a maximum level for the charges that operators may levy at wholesale level as well as maximum retail ceilings (referred to “Eurotariff”) for making and receiving calls while roaming in the EU. In 2009 Regulation 544/2009 was also adopted, which extended tariff regulation through 2012 and also extended the scope of the previous roaming regulation to cover SMS and data services. The wholesale tariff price cap has been set at €0.26 per minute (excluding VAT) from July 2009 and will continue to decrease to €0.22 and €0.18 from July 2010 and from July 2011, respectively. The retail tariff price cap (excluding VAT) has been set at €0.43 per minute for making a call and €0.19 per minute for receiving a call from July 2009, and these prices will continue to decrease for making a call to €0.39 and €0.35, and for receiving a call to €0.15 and €0.11 from July 2010 and from July 2011, respectively. In addition, the new regulation mentioned above limits the price for sending a text message for wholesale and for customers roaming within the EU at €0.04 and at €0.11, respectively. Moreover, the regulation subjects the cost of data transfers to a maximum wholesale cap of €1.00 per megabyte downloaded from August 2009. This cap will be reduced to €0.80 from July 2010 and to €0.50 from July 2011. Receiving an SMS in another EU country will remain free of charge. The new rules will also require that operators protect consumers from “bill shocks” by introducing a cut-off mechanism once a customer’s bill reaches €50 (unless a customer chose another cut-off limit). This cut-off mechanism, along with per second billing after the first 30 seconds for calls made and immediately for calls received must be implemented by March 31, 2010.

In addition, the European Parliament and the Council approved Directive 372/87/EC amending Council Directive 87/372/EEC on the frequency band 900 MHz in order to allow the use of such band by systems capable of providing electronic communication services not limited to GSM. Finally, the Commission also adopted a Recommendation on termination rates for mobile and fixed networks.

EU Competition Law

The EU’s competition rules have the force of law in EU Member States and are, therefore, applicable to our operations in EU Member States.

The EC Treaty prohibits “concerted practices” and all agreements for undertakings that may affect trade between Member States and which restrict, or are intended to restrict, competition within the EU. It also prohibits any abuse of a dominant competitive position within the common market of the EU, or any substantial part of it, that may affect trade between Member States.

The EU Merger Regulation requires that all mergers, acquisitions and joint ventures involving participants meeting certain turnover thresholds be submitted to the EU Commission for review, rather than to the national competition authorities. Under the amended EU Merger Regulation, market concentrations will be prohibited if they significantly impede effective competition in the EU common market. European Commission and the EU Competition Commissioner are granted the authority to apply the European Competition framework.

Similar competition rules are set forth in each EU Member State’s legislation and are enforced by each of their national competition authorities, or NCAs. All European countries where we have activities and referred to below are Member States of the EU.

Table of Contents

Telefónica Spain

Spain

General regulatory framework

The legal framework for the regulation of the telecommunications sector in Spain is principally governed by the General Telecommunications Law (32/2003) and several Royal Decrees. The General Telecommunications Law, among other things, sets forth rules regarding the new system of notification for electronic communications services, establishes the terms by which operators interconnect their networks, defines the universal service provision regime and subjects providers with SMP in particular telecommunications markets to specific obligations.

Regulatory supervision

The Telecommunications Market Commission, or the CMT, is the NRA responsible for regulating the telecommunications and audiovisual service markets in Spain. The CMT supervises the specific obligations imposed on operators in the telecommunications market, and it has the requisite power to enforce its decisions whenever necessary.

The Framework Directive requires that NRAs have the power to issue binding decisions to resolve disputes arising in connection with obligations imposed under the regulatory framework.

The Spanish regulatory framework explicitly acknowledges the right for third parties who are affected by a Spanish NRA decision to challenge this decision before the appeal body.

Licenses and concessions

Pursuant to the EU Framework, parties intending to operate a telecommunications network or engage in the provision of electronic communication services must notify the CMT prior to commencing such activity. The CMT will register the telecommunications operator in the Public Operator Registry. Every three years, operators must notify the CMT of their intention to continue offering electronic communications services or operating telecommunications networks.

Concessions to use spectrum are awarded on a non-discriminatory basis by way of a competitive procedure. Telefónica Móviles España is entitled to provide mobile services on several spectrum bands. Our main concessions are:

Technology	Duration	Ending Date	Extension Period
GSM 900	5 years	February 3, 2015	--
E-GSM 900	15 years	June 6, 2020	5 years
DCS-1800	25 years	July 24, 2023	5 years
UMTS	20 years	April 18, 2020	10 years

Telefónica Móviles España has obtained the extension of the GSM 900 right of use until February 3, 2015.

Market analysis

In accordance with the EU Framework, the CMT should identify those markets which lack effective competition, in which case it would impose specific obligations upon operators with SMP. During 2008, the CMT conducted a second round of market analyses to determine which operators have SMP in which markets, the results of which are described below.

Table of Contents
\
Fixed markets

Retail access to the public telephone network at a fixed location market; Retail market for calls at a fixed location and Retail lease lines market

In March 2006, and following a market analysis, the CMT concluded that Telefónica de España is an operator with SMP in the provision of retail access to the public telephone network service at a fixed location market. As an SMP operator, Telefónica de España has certain specific obligations and is subject to certain restrictions, the most relevant of which are maximum price caps for installation and monthly fees. Telefónica de España also has obligations regarding carrier selection, cost accounting and accounting separation.

With respect to the retail market for calls at a fixed location market, on December 12, 2008, the CMT has determined that this market is competitive and, thus, it has resolved to withdraw all obligations imposed on Telefónica de España with respect to such market.

In 2006, the CMT identified Telefónica de España as an operator with SMP in the retail lease lines market, and imposed, among other obligations, the duty to provide access to a minimum set of lease lines under price controls.

Wholesale fixed call origination market

On March 22, 2007, the CMT adopted new regulations concerning call origination on the wholesale fixed call origination market, introducing additional obligations for Telefónica de España to provide wholesale access to its fixed network to other operators, allowing competitors to use its networks to provide access services and other associated services to their customers.

In December 2008, the CMT concluded that Telefónica de España is an operator with SMP in this market and it has requested that Telefónica de España offer wholesale service to assist other operators in offering IP telephony services and provide transparent information of migration to Next Generation Networks, or NGN, centrals, which implies the provision of broad information to competitors about network evolution.

Fixed call termination market on individual networks

As an operator with SMP in fixed call termination market on individual networks, Telefónica de España is required to submit an “Interconnection Reference Offer (OIR)” outlining the terms and conditions under which it will interconnect with other operators.

In December 2008, the CMT concluded that Telefónica de España is an operator with SMP in this market. The CMT maintained its obligations for Telefónica de España to submit an Interconnection Reference Offer (OIR). The CMT also added the obligation that Telefónica de España provide transparent information with respect to migration to NGN centrals, which implies the provision of broad information to competitors about network evolution.

Mobile market

Mobile voice call termination

In September 2006, the CMT established a progressive reduction schedule for mobile termination rates (the “glide path”) from October 2006 to September 2009. In July 2009, the CMT established a new glide path for mobile voice call termination rates with an objective price of €0.04 per minute by April 2012, through which the mobile voice call termination rates of the four Spanish mobile operators will converge by 2012.

In December 2008, Telefónica Móviles España was again identified by the CMT as an operator with SMP in mobile voice call termination on individual mobile networks, and therefore continues to be subject to the obligations already imposed on it by the CMT and as well as the additional obligation to charge for seconds of usage according to a single termination price established by the CMT.

Table of Contents

Mobile voice call origination

MVNOs are mobile operators that are not entitled to use spectrum for the provision of mobile services. Consequently, they must reach an access agreement with a mobile network operator in order to provide mobile access to their customers.

On February 2, 2006, the CMT established that mobile network operators collectively hold a dominant position in the mobile access and voice call origination market. Mobile operators are, therefore, obliged to negotiate reasonable access to their network upon request from an MVNO, charging reasonable prices for access services provided. MVNOs and mobile operators negotiate an access agreement on a commercial basis. If parties are unable to reach an agreement independently, the CMT may intervene to resolve the dispute.

Wholesale (physical) network infrastructures access

In January 2009, the CMT concluded that Telefónica de España is an operator with SMP in the wholesale (physical) network infrastructures access market, and imposed the following obligations on Telefónica de España: access to full and shared unbundled access to copper loops, sub-loops and ducts, cost oriented tariffs and accounting separation, transparency and non-discrimination obligations including an “Unbundling Reference Offer” and a “Ducts Reference Offer”. In February 2008, the CMT imposed similar obligations with respect to vertical access to buildings.

Wholesale broadband access

In January 2009, the CMT identified Telefónica de España as an operator with SMP in the wholesale broadband access market, and consequently the CMT has imposed on Telefónica de España the obligation to provide wholesale broadband access service until 30 Mbps to other operators in copper and fiber infrastructure .. The CMT also obliges Telefónica de España to publish a wholesale broadband access reference offer, provide cost-oriented tariffs and accounting separation, non-discrimination in network access and to communicate broadband retail changes in services prior to offering them in the market.

Universal service obligations

The General Telecommunications Law outlines provisions to ensure that certain basic telecommunications services are guaranteed to all Spanish citizens.

Universal service is defined, under the law, as a set of communication services guaranteed to all end users, irrespective of their geographic location, of a determined quality and at an affordable price. Universal service ensures that all citizens receive a connection to the fixed line public network and network services, a telephone directory service, a sufficient number of public telephones and functional Internet access. Additional provisions are included under the scope of universal service obligation, or USO, in order to ensure that users with disabilities and special social needs, including those with low incomes, have access to the services enjoyed by the majority of users.

In December 2008, following applications by three operators, Telefónica de España was awarded a tender for the provision of directory enquiry services for a period of three years and it has also been designated for the provision of the remaining universal service elements for a period of two years by virtue of Order ITC/3808/2008.

To finance the USO, the General Telecommunications Law stipulates that the CMT must determine whether the net cost to provide universal service implies an unfair burden for the operators. On September 2008, the CMT published a resolution which established net cost of USO for the years 2003, 2004 and 2005, the obligation of operators to contribute to USO funding and the amount of contributions these operators must make. During 2009, the CMT established the net cost of USO for the years 2006 and 2007.

Protection of consumers

On December 29, 2006, Law 44/2006 regarding the protection of consumers and users was approved. Under this law, users may only be charged for services actually used. Consequently, operators can only charge for the exact seconds of usage. On May 22, 2009 a set of User's Rights was adopted through secondary legislation and it

Table of Contents

constitutes a holistic approach to users' rights. Most of the content has been extracted from the General Telecommunications Law 32/2003 (LGT), Royal Decree 424/2005 of April 15, 2005 (RSU) and Order ITC/912/2006 (Quality Order).

Service quality

On March 29, 2006, a regulation was approved which established certain quality of service, or QoS, obligations for electronic communications service providers such as including service level agreements, or SLAs, commitments in electronic communication retail contracts. This regulation also requires operators to provide adequate information to customers in relation to service quality levels and detailed billing disclosure to customers. Additionally, a standardized process for billing customers has been implemented under this regulation.

Data retention for law enforcement purposes

The 2006 Directive 2006/24/EC of the European Parliament and of the Council on the retention of data generated or processed in connection with the provision of publicly available electronic communications services or of public communications networks ("Data Retention Directive") was incorporated into Spanish legislation on November 9, 2007. Electronic communications operators are obliged to ensure the retention of data on electronic communications for a period of twelve months.

Additionally, Spain has implemented a register of pre-pay mobile customers in conjunction with these requirements. Existing pre-pay customers have a period of two years for the registration since the law entered into force and the new clients must be registered immediately.

Public Broadcasting TV funding mechanism

In August 2009, the Spanish Parliament approved a new funding policy for public television, Radio Televisión Española ("RTVE"), which includes the discontinuation of advertising on public television. The new law includes a tax on telecommunications companies and television stations to help fund the phasing out of advertising on RTVE.

The new law applies a tax of 0.9% on the gross revenue of telecommunications companies providing audiovisual services in Spain and 3.0% in the case of regular TV broadcasters. Pay television stations will pay 1.5% of their gross revenue. Both the Spanish regulator and competition authority have questioned the legality of this funding mechanism in light of the national and European regulatory framework. The EU Directorate General of Competition has already opened an investigation to determine whether such funding mechanism constitutes illegal state aid. Without prejudice to the state aid investigation initiated in December 2009, the European Commission sent on March 18, 2010 a formal request for information to the Spanish government over the new charge imposed on telecommunications operators to offset the discontinuation of advertising on RTVE. The Commission is concerned that this administrative charge, based on authorized operators' gross revenue, may be incompatible with EU law since it does not appear to be related to costs arising from regulatory supervision. The Commission's position takes the form of a "letter of formal notice under EU infringement procedures" and provides the Spanish government with a two-month period to reply. If no reply is received or if the response of the Spanish government is not satisfactory, the Commission may issue a "reasoned opinion" under EU infringement procedures requesting the Spanish government to amend its legislation to ensure full compliance with EU rules.

Telefónica Europe

United Kingdom

The EU Regulatory Framework was implemented in the United Kingdom by the Communications Act in 2003. Under this act, responsibility for the regulation of electronic communications networks and services rests with the Office of Communications, or Ofcom.

Table of Contents

Licenses and concessions

Telefónica O2 UK has provided GSM services since July 1994. Its GSM license is of indefinite duration (GSM 900: 2 x 17.4 MHz and GSM 1800: 2 x 5.8 MHz). In April 2000 Telefónica O2 UK was awarded a UMTS license, which expires on December 31, 2021 (2 x 10 MHz + 5 MHz).

The license can be surrendered by the operator at any time. However, Ofcom can only revoke the license if the licensee does not pay its fees, there has been a breach of the license or for reasons related to the management of the radio spectrum, provided that in such case the power to revoke may only be exercised after one year's notice is given in writing and after Ofcom has considered any pertinent factors. The UK government may also revoke the license for national security reasons or in order to comply with the United Kingdom's EU or other international obligations.

In February 2009, Ofcom published a consultation document setting out Ofcom's proposal to require Vodafone and Telefónica O2 UK to release 2 x 2.5 MHz (each) of 900 MHz spectrum currently held to allow a third operator to have access. Ofcom's consultation also proposed that all 900 MHz and 1800 MHz licenses be enabled for UMTS services in line with the revisions to the GSM Directive, which must be implemented in the United Kingdom by May 9, 2010. Ofcom's consultation has subsequently been superseded by the UK Government's "Digital Britain" process.

In June 2009, the UK government published the "Digital Britain" final report, in which it proposed to issue a Direction to Ofcom to convert UMTS licenses, which currently expire in 2021, to indefinite licenses, subject to a yearly fee to be charged beyond the end of the current term.

Following the Digital Britain final report dated June 2009 and subsequent consultation by the UK government's Department for Business, Innovation and Skills (BIS), BIS published in October 2009 a draft Statutory Instrument ("Draft SI") which provided for the Secretary of State to direct Ofcom to liberalize the 900 MHz and 1800 MHz bands in the hands of the existing licensees, including Telefónica. The Draft SI proposed that Ofcom be directed to include certain wholesale access obligations into the varied 900 MHz licenses. The Draft SI also proposed that Ofcom be directed to convert the UMTS licenses, which currently expire in 2021, to indefinite licenses subject to revised retail service obligations and subject to a yearly fee, to be charged beyond the end of the current term.

Future spectrum

In June 2009, Ofcom withdrew its decision to auction the 2600 MHz band in light of the government's Digital Britain proposals (see above). As a condition of merger control clearance under the EU Merger Regulation for the Joint Venture between T-Mobile UK and Orange UK, the merging parties have committed to divest 2x15 MHz of spectrum in the 1800 MHz band.

Under the terms of the Draft SI, the Secretary of State will direct Ofcom to hold a Combined Auction of spectrum in the 800 MHz (2x30 MHz in six 2x5 MHz lots) and 2600 MHz bands (2x70 MHz of FDD spectrum in seven lots of 2x10 MHz). Ofcom will be also directed to auction 50 MHz of TDD 2600 MHz spectrum in one lot as soon as possible in advance of the Combined Auction. A future consultation on a combined 800 MHz/2600 MHz auction is awaited. The Draft SI includes provisions on the eligibility requirements for auctioned spectrum (including caps on the amount of spectrum held by any single party) and retail service / wholesale access obligations for certain lots of spectrum. Parties will have the ability to relinquish existing spectrum holdings in the 900 MHz and 1800 MHz bands and this spectrum will be auctioned in the Combined Auction.

Market reviews

On March 27, 2007, Ofcom published the charge controls to which mobile operators are subject for the provision of mobile call termination services from April 1, 2007 until March 31, 2011. The charge control requires that Telefónica O2 UK's average termination charges should be reduced to 5.1 pence per minute (at 2006-2007 prices) by the final year of the charge control period, and that the reduction should be implemented in four equal steps across the four years. Ofcom's decision imposing the price controls was appealed by British Telecommunications plc and Hutchison 3G UK Limited and, pursuant to those appeals, the UK Competition

Table of Contents

Commission reduced the level of the price cap to 4.0 pence per minute (at 2006-2007 prices) by the final year of the charge control period.

Germany

The EU Regulatory Framework was implemented in Germany at the end of June 2004 by the Telecommunications Act. Responsibility for regulation of electronic communications networks and services rests with the telecommunications regulator, Budesnetzagentur, or BNetzA.

Licenses and concessions

Telefónica O2 Germany was awarded a GSM license for 1800 MHz spectrum in October 1998, and in February 2007 Telefónica O2 Germany was awarded 900 MHz GSM spectrum for GSM use. Accordingly, Telefónica O2 Germany is now licensed to use GSM900 2 x 5 MHz and GSM 1800: 2 x 17.4 MHz. The GSM license expires on December 31, 2016.

Under Section 58 VIII TKG (the "German Telecommunications Act") frequency assignments are limited in time, although a renewal or extension of the term is possible. The federal network agency has not yet decided on the conditions for renewing the frequency assignments. However, before expiration, we expect there to be a public hearing, and for BNetzA to set out its approach to renewal, including the terms on which the licenses will be extended (pricing, technology neutrality, etc.).

In August 2000, Telefónica O2 Germany was awarded a UMTS license, which expires on December 31, 2020 (2 x 9.9 MHz).

Market reviews

In August 2006, BNetzA completed its review of voice call termination on individual mobile networks and concluded that, as an operator with SMP, the charges Telefónica O2 Germany made to other operators for terminating calls on Telefónica O2 Germany network had to be reduced, requiring Telefónica O2 Germany to lower its call termination charges from €1.24 per minute to €0.994 per minute. In 2007, Telefónica O2 Germany was required to reduce further its termination charges from €0.994 per minute to €0.880 per minute. Telefónica O2 Germany has brought legal challenges against BNetzA's 2006 and 2007 decision that Telefónica O2 Germany has significant market power and against the imposition of regulatory remedies. The Federal Administrative Court, as the highest level of appeal, confirmed all regulatory remedies meaning that the price controls stay in force for all mobile operators. All four German mobile operators filed a Constitutional Complaint in order to challenge the decision regarding significant market power. All other actions (regarding the amount of MTRs) are pending and a decision by the Constitutional Court is expected in the first or second quarter of 2010. The new market analysis of BNetzA in 2008 again concluded that all mobile network operators have SMP, and the decision on remedies does not contain changes in comparison to 2006. This 2008 decision has also been challenged by Telefónica O2 Germany.

In March 31, 2009 and as of April 1, 2009, BNetzA approved MTR for Telefónica O2 Germany at €0.714 per minute for a period of 20 months (until November 30, 2010).

Spectrum

BNetzA decided in February 2006 that Telefónica O2 Germany may use GSM 900 spectrum in exchange for GSM 1800 spectrum. This decision is under the condition that Telefónica O2 Germany provides access to spectrum to German Railways if it is necessary for the European Train Control System (ETCS). Telefónica O2 Germany took legal action against this condition. In the meantime, this condition was repealed by BNetzA in April 2009, and therefore, Telefónica O2 Germany declared the case as settled. However, German Railways, Airdata and Inquam (providers of local networks) appealed the decision. All cases have been dismissed in the first instance in December 2007 and each party appealed its decision. In the German Railways case, the Higher Administrative Court dismissed the appeal of German Railways on September 16, 2009. German Railways did not appeal this decision at the Federal Administrative Court, and the decision is legally binding. In the Airdata case, the appeal to the Higher Administrative Court has been dismissed. Airdata is now appealing at the Federal Administrative Court. The case

Table of Contents

is still open. In the Inquam case, the Administrative Court dismissed the claim of Inquam on October 21, 2009, and the decision is legally binding with no further challenge possible.

In October 2009, BNetzA decided to auction mobile spectrum at 2.6 GHz (70 MHz FDD / 50 MHz TDD) together with available spectrum at 2.1 GHz (19,8 MHz FDD [ex. Mobilcom + QUAM] /19.2 MHz TDD) and 1.8 GHz (10 MHz FDD [ex. O2 + eplus]) and 800 MHz (Digital Dividend). In the 800 MHz range, a bandwidth of 30 MHz paired spectrum will be auctioned off in six blocks of 5 MHz. The decision was published on October 21, 2009. BNetzA has separated the refarming and auction in two procedures. Spectrum redistribution is not included in the refarming process. A spectrum cap of 2x20 MHz for spectrum below 1 GHz has been implemented. In favor of the D-Net-Operators, the spectrum cap has been rounded up to 22.4 MHz (for T-Mobile and Vodafone only). Telefónica O2 Germany filed a claim against that decision on November 18, 2009. The Administrative Court of Cologne decided on March 17, 2009 to dismiss the claims of Telefónica O2, Eplus and Airdata against BNetzA’s decision regarding the design of the upcoming frequency auction. Appeal to the next instance at the Federal Administrative Court is allowed within one month period. The appeal is currently being considered by the parties. Nevertheless, Telefónica O2 Germany submitted an application for participation at the auction. The auction is most likely to start on April 12, 2010.

Table of Contents

Czech Republic

The EU Regulatory Framework was implemented in the Czech Republic in 2005 by the Electronic Communications Act. Responsibility for regulation of electronic communications networks and services rests with the Czech Telecommunication Office, or CTO. Governmental responsibility for the area of electronic communications lies with the Ministry of Industry and Trade.

Several changes occurred in the legal environment of the electronic communications market in the Czech Republic in 2007. Act No. 127/2005 Coll. on electronic communications and on amendment of related laws was amended in respect of provisioning special price plans to the disabled as part of universal service and radio and television broadcasting. Furthermore, an amendment to the act on radio and television broadcasting was passed, primarily to unblock the transition to terrestrial digital broadcasting. In 2008, another amendment to the Act No. 127/2005 Coll for the implementation of Directive 2006/24/EC (Data Retention Directive) and the Regulation (EC) No 717/2007 on roaming on public mobile communications networks within the Community.

Licenses and concessions

Telefónica O2 Czech Republic performs communication activities under the Electronic Communications Act based on a notification to and a certificate from the CTO number 516 as amended by later changes numbers 616/1, 516/2 and 516/3.

Mobile segment

Telefónica O2 Czech Republic provides mobile electronic communications services in the 900 and 1800 MHz frequency bands under the GSM standard on the basis of radio frequency assignment from CTO valid until February 7, 2016; in the 2100 MHz frequency band under the UMTS standard on the basis of radio frequency assignment from CTO valid until January 1, 2022; and in the 450 MHz frequency band using CDMA 2000 (Code Division Multiple Access, or CDMA) technology on the basis of radio frequency assignment from CTO valid until February 7, 2011.

In March 2009 CTO conducted a tender for 32 free channels in the former E-GSM band with participation of Telefónica O2 Czech Republic, T-Mobile and Vodafone. These 32 free channels were divided according to the conditions of the tender as follows:

- Telefónica O2 Czech Republic - 7 channels
- T-Mobile - 6 channels
- Vodafone - 19 channels.

Telefónica O2 Czech Republic was awarded the seven channels in June 2009 with the same conditions as former GSM900 allotment (including date of expiration). The fee for Telefónica O2 Czech Republic's seven channels was CZK 29,654,000.

Market reviews

In accordance with the market analyses performed by the CTO, Telefónica O2 Czech Republic was designated an SMP entity in 12 Czech markets, both retail and wholesale. The CTO started a second round of market analysis in 2007. In accordance with reviewed Commission Recommendation on relevant product and service markets from December 2007, CTO decreased the number of markets susceptible to ex ante regulation from 18 to seven (one retail and six wholesale). Regulatory obligations on the remaining markets were withdrawn in 2008 and 2009. Telefónica O2 Czech Republic was designated as an SMP on the wholesale broadband market in 2009. Market reviews of the remaining six relevant markets are in the final phase, and the CTO proposes to designate Telefónica O2 Czech Republic as SMP operator in all of them.

Table of Contents

Prices and tariffs

In April 2006, price regulations for access at a fixed point to the telephone network and for calls in the fixed network were abolished. Subsequent analyses of the relevant markets showed that no further price regulation was necessary. Additionally, provision of access at a fixed location was taken out of the scope of universal service in 2006. Besides the absence of price controls at the retail level, CTO also refrained from price controls on the wholesale broadband market during both market reviews it has conducted.

Slovakia

Telefónica O2 Slovakia performs electronic communication activities under Act No. 610/2003 Coll., the Electronic Communications Act, (as amended) and General Authorization (as amended) issued by the Slovak NRA (the Telecommunications Office of Slovak Republic) based on a notification, as well as a number of allocation certificates issued by the NRA.

Responsibility for regulation of electronic communications networks and services rests with the Telecommunication Office of Slovakia. Governmental responsibility for the area of electronic communications lies with the Ministry of Transport, Post and Telecommunications of Slovakia.

Licenses and concessions

On September 7, 2006, Telefónica O2 Slovakia was granted a license to provide electronic communications services by the means of the public electronic communications network using the GSM and UMTS mobile telephone network standards and became a third mobile operator in Slovakia after 10 years of duopoly of two original mobile operators. The license has been granted for 20 years and expires in September 2026. The commercial operations were launched on February 2, 2007.

Market analysis

In accordance with the market review performed by the NRA, Telefónica O2 Slovakia has been designated an SMP operator on the wholesale mobile termination market, the only regulated mobile market in Slovakia. Wholesale termination price regulation is effective from August 2009, and since February 2010 the wholesale termination price regulation is based on the EU benchmarking methodology. From September 2009, Telefónica O2 Slovakia as a new entrant and market challenger also benefits from a shorter mobile number portability process, a maximum length of which was set by the regulator to five working days. No retail price regulation is applicable in Slovakia.

Future mobile spectrum

A tender for 2.6 GHz frequencies, with potential of subsequent long-term operation, is expected during the first half of 2011.

Ireland

In Ireland responsibility for the regulation of electronic communications networks and services rests with the Commission for Communications Regulation, or ComReg. The main legislation under which Telefónica O2 Ireland operates includes: the Wireless Telegraphy Act 1926, as amended, (45 of 1926), Post and Telecommunications Services Act 1983 as amended, (24 of 1983),Communications Regulation Acts 2002 (20 of 2002) and 2007 (22 of 2007), 3G Mobile Telephony Licensing Regulations (340 of 2003) and GSM Mobile Telephony Licensing Regulations (339 of 2003).

Licenses and concessions

Telefónica O2 Ireland has provided GSM services since March 1997 after having been awarded a license in May 1996. Its GSM900 license has a duration of 15 years (GSM900: 2 x 7.2 MHz) from 1996. In 2000 it was awarded an additional GSM 1800 license (2 x 14.4 MHz), which also has a term of 15 years. In October 2002 Telefónica O2 Ireland was granted a UMTS license, which has duration of 20 years (2 x 15 MHz + 5 MHz).

Table of Contents

The license can be surrendered by the operator at any time. However, ComReg can only revoke the license before its expiration date if the licensee does not pay its fees or if there has been a substantial breach of the terms of the license.

The Minister for Communications, Energy and Natural Resources may also revoke the license for national security reasons, or in order to comply with EU or other international obligations.

Future mobile spectrum

In March 2008, ComReg published a draft strategy document for spectrum management during the period from 2008 through 2010. ComReg has published three consultation documents in a process to decide the future licenses in the 900 MHz band. At present, ComReg is proposing to auction all of the spectrum in this band in 2010. ComReg has also begun a consultation process to determine how to allocate spectrum in the 2.3 GHz band, and a consultation is expected in 2010 to determine the approach to assignment of the 2.6 GHz band (3G expansion band). ComReg is in favor of licensing the 800 MHz band (Digital Dividend), however, the timing for this is dependent on the government finalizing a date for analogue TV switch-over.

Market reviews

Telefónica O2 Ireland has been found to have SMP in the market for mobile termination. ComReg has previously decided to forebear from the imposition of regulated pricing so long as it could reach agreement with the main operators for a "glide path" for annual reductions in mobile termination rates. A glide path is currently in place for all operators to cut mobile termination rates to €0.05 per minute by 2012/2013, subject to staying within €0.01 per minute, the European regulators' group average MTR.

Telefónica Latin America

Brazil

Regulatory framework

The delivery of telecommunications services in Brazil is subject to regulation under the regulatory framework provided in the General Telecommunications Law enacted in July 1997.

The National Agency for Telecommunications, ANATEL, is the principal regulatory authority for the Brazilian telecommunications sector.

Licenses and concessions

Concessions are granted for services provided in the public regime and authorizations are granted for services provided in the private regime. The only service provided in both regimes is the switched fixed telephone service, or STFC. All other services are provided only in the private regime.

The main differences between the public regime and the private regime relate to the obligations imposed on the companies. The concessionaires in the public regime, such as Telesp, have network expansion obligations (universal services obligations) and continuity of service obligations. These obligations are not imposed on the companies which provide services in the private regime.

In the state of São Paulo, Telesp provides local and long distance STFC under the public regime. In the other Brazilian states, Telesp provides local and long distance STFC under the private regime and broadband services under the private regime.

Telesp's concession agreements (local and long distance) were extended in December 2005 for an additional period of 20 years. These agreements contemplate possible revisions in their terms by ANATEL in 2010, 2015 and 2020. In 2009, Telesp presented comments and suggestions to ANATEL's public consultation regarding the 2010 concession contract revision, but ANATEL has not presented the final version of the contract yet. Telesp's terms of authorization (local and long distance) were granted for an unlimited period of time.

Table of Contents

Under the renewed concession agreements and during the 20-year renewal period, Telesp will be required to pay a biannual fee equal to 2% of its annual net revenue (excluding taxes and social contributions), for the provision of fixed-line public telecommunications services in its concession area (State of São Paulo) for the prior year.

Brazilian telecommunications regulations require ANATEL to authorize private regime companies to provide local, national, and international long distance STFC.

On November 20, 2008, the Presidential Decree 6,654 altered the General Concessions' Plan, enabling one economic group to hold two of the four existing area concessions for providing STFC services. Thus, the Decree increased the flexibility of telecommunications provider groups as STFC concessionaries by allowing such providers to provide services in up to two General Plan regions. Prior to the Decree telecommunications provider groups could offer STFC services in only one region.

Telesp also has an authorization to provide data and broadband services in the private regime in the State of São Paulo.

On December 4, 2002, ANATEL authorized the migration from the cellular mobile service, or SMC, regime to a new licensing regime, personal mobile service. Brasilcel's operators replaced all their old licensing titles granted under the old SMC regime with new personal mobile service authorization titles. The new personal mobile service licenses include the right to provide mobile services for an unlimited period of time but restrict the right to use the spectrum according to certain schedules included in the licenses. All Telefónica's Brazilian mobile operating companies (the existing ones and some new acquisitions) were renamed "Vivo" with the exception of Telemig Celular. The following licenses are held by our Brazilian mobile operating company, Vivo:

- Vivo-Rio Grande do Sul ("A" Band) until 2022 (renewed in 2006);
- Vivo-Rio de Janeiro ("A" Band) until 2020 (renewed in 2005);
- Vivo-Espírito Santo ("A" Band) until 2023 (renewed in 2008);
- Vivo-Bahia ("A" Band) and Vivo-Sergipe ("A" Band) until 2023 (renewed in 2008);
- Vivo-São Paulo ("A" Band) until 2023 or 2024, for the cities of Ribeirão Preto and Guatapará (renewed in 2008);
- Vivo-Paraná/Santa Catarina ("B" Band) until 2013;
- Vivo-Distrito Federal ("A" Band) until 2021, (renewed in 2006);
- Vivo-Acre ("A" Band), Vivo-Rondônia ("A" Band), Vivo-Mato Grosso ("A" Band) and Vivo-Mato Grosso do Sul ("A" Band) until 2024 (renewed in 2008);
- Vivo-Goiás/Tocantins ("A" Band) until 2023 (renewed in 2008);
- Vivo-Amazonas/Roraima/Amapá/Pará/Maranhão ("B" Band) until 2013;
- Telemig Celular (Minas Gerais) ("A" Band) until 2023 (renewed in 2007);
- Telemig Celular (for the cities where CTBC Telecom operates in the state of Minas Gerais) ("E" Band) until 2020.

For “A” and “B” Bands, the renewal of licenses must be solicited 30 months before expiration. Spectrum rights may be renewed only once for a 15-year period, after which title to the license must be renegotiated.

For “E” Band, the renewal of licenses must be solicited between 36 and 48 months before expiration. Spectrum rights may be renewed only once for a 15-year period, after which title to the license must be renegotiated. In December 2007, ANATEL auctioned fifteen new licenses in the 1900 MHz radio frequency band, denominated as “L” Band. Vivo acquired 13 spectrum licenses in “L” Band.

Table of Contents

- Vivo-Rio Grande do Sul ("L" Band) until 2022 (renewed in 2006) or 2022 for the cities of the metropolitan area of Pelotas;
- Vivo-Rio de Janeiro ("L" Band) until 2020 (renewed in 2005);
- Vivo-Espírito Santo ("L" Band) until 2023 (renewed in 2008);
- Vivo-Bahia ("L" Band) and Vivo-Sergipe ("L" Band) until 2023 (renewed in 2008);
- Vivo-São Paulo ("L" Band) until 2023 or 2024, for the cities of Ribeirão Preto and Guatapará (renewed in 2008) or 2022 for the cities where CTBC Telecom operates in the state of São Paulo;
- Vivo-Paraná (excluding the cities of Londrina and Tamarana)/Santa Catarina ("L" Band) until 2013;
- Vivo-Distrito Federal ("L" Band) until 2021, (renewed in 2006);
- Vivo-Acre ("L" Band), Vivo-Rondônia ("L" Band), Vivo-Mato Grosso ("L" Band) and Vivo-Mato Grosso do Sul ("L" Band) until 2024 (renewed in 2008) or 2022 for the city of Paranaíba of Mato Grosso do Sul; and
- Vivo-Goiás/Tocantins ("L" Band) until 2023 (renewed in 2008) or 2022 for the cities where CTBC Telecom operates in the state of Goiás; and Vivo-Alagoas/Ceará/Paraíba/Piauí/Pernambuco/Rio Grande do Norte ("L" Band), until 2022.

For "L" Band, the renewal of licenses must be solicited between 36 and 48 months before expiration. Spectrum rights may be renewed only once for a 15-year period, after which title to the license must be renegotiated.

In April 2008, ANATEL auctioned 36 new licenses in the 1900-2100 MHz radio frequency bands (3G licenses). Vivo was awarded seven spectrum licenses in Band J and Telemig Celular was awarded two licenses.

- Vivo-Rio Grande do Sul (including the cities of the metropolitan area of Pelotas) ("J" Band) until 2023;
- Vivo-Rio de Janeiro ("J" Band) until 2023;
- Vivo-Espírito Santo ("J" Band) until 2023;
- Vivo-Bahia ("J" Band) and Vivo-Sergipe ("J" Band) until 2023;
- Vivo-São Paulo (including the cities of Ribeirão Preto and Guatapará and the cities where CTBC Telecom operates in the state of São Paulo) ("J" Band) until 2023;
- Vivo-Paraná (including the cities of Londrina and Tamarana)/Santa Catarina ("J" Band) until 2023;
- Vivo-Distrito Federal ("J" Band) until 2023;
- Vivo-Acre ("J" Band), Vivo-Rondônia ("J" Band), Vivo-Mato Grosso ("J" Band) and Vivo-Mato Grosso do Sul (including the city of Paranaíba) ("J" Band) until 2023;
- Vivo-Goiás (including the cities where CTBC Telecom operates in the state of Goiás)/Tocantins ("J" Band) until 2023;

- Vivo-Alagoas/Ceará/Paraíba/Piauí/Pernambuco/Rio Grande do Norte (“J” Band), until 2023;
- Vivo-Amazonas/Roraima/Amapá/Pará/Maranhão (“J” Band) until 2023; and
- Telemig Celular (including the cities where CTBC Telecom operates in the state of Minas Gerais) (“J” Band) until 2023.

Table of Contents

For “J” Band, the renewal of licenses must be solicited between 36 and 48 months before expiration. Spectrum rights may be renewed only once for a 15-year period, after which title to the license must be renegotiated.

Prices and tariffs

ANATEL regulates rates for the STFC provided in the public regime. Operators with licenses to operate under the personal mobile regime are authorized to increase basic plan tariffs only for inflation and only on an annual basis. Operators are also allowed to establish non-basic tariffs and modify them without ANATEL’s prior approval.

Interconnection

In July 2005, ANATEL published a new regulation for interconnection among providers of telecommunications services, which require operators to issue a public document disclosing all of the conditions for the establishment of interconnection for all classes and types of services.

The SMP regime allows operators to freely negotiate interconnection rates with other operators. If they fail to reach an agreement, each operator may call upon ANATEL to determine the terms and conditions of interconnection.

Competition law

Brazilian competition regulation is based on Law No. 8,884 of June 11, 1994 which prohibits any practice aimed at restricting free competition, dominating the relevant market of goods or services, arbitrarily increasing profits, or abusively exercising dominant market position. The Economic Law Office, or SDE, the Secretariat for Economic Monitoring, or SEAE, and the Administrative Council for Economic Defense, or CADE, are the agencies authorized to enforce the competition rules.

Mexico

Regulatory framework

The provision of all telecommunication services in Mexico is governed by the Federal Telecommunication Law and various service-specific regulations. The governmental agencies which oversee the telecommunications industry in Mexico are the Secretariat of Communications and Transportation, or SCT, and the Federal Telecommunications Commission, or COFETEL.

Licenses and concessions

In Mexico, authorizations to provide mobile telephony services (mobile and personal communication services, or PCS, for the 800 MHz and 1.9 GHz bands, respectively) are granted through concessions. Currently, regarding the mobile concessions (800 MHz), only one Band A and one Band B service provider may provide mobile telephony services in each of the nine regions of the country. Regarding PCS concessions, there is no exclusivity in the provision of service, in each region by more than one operator. In fact, there are currently three operators in each region. These concessions were granted in 1998 and 2005 for a period of twenty years, and may be renewed for additional 20-year periods, subject to the fulfillment by the operator of certain terms and conditions.

In total, Telefónica Móviles México, and its subsidiaries and participated companies have 22 licenses granted by SCT, which enable it to provide telecommunications services:

-

Telefónica Móviles México's mobile operating companies have been granted concessions to operate mobile telephony services on Band A until 2010. SCT granted licenses to Baja Celular Mexicana, S.A. de C.V., or Bajacel, dated July 17, 1990; Movitel del Noroeste, S.A. de C.V., or Movitel, also dated July 17, 1990; Telefonía Celular del Norte, S.A. de C.V., or Norcel, dated July 23, 1990; and Celular de Telefonía, S.A. de C.V., or Cedetel, dated August 2, 1990. The renewal of these four concessions was requested in 2005. We presented in 2005 four requests for extension of these concessions before SCT. The concessions of Bajacel, Movitel y Norcel have been renewed for 15 years from 2010. The terms and conditions of the renewed concessions are consistent with those concessions that SCT has recently assigned and to those

Table of Contents

terms and conditions that it will establish in future concessions. As of the date of this report, we are expecting the formality of receiving the concessions. In respect of Cedetel, the proposal for renewal was notified by the STC, and it is expected that Cedetel will acept the proposal in due course. Any further delay in the renewal process to obtain the requested extensions will be attributed to the SCT.

- Furthermore, SCT granted to Telefónica Móviles México, through Pegaso Comunicaciones y Sistemas, S.A. de C.V. a concession to provide public telecommunications services, on June 23, 1998, and nine spectrum licenses, dated October 7, 1998, in the 1900 Mhz band to provide personal communication services in each of the nine PCS service region, and valid until 2018. Those licenses may be extended for additional twenty-year periods. For all of these licenses renewal was requested in 2008, the renewal decision is still pending, and we are permitted to continue operating under the terms of the expired licenses until the renewal has been approved. On April 21, 2005, SCT granted Telefónica México four more spectrum licenses in the same 1900 MHz band, to provide the PCS service and have more bandwidth in regions 3, 5, 7 and 8, valid for 20 years, and with the possibility be renewed for up to 20 additional years. On September 7, 2009, a modification to Pegaso's concession was authorized to provide trunked radio services.

- SCT also granted to Grupo de Telecomunicaciones Mexicanas, S.A. de C.V., or GTM, a company in which Telefónica Móviles México has an interest, several licenses:

i) on June 24, 1998, to install microwave links in 23 GHz frequencies, for a period of 20 years;

ii) on December 13, 1999, to install microwave links in 7 GHz frequencies, for a period of 20 years, and that can be renewed;

iii) on June 5, 2003, to install a public telecommunication network to provide domestic and international long distance service granted, for a period of 15 years, and that can be renewed; and

iv) on March 28, 2006, GTM was authorized a renewal of the concession to provide fixed telephony and public telephony, nationwide for a period of 15 years, that can be renewed.

Prices and tariffs

Tariffs charged to customers are not regulated. They are set by mobile operating companies and must be registered with COFETEL. Rates do not enter into force until registered by COFETEL.

Interconnection

Mexican telecommunications regulations obligate all telecommunications network concessionaires to execute interconnection agreements on specific terms when requested by other concessionaires. Interconnection rates and conditions may be negotiated by the parties. However, should the parties fail to agree, COFETEL must fix the unresolved issues, including tariffs.

Foreign ownership/restrictions on transfer of ownership

Mexican foreign investment law restricts foreign investment in local fixed service and other telecommunications services to a maximum of 49% of the voting stock, unless the Mexican National Commission of Foreign Investment approves a higher percentage participation, which it can do only in the case of mobile telecommunications companies.

Bajacel, Movitel, Norcel, Cedetel and Pegaso, as mobile telecommunications companies, received the required approvals from the National Commission of Foreign Investment permitting our ownership of more than 49% of their outstanding voting capital.

GTM, a company in which Telefónica México has an interest, provides local fixed and long distance services. This operator complies with Mexican foreign investment law, and has a stock structure that includes the participation of its Mexican partner, Enlaces del Norte. S.A. de C.V., which has 51% of the voting stock.

Table of Contents

Competition law

The Federal Economic Competition Law enacted in 1992 and amended on June 28, 2006 prohibits monopolies and any practices that tend to diminish, harm or impede competition in the production, processing, distribution or marketing of goods and services. The Federal Competition Commission, or COFECO, is the administrative body empowered to enforce the Law.

Venezuela

On June 1, 2000, the national legislative commission approved the Telecommunication Law. On February 1, 2006, the national legislative commission approved the Ley Habilitante that grants the President of the Republic capacity to enact decrees in relation to the telecommunication sector, though no formal modification to current law has been made.

On December 2009, a new regulation applicable to all subscription TV service providers was enacted by CONATEL in order to stipulate a new obligation concerning a mandatory percentage of inclusion (12%) of national production services (channels in which both reception and diffusion of sound and images take place in the country to later transmit it by means of subscription TV service providers) in the regular programming packages. The calculation of the mandatory percentage is to be made on the basis of the totality of the TV channels. Qualification of a channel as a "national productions service" is a task of CONATEL, who must keep an updated record of those services.

An Administrative Decision on Services Agreements (Providencia n° 1302 sobre Condiciones Generales de los Contratos de Servicios de Telecomunicaciones) was adopted. As a consequence of this regulation (2009), Telcel proceeded to adapt all of its nine services agreements to fulfill all the conditions and impositions established, mainly related to consumer protection. We have currently received regulator observations of two of the agreements (TV service and radio localization service), and we are in process of including the modifications based on the observations.

Licenses and concessions

Telcel has been granted a mobile telephony concession to operate and offer mobile services in the 800 MHz band with national coverage, granted in 1991 and expiring on May 31, 2011 that may be extended for a term no longer than 20-year, subject to CONATEL's discretion. Telcel also holds a private network services concession, granted in 1993 and renewed on November 28, 2007, until December 15, 2025, that allows Telcel to offer point-to-point or point-to-multipoint private telecommunication services to corporations. In 2000, Telcel was granted a general license (Habilitación General) to offer local telephony services, national long distance services and international long distance services and to otherwise operate telecommunications networks for a 25-year period expiring on December 15, 2025. In 2001, Telcel obtained a concession to offer fixed wireless access services nationwide using wireless local loop technology.

On November 28, 2007, the National Telecommunications Commission, or CONATEL, in accordance with the Telecommunications Law, incorporated into the general license the rest of the services provided by Telcel: mobile, private networks, Internet access and transport. On that same date, Telcel was granted a concession to operate in the 1990 MHz band for a period of 15 years, until November 22, 2022, renewable for a period of ten years.

Prices and tariffs

Under Venezuelan regulations, telecommunications operators are free to determine and set prices for the services that they offer, within the price cap established by the regulator. However, exemptions to the free pricing regime may be applicable to market dominant operators, universal services projects or as a result of market distortions caused by anti-competitive conduct as determined by the Competition Agency.

Competition law

Venezuelan law governing competition is the Promotion and Protection of Free Competition Act 1992. It prohibits monopolistic and oligarchic practices and other means that could impede, restrict, falsify, or limit the

71

Table of Contents

enjoyment of economic freedom. The Office of the Superintendent for the Promotion and Protection of Free Competition is the agency empowered to apply the Competition Act.

Chile

Regulatory framework

The General Telecommunications Law No. 18,168 of 1982, as amended, establishes the legal framework for the provision of telecommunications services in Chile.

The main regulatory authority in Chile is the Under-Secretary of Telecommunications, or SUBTEL.

Licenses and concessions

Under the General Telecommunications Law, companies must obtain licenses in order to provide fixed telecommunications services. Licenses granted for public and intermediate services generally have 30-year terms and may be renewed indefinitely for 30-year periods at the request of the operator, though certain licenses held by Telefónica Chile have longer terms.

Telefónica Chile holds the following licenses for the provision of telecommunications services:

- Local telephony public service licenses. Telefónica Chile holds a license for local telephone service in all regions of Chile for a 50-year renewable period which began on December 1982, except Regions X and XI, which were incorporated to such license in 1995. In addition, Telefónica Chile holds various other renewable license for nationwide local telephone services oriented, exclusively, for rural localities Telefónica Chile also holds a nationwide public service renewable license for data transmission for a 30-year period beginning as of July 1995, and four other public service renewable licenses for data transmission for a 30-year period beginning as of June 2008.

- Multicarrier long-distance licenses. Under the Multicarrier System, Telefónica Chile's former long-distance subsidiary, Telefónica Mundo Larga Distancia S.A. (before Telefónica Mundo), held 30-year renewable licenses, for a period beginning as of November 1989, to install and operate a nationwide fiber-optic network, a network of base stations and other transmission equipment, and to provide domestic and international long-distance services, including voice, data and image transmission, throughout Chile. In addition, Telefónica Mundo Larga Distancia S.A. held 30-year renewable licenses, for a period beginning as of June 1993, to nationwide public service data transmission. Telefónica Chile's other long-distance subsidiary, Globus, also held licenses for an indefinite term to provide domestic and international long-distance services through central switches and cable and fiber-optic networks nationwide. After the merger of these subsidiaries in 2006, all the aforementioned licenses remain under the ownership of the same company, which is now known as Telefónica Larga Distancia.

    - Public service data transmission. In addition to the 30-year data transmission license previously mentioned, Telefónica Chile, through Telefónica Empresas, holds, as of March 1987, nationwide public service data transmission licenses for an indefinite term.

- Public service mobile telephony licenses. Telefónica Móviles Chile holds licenses with indefinite terms, beginning as of November 1989, to provide public service mobile telephony services throughout Chile in the 800 megahertz frequency range. Telefónica Móviles Chile also holds three concessions for the provision of mobile telecommunications services nationwide in the 1900 MHz band. These concessions may be renewed for successive thirty-year periods as of 2002 at the request of the holder.

- Limited television license. Telefónica Chile's subsidiary Telefónica Multimedia, has a license to establish, operate, and use a part of the spectrum of the 2.6 GHz bandwidth in Santiago, Chile, for an intermediate telecommunications service concession, authorizing the frequencies used to communicate voice, data and images, for a 30-year period beginning as of May 2008 Telefónica Multimedia also holds a license authorized by Resolution No. 47 enacted on November 28, 1990, amended by Resolution No. 1536 of 1994, and Resolution 1453 of 2002, to provide limited television service in 2,6 GHz. Since December

Table of Contents

2005, Telefónica Chile, through Telefónica Multimedia, holds a nationwide 10-year renewable license to provide limited satellite television service. Additionally, in January of 2006, Telefónica Chile, through Telefónica Multimedia, was assigned a limited television service license to provide the service nationwide in the main municipalities, except Region III, through Telefónica Chile's xDSL broadband network for an indefinite period. Moreover, in March 2007, a limited television service license was granted in order to provide this service, through the DSL broadband network, in the Santiago Metropolitan area, for an indefinite period.

Prices and tariffs

Under the General Telecommunications Law, maximum tariffs for telephony services are set every five years by the Ministry of Transport and Telecommunications and the Ministry of Economy. In addition, the Competition Tribunal may subject any telephony service to price regulation, except for mobile telephone services to the public that are expressly exempted under the General Telecommunications Law.

The Competition Tribunal ruled in January 2009 that only some local telephone services were to be subject to tariff regulation (line connections, monthly fixed charges, variable traffics charges, and public payphone services are excluded). Accordingly, it was determined that every local telephone company, within its service zones, would be regulated with respect to tariff levels and structure. In addition, Telefónica Chile, in its capacity as a "dominant operator" (except in regions where other companies are the dominant operators), is regulated on a non-price basis, with requirements that it not engage in discriminatory pricing and that it give previous notice of plans and packages.

Interconnection

Interconnection is obligatory for all license holders with the same type of public telecommunications services and between telephony public services and intermediate services that provide long distance services. The same requirement applies to holders of those intermediate service licenses, who are required to interconnect their networks to the local telephone network.

A "calling party pays" tariff structure was implemented on February 23, 1999. Under this tariff structure, local telephone companies pay mobile telephone companies an access charge for calls placed from fixed networks to mobile networks. Local telephone companies may pass this interconnection charge on to their customers. Every five years, SUBTEL sets the applicable tariffs for services provided through the interconnected networks.

Competition law

The principal regulation concerning competition in Chile is Decree No. 211 of 1973, whose current text was established in Decree Nº 1 of 2005. Pursuant to the provisions of this law, acts or behavior involving economic activities that constitute abuse of a dominant market position, or limit, restrain, or distort free competition in a manner that injures the common economic interest in the national territory are prohibited. The Competition Tribunal deals with infringements of competition law.

Argentina

Regulatory framework

The basic legal framework for the provision of telecommunications services in Argentina is set forth in the National Telecommunications Law (No. 19,798) of 1972 and in the specific regulations governing each type of telecommunications service. Also, Decree 264/98 established a transitory period from a monopolistic market towards a free market, promoting the protection of small operators while imposing obligations on basic services licensees. Decree 764/00, established the new and actual regulatory framework rules for a free market, and includes interconnection, licenses, universal service and spectrum rules.

The following regulatory authorities oversee the Argentine telecommunications industry:

- the National Communications Commission, or CNC, supervises compliance with licenses and regulations, and approves changes to mandatory goal and service requirements; and

- the Secretariat of Communications, or SECOM, grants new licenses, regulates the bidding and selection processes for radio-spectrum authorizations, and approves the related bidding terms and conditions.

Licenses and concessions

Telefónica de Argentina holds licenses for fixed line services, all granted for an unlimited period of time, which entitle it to provide fixed line telecommunications services; international telecommunications services; local services in the northern and southern regions; long distance, international and data transmission telecommunications services in the northern region; and Internet access and international data transmission services.

Telefónica Móviles de Argentina's licenses for the provision of mobile services include PCS licenses and corresponding authorizations for use of spectrum for different regions, licenses and corresponding authorizations for use of spectrum for mobile telephone services for different regions; and licenses for trunking, or closed user group, services for different cities.

These licenses do not expire, but may be cancelled by the SECOM as the result of failure to comply with the terms of its license.

Prices and tariffs

On October 21, 2003, Law No. 25,790 became effective, extending the term for the renegotiation of concession or licensing agreements with public utilities until December 31, 2004, which was subsequently extended until December 31, 2011. This law also established that the decisions made by the Argentine government during the renegotiation process shall not be limited by, nor subject to, the stipulations contained in the regulatory frameworks currently governing concession or licensing agreements for the respective public utilities. Renegotiated agreements may cover some aspects of concession or licensing agreements and may contain formulas to adjust such agreements or temporarily amend them. As an investor in Argentina through Telefónica de Argentina, we commenced arbitration proceedings against the Republic of Argentina based on the Reciprocal Protection of Investments Treaty between Spain and Argentina for damages suffered by us because of the measures adopted by the Argentine government. On August 21, 2009, the parties requested the Tribunal, in accordance with Rule 43 of the ICSID Arbitration Rules, declare a resolution of the termination of the proceedings. The agreement of the parties envisages the possibility of a new request for arbitration under the ICSID Convention being submitted by Telefónica. Such request would be processed in accordance with the ICSID Convention and the Center's normal rules and procedures taking note of the discontinuance issued by the Tribunal on September 24, 2009.

Additionally, Decree No. 764/00 established that providers of telephone services may freely set rates and/or prices for their service which shall be applied on a non-discriminatory basis. However, until the Secretary of Communications determines that there is effective competition for telecommunications services, the "dominant" providers in the relevant areas (which include Telefónica de Argentina) must respect the maximum tariffs established in the general tariff structure. Providers may freely set their rates by areas, routes, long distance legs and/or customer groups so long as they are below the amounts established by the general tariff structure.

Table of Contents

Also, the guidelines set forth in article 26 of Decree No. 1185/90 continue in effect for operators with significant market power. These guidelines establish information obligations with which operators must comply with respect to tariffs, both toward clients and the national regulator. This Decree also establishes the powers the regulator has to revise or revoke such tariffs.

Tariffs charged to customers for mobile services are not regulated in Argentina.

Interconnection

Decree No. 764/00 approved new rules for national interconnection and established interconnection standards and conditions with which telephone service providers must comply regardless of pre-existing agreements. The rules for national interconnection set forth that interconnection agreements are to be freely negotiated between the relevant service providers, on a non-discriminatory basis. The regulations also establish the obligation for dominant and significant market operators to unbundle their local loops and to allow competitors to use them on a reasonable basis.

Competition law

Law 25,156, on Protection of Competition prohibits any acts or behaviors related to the production or trade of goods or services, whose purpose or effect is to prevent, restrict or distort competition or market access, or that constitute abuse of dominant position in a market. The National Commission for the Defense of Competition is the authority entrusted with application of the law.

Colombia

Regulatory framework

In Colombia, telecommunications are a public service, subject to state regulation and oversight. Law 1341/09 reformed the legal framework, establishing the general regime for information and communication technologies. Under this law, providers of network and telecommunications services in Colombia must register with the Information and Communication Technologies Minister. In addition, operators must obtain a concession from the National Television Commission in order to provide television services.

Law 1341/09 established a transition period in which operators can: (i) preserve the original titles (licenses, contracts, permissions, authorizations) until their expiration or (ii) adopt the regime of general authorization stated by the law and the corresponding registration and preserve the necessary permissions in order to use the spectrum.

During 2009 the Colombian telecommunications regulator, Comisión de Regulación de Comunicaciones or CRC, identified the telecommunications relevant markets and operators with dominant position and established some remedies via ex ante regulations.

Licenses and concessions

Concessions for mobile services in the Eastern Region, the Caribbean Coast Region and the Western Region were granted in March 1994 for a ten-year period and extended for ten years until March 28, 2014. Before 2014 and because of the transition period set forth under Law 1341/2009, Telefónica Móviles Colombia can renounce its concessions, renew the permission for spectrum use for one period of ten years and subsequently renegotiate an extension. If Telefónica Móviles Colombia continues with its current concessions until 2014, in that year it must register as a telecommunications provider and request permission for spectrum use.

Additionally, Telefónica Móviles Colombia holds concessions for carrier services nationwide, granted in June and November 1998 (initially for ten years and extended once for an additional ten years). Due to decree 2870 of 2007, these concessions were transformed into a convergent title. The Ministry of Communications granted Telefónica Móviles Colombia on November 6, 2008 a convergent title to render carrier services for an additional ten-year period (which can be extended for an additional ten years). Like in the case of concessions for mobile services, these licenses are in force until the end of their validity, or Telefónica Móviles can decide to renounce and register as an operator under the general authorization granted by law.

Table of Contents

With respect to fixed line services, Law 1341/2009 preserves the indefinite permission for all operators to operate as local exchange carriers in the national area that Law 142/94 had established. Colombia Telecom must register as a telecommunication provider before the CRC. This registration also covers the general authorization to provide other telecommunications services like long-distance carrier services, value added services, carrier services nationwide and mobile services, among others.

Interconnection

Mobile and fixed operators in Colombia have the right to interconnect to other operators' networks. Before the intervention of regulatory authorities, operators must attempt direct negotiations. Interconnection must assure compliance with the objectives of non-discriminatory treatment, transparency, prices based on costs plus a reasonable profit and promotion of competition.

Prices and tariffs

Mobile tariffs charged to customers are not regulated, although they may not be discriminatory. Nevertheless fixed-to-mobile tariffs are subject to a price cap. Rates are fixed by mobile operating companies and must be registered with the Comisión de Regulación de Telecomunicaciones. The regulator set a price cap of 392 Colombian pesos per minute for fixed to mobile tariffs since November 1, 2006, and in 2009 the CRC reduced the tariff to 198.4 Colombian pesos per minute. Local tariffs are regulated, but operators have the opportunity to offer several alternative plans that are not regulated although they must be registered.

Due to market regulation process, the Telecommunications Commission in December 2008, published a proposed amendment to modify the price cap of 392 to 200 Colombian pesos per minute for fixed to mobile communications. This proposed amendment is currently subject to discussion with operators.

Television services

In January 2007, Colombia Telecom signed a concession agreement with the Television Commission to provide DTH services for ten years. This is a concession granted with a national scope.

In December 2008, the Television Commission published Agreement No. 006. By this disposition the carry obligations of operators of closed television has been modified to require that regional channels be broadcast only in the cover area of the channel and only if it is possible technically.

Competition law

The Colombian Competition Law is incorporated in the Law No. 155/59, Decree No 2153/92 and Law 1340/09 on Restrictive Trade Practices. The law prohibits entering in any agreement or engaging in any type of practice, procedure, or system that aims to limit free competition and abuse of a dominant position. The Superintendent of Industry and Commerce is the Colombian competition authority.

Peru

Regulatory framework

The provision of telecommunications services in Peru is governed by the Telecommunications Law and related regulations.

Licenses and concessions

Telefónica del Perú provides fixed line telecommunications services based on concessions granted by the Ministry of Transportation and Communications, or TMC. The concession term is for 20 years, which may be renewed totally or partially at Telefónica del Perú's request. Total renewal is for an additional 20-year period. Partial renewal is for periods of up to five additional years. Three partial renewals have been approved, extending the concession term until 2027.

Table of Contents

Providers of mobile services seeking to operate in Peru must obtain a non-exclusive license from the TMC. Licenses are granted by means of a license agreement entered into between the TMC and the licensee and set forth the licensee's rights and obligations, including the regions where the licensee is authorized to operate. Licenses are granted either by application or through a bidding process.

Telefónica Móviles Perú has a concession for the provision of mobile services on Sub Band A of the 850 MHz Band and Sub Band of 1900 MHz (in these bands, Telefónica Móviles Perú can also provide fixed wireless services) for a 20-year period, renewable upon request for identical periods. It also holds concessions for offering international and domestic long distance carrier services, granted in February 2002 for a 20-year period. Additionally, it has a concession for the provision of wireless fixed telephony services on the 450 MHz and 900 MHz band for a 20-year period. Both concessions were granted on March 3, 2008. It also holds the concessions for local carrier services, which expire between 2016 and 2022. Concessions for domestic and international carrier services expire on February 5, 2019. In addition, it has a concession for local fixed telephony services for national coverage, granted on August 10, 1999 for a 20 year period. These concessions may be renewed for an additional 20-year period.

Under the concessions to provide mobile services, mobile operators are obligated to meet certain quality service requirements with respect to call failure, radio-electric coverage and quality of communications. These requirements are established on a yearly basis and are gradually increased in order to improve the quality of the service provided.

Prices and tariffs

Tariffs for fixed telephony services must be approved by the National Regulatory Authority, the Organization for Supervision of Private Investment in Telecommunications, or OSIPTEL, in accordance with a price cap formula based on a productivity factor. Rates charged by mobile providers to their customers have been subject to a free tariff regime supervised by OSIPTEL. Tariffs must be reported to OSIPTEL prior to implementation.

Interconnection

Mobile service providers are required, upon request, to interconnect with other concession holders. According to the principles of neutrality and non-discrimination contemplated in the Telecommunications Law, the conditions agreed upon in any interconnection agreement will apply to third parties in the event that those conditions are more beneficial than terms and conditions agreed upon separately.

Competition law

The general competition framework in Peru is based on the Legislative Decree No. 1034. This law prohibits any monopolistic practices, controls, and restraints on free competition and it is applied, in the telecommunication sector, by OSIPTEL.

Ecuador

Regulatory framework

The Special Telecommunications Law and the General Regulation to the Special Telecommunications Law establish the regulatory regime applicable to the provision of telecommunications services in Ecuador.

Licenses and concessions

After a new agreement with the Ecuadorian government, Otecel renewed its mobile telephony services concession which now allows Otecel to provide advanced mobile services, including 3G services. The concession will expire on November 29, 2023 and may be extended for a subsequent 15-year period.

Beside the above mentioned concession, Otecel holds a concession to provide fixed and mobile services carrier services, which expires on April 22, 2017 and may be extended for a subsequent 15-year period. The different licenses for the provision of mobile value added services and Internet mobile access, each of which expires on

Table of Contents

February 21, 2010, are now under the scope of the new agreement with the Ecuadorian government described in the previous paragraph. It also holds a license to provide conventional Internet services, which expires on January 25, 2011 and may be extended for a subsequent ten-year period.

A monthly fee amounting to 1% of the invoiced revenues of mobile services must be paid by all operators holding concessions to the National Secretary of Telecommunications as a contribution to support universal service. Under its contract, Otecel may cancel such fee by giving services to agreed zones within the National Plan for Universal Service.

Prices and tariffs

The mobile services concession of Otecel is subject to a maximum rate of $0.50 per minute for mobile services and a maximum rate of $0.10 per minute for rural public telephony. Otecel may set rates freely so long as it does not exceed these rates, and provided that it notifies the correspondent regulatory body 24 hours ahead of any price increase.

Otecel may set rates freely under its carrier services concession.

Other business lines in Latin America

Country	License/Concession and authorizations	Type of service	Spectrum	Band	Expiration
El Salvador	Concession	Telecommunications services (1)	25 MHz/800 MHz	B Band	2018(2)
	Concession	Telecommunications services (1)	30 MHz/1900 MHz	C Band	2021
Guatemala	Concession	Telecommunications services (1)	80 MHz/1900 MHz	B, C, E and F Bands	2014(3)
	Concession	Telecommunications services (1)			2014(3)
	Concession	Telecommunications services (1)			2014(3)
Nicaragua	Concession	Mobile telecommunications services	800 MHz	A Band	2013(4)
	Concession	Mobile telecommunications services	Additional spectrum 1900	D Band	2013
Panama	Concession	GSM/UMTS	800/1900 Mhz	A Band	2016(5)
Uruguay	License	Mobile telephony	25 MHz 800 MHz		2022-2024(6)

(1) According to the Telecommunications Law all of such concessions were granted to provide any telecommunications services.

(2) Concessions for use of spectrum are granted for a 20-year period and may be renewed for additional 20-year periods upon execution of the proceedings set forth in the Telecommunications Law.

(3) All of such concessions are granted for a 15-year term and may be renewed for subsequent fifteen-year terms at the request of the holder. In order to renew a title, the holder must demonstrate before the regulatory body, that the spectrum was effectively used during the previous 15-year term. All of these titles are set to expire in 2014.

(4) Telefónica Móviles Nicaragua was granted a concession in 1992 for a ten-year period for the use of 25 MHZ of spectrum in the 800 MHz Band A to provide mobile telecommunications services, the regulatory entity granted to Telefónica Nicaragua 10 Mhz of additional spectrum in the 1900 Band D. This concession was renewed for another ten-year period in 1998, and will expire on July 31, 2013. The concession may be renewed for another ten-year period through negotiation with TELCOR two years prior to the expiration of the current concession, subject to the fulfillment of certain terms and conditions by the operator.

(5) The concession period is for 20 years and expires in 2016. This can be extended for another period in accordance with the concession contract. The Panamanian government granted us the right to use 10 MHz (5+5) in the 1900 MHz Band until 2016, which can be extended for another period.

Table of Contents

(6) The expiration date depends on the spectrum concession: band 800 MHz (12.5 MHz + 12.5 MHz) – 20 years from July 2004; band 1900 MHz (5 MHz + 5 MHz) – 20 years from December 2002; and band 1900 MHz (5 MHz + 5 MHz) – 20 years from July 2004.

Seasonality

Our main business is not significantly affected by seasonal trends.

Patents

Our business is not materially dependent upon the ownership of patents, commercial or financial contracts or new manufacturing processes.

C. Organizational Structure

See "—History and Development of the Company" and "—Business Overview."

D. Property, Plant and Equipment

In 2007, we moved to our new central headquarters for the Telefónica Group, "Distrito C", in Las Tablas (Madrid), Spain.

Fixed Networks

We own fixed networks in Spain, Latin America and Europe, having an incumbent role in Spain, Argentina (the greater Buenos Aires metropolitan area and the southern portion of the country), Brazil (São Paulo), Chile, Peru, Colombia and the Czech Republic.

Following market trends, competitive environments, evolution of technologies and new multimedia and broadband services demanded by our customers, we have upgraded our networks in recent years in the following manners:

- progressive introduction of broadband access technologies over copper: ADSL, ADSL2+, VDSL2, etc., increasing the bandwidth capacity provided to our broadband clients several times in the last four years;

- introduction of fiber access technologies (xPON) across different deployment scenarios: fiber to the home (FTTH), fiber to the building (FTTB), fiber to the curb (FTTC), fiber to the node (FTTN), etc., increasing the access speed up to 100 Mbps;

- service support based on powerful Internet Protocol/ Multiprotocol Label Switching (IP/MPLS) backbones, providing full connectivity to the rest of the network layers, such as access and control, to support services for business and customer market segments (fixed and mobile);

- migration of the legacy time division multiplexing (TDM) switching networks (PSTN and ISDN) to new generation network (NGN) over all-IP packet networks;

- migration from legacy transport technologies, such as asynchronous transfer mode (ATM), frame relay (FR), low-rate leased lines , plesiochronous digital hierarchy (PDH) and synchronous digital hierarchy (SDH), to the new generation of optical transport ones, such as dense wavelength division multiplexing (DWDM), coarse wavelength division multiplexing (CWDM) and new generation - synchronous digital hierarchy (NG-SDH);

- introduction of IMS (Internet Multimedia Subsystem) in many countries to simplify the control of the network and ease the deployment of new services over the all-IP converged network;

- empowerment of the intelligence of the network to better manage its use, to avoid saturations and frauds and to identify new business opportunities;

Table of Contents

- convergence of fixed and mobile networks, services and support systems from both technological and operational points of view; and

- deployment of new services such as pay TV, under the Imagenio brand, to customers connected through broadband accesses in Spain, Czech Republic, Peru, Chile, Colombia and Brazil.

Mobile Networks

We operate mobile networks in Spain, the United Kingdom, Germany, Ireland, the Czech Republic, Slovakia, Brazil, Argentina, Venezuela, Chile, Peru, Colombia, Mexico, Guatemala, Panama, El Salvador, Nicaragua, Ecuador and Uruguay. In the case of Brazil (Vivo) the ownership of the networks is shared 50/50 with Portugal Telecom.

We use a number of mobile technologies in the countries in which we operate, namely: GSM and UMTS in Spain, the United Kingdom, Ireland, Germany, Czech Republic, Slovakia and Latin America; CDMA 1X in other countries in Latin America (such as, Brazil, Venezuela and Colombia) and, in the Czech Republic (CDMA 450 Mhz). We continue the work of upgrading our mobile networks in line with market trends, the demand of new services from customers and the evolution of technologies. The main steps we are currently taking include:

- progressive migration from CDMA technologies to GSM or UMTS technologies in markets where we still exploit these legacy technologies;

- introduction of broadband into mobile access using technologies such as UMTS, HSDPA, HSUPA and HSPA+;

- deployment of new services such as mobile television and distribution services for next generation music, video and games;

- exploration of the adequacy of new technologies such as HSPA and LTE (Long Term Evolution) to provide mobile accesses with increased bandwidth, in particular:

- HSPA: we have been committed to the deployment of this technology in countries in which we have a presence and as of December 31, 2009, we have extended our coverage up to the majority of the urban/suburban areas, and we have increased the capacity of the network by upgrading the network technology to the latest available releases of UMTS standards 3GPP REL 6 and REL 7;

- LTE: together with main vendors and sharing experience with other operators, we have extensively analyzed the opportunities LTE will bring as 4G mobile technology is used to complement current network technology by creating higher capacity at lower relative cost by user/traffic unit, and, in this regard, we have deployed the first demonstration trials in 2009, which have been successful so far; and

- convergence of fixed and mobile networks, services and support systems from both technological and operational points of view.

Satellite communications

We hold a 13.23% interest in Hispasat, which leases capacity to Eutelsat, Intelsat, New Sky Satellite and occasionally ArabSat.

The services provided using satellite platforms include television contribution signal to feed cable and IPTV head ends, DTH television, VSAT mainly for telephony and Internet access in rural areas, emergency solutions, corporate communications and international communications with some countries in Africa and in Asia.

Submarine cables

We are one of the world's largest submarine cable operators. We participate in approximately 25 international underwater cable systems (nine of which are moored in Spain) and own eleven domestic fiber optic cables.

Table of Contents

There are submarine cable connections between Spain and Africa, America, Asia and Europe, respectively, that are jointly owned by us with other telecom operators. The SAM-1 cable, which we own, has a length of approximately 22,000 kilometers underwater and 3,000 kilometers terrestrial and links different countries such as the United States, Puerto Rico, Ecuador, Guatemala, Peru, Chile, Brazil, Argentina and Colombia.

The principal services using the capacity of submarine cables are voice circuits, Internet and dedicated circuits for international traffic and for corporations and business customers.

Item 4A. Unresolved Staff Comments

Not applicable.

Item 5. Operating and Financial Review and Prospects

A. Operating Results

Overview

We have implemented a regional, integrated management model based on three business areas, with each area in charge of the fixed and mobile telephone and other businesses within its borders. Our areas are:

- Telefónica Spain: oversees the fixed and mobile telephone, broadband, Internet, pay TV and valued added services and data businesses in Spain.

- Telefónica Europe: oversees the fixed and mobile telephone, broadband, Internet, pay TV and value added services and data businesses in the United Kingdom, Germany, Ireland, the Czech Republic, Slovakia and the Isle of Man.

- Telefónica Latin America: oversees the fixed and mobile telephone, broadband, Internet, pay TV and value added services and data businesses in Latin America.

We are also involved in the media and contact center segments through Telefónica de Contenidos and Atento, respectively.

Presentation of Financial Information

The information in this section should be read in conjunction with our Consolidated Financial Statements and the notes thereto, included elsewhere in this Annual Report. Our Consolidated Financial Statements have been prepared in accordance with IFRS as issued by the IASB.

At its meeting on July 26, 2006, our Board of Directors agreed to restructure the way in which we are managed in order to respond to the increasing convergence of fixed and mobile telephony in the markets in which we operate. In order to adapt to this new environment, we have developed a regional, integrated management model, combining fixed line and mobile telephony services in order to offer customers the best integrated solutions and support in an era of fixed-mobile convergence. We are managed as three business areas: Telefónica Spain, Telefónica Europe and Telefónica Latin America, each of which oversees the integrated fixed and mobile telephone and other businesses in its region. Our three business areas form the basis of our segment reporting in our Consolidated Financial Statements.

Non-GAAP financial information

Operating income before depreciation and amortization

Operating income before depreciation and amortization, or OIBDA, is calculated by excluding depreciation and amortization expenses from our operating income in order to eliminate the impact of generally long-term capital investments that cannot be significantly influenced by our management in the short term. Our management believes that OIBDA is meaningful for investors because it provides an analysis of our operating results and our segment profitability using the same measure used by our management. OIBDA also allows us to compare our results with

Table of Contents

those of other companies in the telecommunications sector without considering their asset structure. We use OIBDA to track our business evolution and establish operational and strategic targets. OIBDA is also a measure commonly reported and widely used by analysts, investors and other interested parties in the telecommunications industry. OIBDA is not an explicit measure of financial performance under IFRS and may not be comparable to other similarly titled measures for other companies. OIBDA should not be considered an alternative to operating income as an indicator of our operating performance, or an alternative to cash flows from operating activities as a measure of our liquidity.

The following table provides a reconciliation of our OIBDA to operating income for the periods indicated.

	Year ended December 31,		
	2007	2008	2009
	(in millions of euros)		
Operating income before depreciation and amortization	22,824	22,919	22,603
Depreciation and amortization expense	(9,436)	(9,046)	(8,956)
Operating income	13,388	13,873	13,647

The following tables provide a reconciliation of OIBDA to operating income for us and each of our business areas for the periods indicated.

	Year ended December 31, 2009				
	Telefónica Spain	Telefónica Latin America	Telefónica Europe	Others and Eliminations	Total
	(in millions of euros)				
Operating income before depreciation and amortization	9,757	9,143	3,910	(207)	22,603
Depreciation and amortization expense	(2,140)	(3,793)	(2,895)	(128)	(8,956)
Operating income	7,617	5,350	1,015	(335)	13,647

	Year ended December 31, 2008				
	Telefónica Spain	Telefónica Latin America	Telefónica Europe	Others and Eliminations	Total
	(in millions of euros)				
Operating income before depreciation and amortization	10,285	8,445	4,180	9	22,919
Depreciation and amortization expense	(2,239)	(3,645)	(3,035)	(127)	(9,046)
Operating income	8,046	4,800	1,145	(118)	13,873

	Year ended December 31, 2007				
	Telefónica Spain	Telefónica Latin America	Telefónica Europe	Others and Eliminations	Total
	(in millions of euros)				
Operating income before depreciation and amortization	9,448	7,121	4,977	1,278	22,824
Depreciation and amortization expense	(2,381)	(3,559)	(3,386)	(110)	(9,436)
Operating income	7,067	3,562	1,591	1,168	13,388

Net financial debt and net debt

We calculate net financial debt by deducting the positive mark-to-market value of derivatives with a maturity beyond one year from the relevant balance sheet date and other interest-bearing assets (each of which are components of non-current financial assets in our consolidated statement of financial position), current financial assets and cash and cash equivalents from the sum of (i) current and non-current interest-bearing debt (which includes the negative mark-to-market value of derivatives with a maturity beyond one year) and (ii) other payables (a component of non-current trade and other payables in our consolidated statement of financial position). We calculate net debt by adding to net financial debt those commitments related to financial guarantees, not considered

Table of Contents

as net financial debt, and those related to workforce reduction. We believe that net financial debt and net debt are meaningful for investors because they provide an analysis of our solvency using the same measures used by our management. We use net financial debt and net debt to calculate internally certain solvency and leverage ratios used by management. Neither net debt nor net financial debt as calculated by us should be considered an alternative to gross financial debt (the sum of current and non-current interest-bearing debt) as a measure of our liquidity.

The following table provides a reconciliation of our net financial debt and net debt to gross financial debt at the dates indicated:

	As of December 31,		
	2007	2008	2009
	(in millions of euros)		
Non-current interest-bearing debt	46,942	45,088	47,607
Current interest-bearing debt	6,986	8,100	9,184
Gross financial debt	53,928	53,188	56,791
Other payables	327	477	515
Non-current financial assets(1)	(2,284)	(4,439)	(2,736)
Current financial assets	(1,622)	(2,216)	(1,906)
Cash and cash equivalents	(5,065)	(4,277)	(9,113)
Net financial debt	45,284	42,733	43,551
Commitments related to financial guarantees	365	365	71
Net commitments related to workforce reduction	3,289	2,687	2,261
Net debt	48,938	45,785	45,883

(1) Positive mark-to-market value of derivatives with a maturity beyond one year from the relevant statement of financial position date and other interest-bearing assets.

Significant Factors Affecting the Comparability of our Results of Operations in the Periods Under Review

During the years ended December 31, 2007, 2008 and 2009, various changes occurred in our composition that affect the comparability of our operating results between the periods. See Appendix I to our Consolidated Financial Statements for a detailed description of the principal changes in our composition affecting our financial statements during the periods under review covered by our Consolidated Financial Statements. The most significant factors affecting the comparability of our results of operations in the periods under review are discussed below.

Classification of Venezuela as a hyperinflationary economy

Throughout 2009 and in the early part of 2010, a number of factors arose in the Venezuelan economy that led us to reconsider the treatments we follow with the respect to the translation of the financial statements of our investees, as well as the recovery of our financial investments in that country. Within these factors it is worth highlighting the level of inflation reached in 2009 and the cumulative inflation over the last three years, the restrictions to the official foreign exchange market and, finally, the devaluation of the Bolivar fuerte on January 8, 2010.

Table of Contents

As a result, in accordance with IFRS Venezuela must be considered a hyperinflationary economy in 2009. The main implications of this are as follows:

- The 2008 figures should not be restated.

- Adjustment of the historical cost of non-monetary assets and liabilities and the various items of equity of Venezuelan companies from the date of acquisition or inclusion in Telefónica's consolidated statement of financial position to the end of the year to reflect the changes in purchasing power of the currency caused by inflation.

The cumulative impact of the accounting restatement to adjust for the effects of hyperinflation for years prior to 2009 is reflected in the translation differences at the beginning of the 2009 financial year.

- Adjustment of the income statement to reflect the financial loss caused by the impact of inflation in the year on net monetary assets (loss of purchasing power).

- The various components in the income statement and statement of cash flows have been adjusted for the inflation index since their generation, with a balancing entry in net financial results and a reconciling item in the statement of cash flows, respectively.

- All components of the financial statements of the Venezuelan companies have been translated at the closing exchange rate, which at December 31, 2009 was 2.15 Bolivar fuerte per dollar (3.1 Bolivar fuerte per euro).

The main effects on the Telefónica Group's consolidated financial statements for 2009 derived from the items mentioned above are as follows:

	Million of euros
Revenue	267
Operating income excluding the impact of depreciation and amortization cost	64
Net profit	(548)
Translation differences	1,224
Impact on equity	676

Regarding the devaluation of the Venezuelan Bolivar fuerte on January 8, 2010 (see Note 2 to our Consolidated Financial Statements), the two main factors to consider with respect to the Telefónica Group's 2010 financial statements will be:

- The decrease in the Telefónica Group's net assets in Venezuela as a result of the new exchange rate, with a balancing entry in equity of the Group. This effect is estimated at approximately €1,810 million.

- The translation of results and cash flows from Venezuela at the new devalued closing exchange rate.

Finally, on January 19, 2010, the Venezuelan Authorities announced that they would grant a preferential rate of 2.60 Bolivar fuerte per dollar for new items, among which payment of dividends is included, as long as the request for Authorization of Acquisition of Foreign Exchange was filed before January 8, 2010. To that date, we had in fact requested authorizations related to the distribution of dividends of prior years (see Note 16 to our Consolidated Financial Statements).

Tax amortization of goodwill

In December 2007, the European Commission opened an investigation involving the Kingdom of Spain relating to the potential consideration of the deduction for tax amortization of financial goodwill arising on certain foreign shareholding acquisitions as government aid under the provisions of article 12.5 of the revised Spanish Income Tax Law ("TRLIS"). This investigation led to widespread uncertainties regarding the effect any decision by the European Commission would have on, among others, the Telefónica Group.

Table of Contents

In the case of the Telefónica Group, as a result of this uncertainty we deemed it necessary to recognize a liability as the deduction had been applied in the consolidated financial statements pending completion of the investigation.

In December 2009, the European Commission released its decision regarding the investigation, deeming the deduction as state aid. However, this decision does not affect investments made before December 21, 2007, which is the case with the investments made by the Telefónica Group in companies such as O2, Bellsouth's Latin America operators, Colombia Telecomunicaciones, S.A. ESP and Cesky Telecom. As a result of this decision, and considering the corporate structure of these investments, income tax in our consolidated income statement for the year ended December 31, 2009 is €591 million lower due to the reversal of this liability.

Share exchange between Telefónica, S.A. and China Unicom Limited, and signing of strategic alliance.

On October 21, 2009, pursuant to our previously described strategic alliance agreement with China Unicom, we exchanged 40,730,735 of our shares for 693,912,264 newly issued shares of China Unicom. As a result of this exchange, our voting interest in the share capital of China Unicom increased from 5.38% to 8.06%, and China Unicom has a 0.87% voting interest in our share capital at that date. As of the date of this Annual Report, and after the capital reduction carried out by China Unicom, we hold shares representing 8.37% of China Unicom's voting share capital and the right to appoint a member to its board of directors.

As a result, our investment in China Unicom is now accounted for using the equity method. The cumulative amount of this investment at December 31, 2009 was €2,301 million.

Tender offer for all the remaining outstanding shares of Compañía de Telecomunicaciones de Chile, S.A.

On September 17, 2008, we launched a tender offer through our subsidiary Telefónica Internacional to acquire all the outstanding shares of CTC that we did not already control directly or indirectly, amounting to 55.1% of CTC's share capital.

Once the acceptance period had ended and the transaction had been settled on October 30, 2008 our indirect ownership in CTC increased from 44.9% to 96.75%. This is the percentage that appears as the percentage of ownership as of December 31, 2008 in the accompanying Consolidated Financial Statements.

Subsequently, pursuant to Chilean law, on December 1, 2008, Telefónica Internacional launched a new tender offer for all the shares of CTC that it did not own directly or indirectly after settlement of the first offer, on the same economic terms. The acceptance period for the second offer ended December 31, 2008, but was then extended to January 6, 2009, as allowed by Chilean law.

Upon the end of the acceptance period of the second tender offer, our indirect ownership percentage in CTC's share capital had increased from 96.75% of all CTC's outstanding shares, as reached in the first tender offer, to 97.89%. The total payment for the two tranches was 558.55 million Chilean pesos, equivalent to approximately €658 million.

Sale of shareholding in Airwave O2, Ltd.

In April 2007, Telefónica O2 Europe, Plc, our wholly-owned subsidiary, sold 100% of the share capital of the UK company, Airwave O2, Ltd, for £1,932 million (equivalent to €2,841 million at the transaction date). The sale produced a gain of €1,296 million, recognized under "Other income" in our consolidated income statement for 2007. See Note 19 to our Consolidated Financial Statements.

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

In May 2007, we signed an agreement to sell our 99.7% stake in the Dutch company Endemol Investment Holding, B.V. to a consortium owned by Mediacinco Cartera, S.L., Cyrte Fond II, B.V. and G.S. Capital Partners VI Fund, L.P, for €2,629 million. The transaction was completed on July 3, 2007, producing a gain of €1,368 million, recognized under "Other income" in our consolidated income statement for 2007. See Note 19 to our Consolidated Financial Statements.

Acquisition of indirect shareholding in Telecom Italia

On April 28, 2007, we, together with our partners Assicurazioni Generali, S.p.A., Intesa Sanpaolo, S.p.A., Mediobanca, S.p.A. and Sintonía, S.A., entered into a co-investment agreement and shareholders' agreement which established the terms and conditions of our acquisition of an indirect shareholding in Telecom Italia through an Italian company, Telco, in which we have 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 acquired 100% of Olimpia, S.p.A., which held 18% of the voting shares of Telecom Italia. 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 Lebenversicherung A.G. and Generali Vie S.A.) and Mediobanca S.p.A. contributed an aggregate of 5.6% of Telecom Italia's voting shares to Telco.

On December 10, 2007, an agreement was reached to merge Olimpia, S.p.A. into Telco, as a result of which Telco's entire stake in the voting shares of Telecom Italia (23.6%) became a direct stake.

In March 2008, Telco acquired an additional 121.5 million shares of Telecom Italia (representing 0.9% of its share capital), bringing its ownership to 24.5% of the voting rights and 16.9% of the dividend rights. As a result, we indirectly hold 10.49% of Telecom Italia voting rights and 7.21% of its dividend rights. We account for our investment in Telco using the equity method.

On December 22, 2009, Telco and Sintonia completed (i) the acquisition in cash by Sintonia of the Telecom Italia shares held by Telco attributable to it on a pro rata basis (approximately 275.1 million Telecom Italia ordinary shares, equal to 2.06% of the ordinary share capital) at a price of €2.2 per share, a total purchase price of approximately €605 million; and (ii) the acquisition by Telco of Sintonia's entire shareholding in Telco (approximately 162.8 million class A shares, equal to 8.39% of Telco's share capital). For additional information on this acquisition see Note 2 to our Consolidated Financial Statements and "Item 10. Additional Information—Material Contracts".

Significant Changes in Accounting Policies

The accounting policies applied in the preparation of our consolidated annual financial statements as of and for the year ended December 31, 2009 are consistent with those used in the preparation of our consolidated annual financial statements as of and for the year ended December 31, 2008, except for the adoption of new standards, amendments to standards and interpretations published by the International Accounting Standards Board (IASB) and the IFRIC (International Financial Reporting Interpretations Committee), effective as of January 1, 2009, noted below.

Amendment to IAS 23: Borrowing Costs

The amendment consists of the elimination of the possibility to immediately recognize in profit or loss the borrowing costs related to the production or development of qualifying assets. This amendment has had no impact on the accounting policies applied by us.

Amendment to IAS 1: Presentation of Financial Statements: A Revised Presentation

The revised standard separates owner from non-owner changes in equity. The statement of changes in equity includes only details of transactions with owners, with non-owner changes presented as a single line item. In addition, the standard introduces the "statement of comprehensive income", which can be presented in one single statement or in two linked statements. We elected to present two statements. This change is not mandatory, but we have decided to use the proposed titles, which are:

- “statement of financial position”, instead of “balance sheet”
- income statement

86

Table of Contents

- "statement of comprehensive income", instead of "statement of recognized income and expense"
- "statement of changes in equity" instead of "movements in equity"
- "statement of cash flows" instead of "cash flow statement"

Amendment to IFRS 2: Share-based Payment: Vesting Conditions and Cancellations

This amendment clarifies the definition of vesting conditions and prescribes the accounting treatment of an award that is cancelled because a non-vesting condition is not met. The adoption of this amendment did not have any impact on our financial position or performance.

Amendments to IAS 32 and IAS 1: Presentation of Financial Statements — Puttable Financial Instruments and Obligations Arising on Liquidation

These amendments include a limited scope exemption for puttable financial instruments to be classified as equity if they fulfill specified criteria. The adoption of these amendments did not have any impact on our financial position or performance.

Improvements to IFRSs (issued by the IASB in May 2008)

These improvements establish a broad range of amendments to current IFRSs with the primary aim of removing inconsistencies and clarifying wording. These amendments have not had any impact on our financial position or performance.

Amendments to IFRS 7: Financial Instruments: Disclosures

This amendment enhances the disclosures required about fair value measurements and liquidity risk. The amendment requires the classification of fair value measurements using a three-level hierarchy that reflects the significance of the inputs used in making the measurement, as well as the disclosure of any eventual change in valuation techniques and the reasons for making such change. These amendments have not had any impact on our financial position or performance.

Amendments to IFRIC 9 and IAS 39: Embedded derivatives

These amendments clarify the impact that a reclassification of a financial asset out of the fair value through profit or loss category has on the assessment of whether an embedded derivative shall be separated from its host contract. Additionally, it prohibits the reclassification when the embedded derivative is not subject to a separate valuation upon the moment of reclassification of a hybrid contract out of the aforementioned category. These amendments have not had any impact on our financial position or performance.

IFRIC 12: Service Concession Arrangements

This interpretation provides guidance on the accounting by operators for obligations assumed and related rights acquired under service concession arrangements. The adoption of this interpretation did not have any impact on our financial position or performance.

IFRIC 13: Customer Loyalty Programs

This interpretation establishes that entities that have programs which award points or credits to their customers as the result of a commercial transaction, which in the future will be redeemed for free or discounted products or services, must treat these points as part of the commercial transaction that generates them. In other words, it is a transaction with multiple components, comprising the sale of the product or service itself and the sale of points or credits, therefore such that a part of the amount earned must be allocated to the points awarded and its recognition deferred until their redemption. The portion corresponding to the points will be determined by reference to their fair value. The adoption of this interpretation did not have a significant impact on our financial position or performance.

Table of Contents

IFRIC 15: Agreements for the Construction of Real Estate

This interpretation refers to agreements for the construction of real estate and addresses two related issues: (i) whether the construction of real estate is within the scope of IAS 11, Construction Contracts, or IAS 18, Revenue and (ii) when revenue from the construction of real estate should be recognized. The adoption of this interpretation did not have any impact on our financial position or performance.

IFRIC 16: Hedges of a Net Investment in a Foreign Operation

This interpretation establishes the criteria for the recognition of hedges of a net investment in foreign operations, including the foreign currency risks that qualify for hedge accounting in the hedge of a net investment, where within the group the hedging instruments can be held and how an entity should determine the amount of foreign currency gain or loss relating to both the hedging instrument and the hedged item that must be recognized in profit or loss on disposal of the investment. The adoption of this interpretation did not have any impact on our financial position or performance.

IFRIC 18: Transfers of Assets from Customers

This interpretation applies to deliveries of assets from customers as of July 1, 2009. This interpretation establishes the criteria for accounting for transactions in which an entity receives from a customer an item of property, plant and equipment (or cash for their acquisition or construction) that the entity must use either to connect the customer to a network and/or to provide the customer with ongoing access to a supply of goods or services. The adoption of this interpretation did not have any impact on our financial position or performance.

In addition to this, an amendment to IAS 39 concerning intersegment hedge accounting included in the Improvements to IFRSs issued by the IASB in April 2009 is effective for annual periods beginning on or after January 1, 2009, but is not endorsed by the European Union as of the date of publication of these consolidated financial statements. This amendment clarifies that hedge accounting not be applied to transactions between segments in accordance with the principle in IAS 39, which does not allow hedge of intragroup transactions in the consolidated financial statements. The application of this amendment would not have had any impact on the 2009 consolidated financial statements.

Finally, the following IFRS and IFRIC interpretations were issued but not effective at the date of preparation of our Consolidated Financial Statements:

Standards and amendments		Mandatory application: annual periods beginning on or after
IFRS 9	Financial Instruments	January 1, 2013
Revised IFRS 3	Business Combinations	July 1, 2009
Amendment to IAS 27	Consolidated and Separate Financial Statements	July 1, 2009
Improvements to IFRS (April 2009)		January 1, 2010 (*)
Revised IAS 24	Related Party Disclosures	January 1, 2011
Amendments to IAS 39	Eligible Hedged Items	July 1, 2009
Amendment to IFRS 2	Group Cash settled Share-based Payments	January 1, 2010
Amendment to IFRS 1		January 1, 2010

	Additional Exemptions for First-time adopters	
Amendments to IAS 32	Classification of Rights Issues	February 1, 2010

(*) The amendments to IFRS 2, IAS 38 (relating to intangible assets acquired in business combinations) IFRIC 9 and IFRIC 16 are effective for all fiscal years beginning July 1, 2009. There is no mandatory application date for the additional guidance to the appendix of IAS 18 on the determination of agent/principal because this appendix is not part of the standard.

Interpretations		Mandatory application: annual periods beginning on or after
IFRIC 17	Distributions of Non-cash Assets to Owners	July 1, 2009
IFRIC 19	Extinguishing Financial Liabilities with Equity Instruments	July 1, 2010
Amendment to IFRIC 14	The limit of a Defined Benefit Asset, Minimum Funding Requirement and their Interaction	January 1, 2011

Table of Contents

We are currently assessing the impact of the application of these standards, amendments and interpretations. From the analyses made, we estimate that their adoption will not have a significant impact on our consolidated financial statements in the initial period of application. However, the changes introduced by the revised IFRS 3 and amendments to IAS 27 will affect future acquisitions and transactions with non-controlling interests carried out on or after January 1, 2010. The changes introduced by IFRS 9 will affect financial assets and future transactions with financial assets carried out on or after January 1, 2013.

Critical Accounting Policies and Estimates

The preparation of financial statements in conformity with IFRS requires management to make estimates and assumptions that affect the amounts reflected in the Consolidated Financial Statements and accompanying notes. We base our estimates on historical experience, where applicable, and other assumptions that we believe are reasonable under the circumstances. Actual results may differ from those estimates under different assumptions or conditions.

We consider an accounting estimate to be critical if:

- it requires us to make assumptions because information was not available at the time or it included matters that were highly uncertain at the time we were making our estimate; and

- changes in the estimate or different estimates that we could have selected may have had a material impact on our financial condition or results of operations.

The various policies that are important to the portrayal of our financial condition, results of operations and cash flows include:

- accounting for long-lived assets, including goodwill;
- deferred taxes;
- provisions; and
- revenue recognition.

Accounting for long-lived assets, including goodwill

Property, plant and equipment and intangible assets, other than goodwill, are recorded at acquisition cost. If such assets are acquired in a business combination, the acquisition cost is the estimated fair value of the acquired property, plant and equipment or intangible assets. Property, plant and equipment and intangible assets with definite useful lives are depreciated or amortized on a straight-line basis over their estimated useful lives.

Intangible assets with indefinite useful lives are not amortized, but are, instead, subject to an impairment test on a yearly basis and whenever there is an indication that such assets may be impaired.

Accounting for long-lived assets and intangible assets involves the use of estimates for determining: (a) the fair value at the acquisition date in the case of such assets acquired in a business combination, and (b) the useful lives of the assets over which they are to be depreciated or amortized. We believe that the estimates we make to determine an asset's useful life are "critical accounting estimates" because they require our management to make estimates about technological evolution and competitive uses of assets.

When an impairment in the carrying amount of an asset occurs, non-scheduled write-downs are made. We perform impairment tests of identifiable intangible and long-lived assets whenever there is reason to believe that the carrying value may exceed the recoverable amount, which is the higher of the asset's fair value less costs to sell and its value in use. Furthermore, previously recognized impairment losses may be reversed when changes in the estimates used to determine the asset's recoverable amount indicate that an impairment loss recognized in prior periods no longer exists or may have decreased.

Table of Contents

The determination of whether the impairment of long-lived and intangible assets is necessary involves the use of significant estimates and judgment that includes, but is not limited to, the analysis of the cause of potential impairment in value, the timing of such potential impairment and an estimate of the amount of the impairment, which requires the estimation of the future expected cash flows, discount rates and the fair value of the assets.

Specifically, management has to make certain assumptions in respect of uncertain matters, such as growth in revenues, changes in market prices, operating margins, and technology developments and obsolescence, discontinuance of services and other changes in circumstances that indicate the need to perform an impairment test. Management's estimates about technology and its future development require significant judgment because the timing and nature of technological advances are difficult to predict.

Goodwill arises when the cost of a business combination exceeds the acquirer's interest in the net fair value of the identifiable assets acquired and liabilities and contingent liabilities assumed. Goodwill is not amortized, but is, instead, subject to an impairment test on a yearly basis and whenever there is an indication that the goodwill may be impaired.

Non-scheduled write-downs of goodwill are made when an impairment in the carrying amount of goodwill occurs. We review, on a regular basis, the performance of our cash-generating units. We compare the carrying amount of the cash-generating unit to which the goodwill has been allocated with its recoverable amount. The determination of the recoverable amount of the cash-generating unit involves extensive use of estimates and significant management judgment is involved. Methods commonly used by us for valuations include discounted cash flow methods.

A significant change in the facts and circumstances that we relied upon in making our estimates may have a material impact on our operating results and financial condition.

Deferred taxes

Management assesses the recoverability of deferred tax assets on the basis of estimates of our future taxable profit. The recoverability of deferred tax assets ultimately depends on our ability to generate sufficient taxable profit during the periods in which the deferred tax assets are utilized. In making this assessment, our management considers the scheduled reversal of deferred tax liabilities, projected taxable profit and tax planning strategies.

This assessment is carried out on the basis of internal projections, which are updated to reflect our most recent operating trends. In accordance with applicable accounting standards, a deferred tax asset must be recognized for all deductible temporary differences and for the carry-forward of unused tax credits and unused tax losses to the extent that it is probable that taxable profit will be available against which the deductible temporary difference can be utilized. Our current and deferred income taxes are impacted by events and transactions arising in the normal course of business as well as in connection with special and non-recurring items. Assessment of the appropriate amount and classification of income taxes is dependent on several factors, including estimates of the timing and realization of deferred tax assets and the timing of income tax payments. Actual collections and payments may materially differ from these estimates as a result of changes in tax laws as well as unanticipated future transactions impacting our income tax balances.

Provisions

Provisions are recorded when, at the end of the period, we have a present obligation as a result of past events, whose settlement requires an outflow of resources that is considered probable and can be measured reliably. This obligation may be legal or constructive, arising from, but not limited to, regulation, contracts, common practice or public commitments, which have created a valid expectation for third parties that we will assume certain responsibilities. The amount recorded is the best estimation performed by the management in respect of the expenditure that will be required to settle the obligations, considering all the information available at the closing date, including the advice of external experts, such as legal advisors or consultants.

If we are unable to reliably measure the obligation, no provision is recorded and information is then presented in the notes to the Consolidated Financial Statements.

Table of Contents

Because of the inherent uncertainties in this estimation, actual expenditures may be different from the originally estimated amount recognized.

Revenue recognition

Connection fees

Revenues from connection fees originated when customers connect to our network are deferred over the average expected length of the customer relationship.

The expected customer relationship period is estimated based on recent historical experience of customer churn rates. Significant changes in our estimations may result in differences in the amount and timing of revenues recognized.

Multiple-element arrangements

Arrangements involving the delivery of bundled products or services are assessed to determine whether it is necessary to separate the arrangement into individual component deliverables, each with its own revenue recognition criteria.

Revenue relating to the bundled contract is allocated to the different deliverables identified, based on their relative fair values (i.e., the fair value of each individual component deliverables in relation to the total fair value of the bundled deliverables). Given that the handsets and airtime are price-sensitive and volatile in a competitive marketplace, the determination of fair values in the mobile phone business is quite complex.

Additionally, a significant change in the facts and circumstances upon which we based our fair value estimates may have an impact on the allocation of revenue among the different deliverables identified and, consequently, on future revenues.

Operating Environment

Our results of operations are dependent, to a large extent, on the level of demand for our services in the countries in which we operate. Demand for services in those countries is affected by the performance of their respective economies, including changes in gross domestic product, or GDP, inflation, or CPI, external accounts and unemployment rates.

Operating environment by country

Spain

In 2009, Spanish GDP contracted by 3.6%, compared with a positive average annual growth rate of 3.6% in the period 1998 through 2008. This slowdown was explained by a strong deceleration of internal demand, both household consumption which contracted at an annual rate of 5.0% during 2009 compared to average growth of 3.3% during the period 1998 through 2008, and investment which contracted at an annual rate of 15.0% in 2009 compared to average annual growth of 3.4% during the period 1998 through 2008. Inflation averaged -0.3% in 2009, compared with 4.1% in 2008 and 2.8% in 2007. Despite the lower average annual inflation rate, prices in 2009 experienced a high degree of volatility through the year, reaching a minimum of -1.4% in July and increasing up to 0.8% by the end of the year. The current account deficit for 2009 reached 5.6% of GDP, almost half the percentage in the prior two years (9.5% of GDP in 2008 and 10.0% in 2007). This improvement was mostly explained by the trade balance (imports fell significantly more than exports due to the sharp slowdown in domestic demand). The unemployment rate reached

18.8% at the end of the year, notably higher than the average rate of 13.9% in 2008 and 8.6% in 2007. The increase in the unemployment rate was mostly explained by the poor employment performance during 2009; 1.2 million jobs were lost, twice the number of 2008 (619,000) and a reversal from 2007 when 475,000 jobs were created in Spain.

Table of Contents

United Kingdom

In 2009, the British economy, measured in terms of GDP, contracted by 4.8%, compared with a positive growth rate of 0.6% in 2008 and 2.6% in 2007. A sharp slowdown in domestic demand in 2009 explained the negative GDP growth. In addition, during 2009, fixed capital investment contracted at an annual rate of 14.6%, compared to a contraction of 3.5% in 2008 and growth of 7.9% in 2007. Private consumption deteriorated less severely, falling at an annual rate of 3.1% in 2009, compared with a positive annual growth rate of 0.9% in 2008 and 2.1% in 2007. The CPI increased by an average annual growth rate of 2.2% in 2009, compared with 3.6% in 2008 and 2.3% in 2007. The deceleration in the rate of average annual CPI growth was partially explained a temporary VAT reduction of 2.5 percentage points (from 17.5% to 15.0%) and worsening consumer demand. During the first ten months of 2009, employment decreased at an annual rate of 1.6%, compared to an annual increase of 0.7% in both 2008 and 2007 (Labor Force Survey). As a result, the unemployment rate reached 7.8% in December 2009, compared to an average annual rate of 5.7% in 2008 and 5.3% in 2007.

Germany

In 2009, the German economy contracted 5.0%, after growing 1.3% in 2008 and 2.5% in 2007. This significant slowdown was due to a contraction in fixed income investment of 8.6% in 2009, and the negative contribution of the external sector to GDP growth (exports decreased 14.6% while imports contracted just 8.9%). Because of this, the current account balance declined to 4.2% of GDP in 2009, from 6.6% of GDP in 2008 and 8.0% of GDP in 2007. Inflation averaged 0.3% in 2009, which was significantly less than the average in 2008 and 2007 (2.6% and 2.3%, respectively) At the end of 2009, inflation stood at 0.8%. During 2009, the unemployment rate stood at 8.2%, slightly higher than the rate in 2008 (7.8%) but not reaching 2007 levels (9.0%). However, in 2009, 186,000 jobs were lost, compared to a positive job creation of 296,000 in 2008 and 591,000 in 2007.

Czech Republic

The Czech economy contracted by 4.1% in 2009 as opposed to growth of 2.5% in 2008 and 6.1% in 2007. Internal demand in 2009 underperformed with respect to previous years mainly due to investment, which decreased by 8.3% in 2009 compared to a decrease of 1.5% in 2008 and growth of 10.8% in 2007. Household consumption contracted 0.1% in 2009, compared to growth of 3.5% and 4.9% in 2008 and 2007, respectively. Inflation, as measured by the CPI, grew 1% in December 2009 compared to December 2008, well below the Central Bank objective (2%) and well below the 6.3% and 2.9% levels reached in 2008 and 2007, respectively. The current account had a €1.5 billion deficit for 2009, higher than the €1 billion deficit recorded in 2008 but lower than the €4 billion deficit of 2007. However, net foreign direct investment was clearly lower than in past years. During 2009, net foreign direct investment decreased 35% with respect to 2008 (€1 billion in 2009 compared to €1.5 million in 2008). The increase in global risk aversion negatively affected the Czech crown, with the average Czech crown to euro exchange rate for 2009 depreciating by 6% against the euro in 2009, contrasting with a 10.1% appreciation in 2008 and 2.1% in 2007.

Brazil

Brazil's 2009 GDP was negatively affected by the economic downturn, which began in the last quarter of 2008. As expected by economic forecasters surveyed by Focus Economics, positive quarterly growth in GDP since the second quarter of 2009 did not compensate for the contraction in the previous quarters. As a result, Brazilian GDP decreased 0.2% in 2009, after posting growth of 5.1% in 2008 and 6.1% in 2007. The same forecasters expect the expansion of private consumption in 2009 to be 3.0%, less then half of the 7.0% growth rate reached in 2008 and the 6.3% recorded in 2007. Investment decreased by 9.9% in 2009, after rising by 13.4% in the previous year and 13.9% in 2007. Inflation, as measured by the CPI, slowed down to an increase of 4.3% in 2009, below the inflation target established by the Central Bank, of 4.5%, and lower than the 5.9% posted in 2008 and 4.5% in 2007. Due to the deceleration of economic activity and inflation, the basic interest rate, the SELIC, was reduced from 13.75% to 8.75%. The current account deficit reached $24.3 billion in 2009, compared to $28.2 billion in 2008 and a surplus of $1.6 billion in 2007. This deficit in 2009 was financed by capital inflows, such as foreign direct investments of $25.9 billion and portfolio investments of $46.7 billion. As a consequence, international reserves rose by $32.2 billion in 2009, to a record level of $239.1 billion. The improvement in domestic economic data, along with increased liquidity in the international capital markets, led to a decrease in country risk. The J.P. Morgan Emerging

Table of Contents

Markets Bond Index Plus (EMBI + Brazil) ended 2009 at 197 basis points, from 428 basis points at the end of 2008 and 221 basis points at the end of 2007. As the risk reduced and capital inflows gained strength, the exchange rate restarted its appreciation trend, as observed since 2004. The Brazilian real appreciated against the U.S. dollar by 25.6% in 2009, reaching an exchange rate of R$1.74/ $1.00 on December 31, 2009, from R$2.34 per $1.00 by the end of 2008 and R$1.77 per $1.00 at the end of 2007.

Mexico

Mexico's real GDP shrank 6.5% in 2009 compared to a previous growth of 1.4% in 2008 and 3.3% in 2007. Inflation, as measured by the CPI, grew 3.6% in December 2009 compared to December 2008, slightly above the central bank's target of 3% but within its tolerance range of 2% to 4%. Inflation was highly reduced with respect to 2008 (6.5% growth in December 2008 with respect to December 2007) due to a fall in agricultural prices and to the introduction of fuel subsidies by the government during 2009. Mexico has been the country with the most severe contraction in Latin America, suffering from its high exposure to the U.S. economy and from the swine flu epidemic that reduced tourism and the already declining capital inflows. However, this recession differs from previous ones in that Mexico has been better prepared, having sound macroeconomic fundamentals including a solvent fiscal position, a floating exchange rate system and an independent central bank committed to price stability. Moreover, the lines provided by the U.S. Federal Reserve and the International Monetary Fund, or IMF, contributed to greater financial resilience. Despite the harsh economic downturn, the second half of 2009 was promising. The Mexican economy, in terms of GDP, grew 2.9% quarter-on-quarter during the third quarter of 2009 and 2.0% quarter-on-quarter during the fourth quarter of 2009. The trade balance posted a deficit of $4.7 billion, $12.9 billion lower than in 2008 due to a higher fall in imports as a consequence of the internal demand collapse. These external imbalances were well financed by capital inflows, which grew in the last quarter, and international reserves held by the central bank reached a new record of $90.9 billion in 2009 (amounting to 10.2% of GDP). The exchange rate relative to the U.S. dollar reached a maximum in March 2009 of 15.56 Mexican pesos to the U.S. dollar, a level never seen before. However, from that moment the exchange rate relative to the U.S. dollar appreciated. It closed at 13.06 Mexican pesos to the U.S. dollar at the end of 2009, 4.3% more compared to the end of 2008 but 20% less with respect to the end of 2007.

Venezuela

The Venezuelan economy reversed from the positive results demonstrated during the previous five years. In 2009, GDP contracted approximately 3.3% as a result of lower oil prices in the first part of the year and high inflation. Both factors had a negative impact on private consumption, which decreased by 3.2% in 2009, compared to growth of 7.1% in 2008 and 18.7% in 2007. The rest of the components of aggregate demand, also slowed markedly below the figures recorded in 2008 and 2007. In 2009, investment dropped 20.0% (growth of 2.5% in 2008 and 23.0% in 2007), public consumption grew 2.3% (growth of 6.7% in 2008 and 6.1% in 2007), exports fell 12.9% (decreases of -2.7% in 2008 and -7.0% in 2007), and imports faced dramatic contraction of 19.6% (growth of 3.8% in 2008 and 29.9% in 2007). In terms of inflation, the national CPI rose to 25.1% in 2009, which represents a lower figure in comparison with 30.9% in 2008 and 22.5% in 2007 (The national CPI was created in 2008 and because of that, 2007 variation corresponded to Caracas CPI); however, Venezuela continues with the highest levels of inflation in Latin America. The unemployment rate reached 6.6% at the end of 2009, which was higher than the 6.1% observed in December 2008 and 6.2% in December 2007, because of the fall in economic activity. The external accounts suffered a negative impact as a result of lower oil prices, with the current account surplus decreasing to $8.6 billion in 2009, in comparison with $37.4 billion in 2008 and $18.1 billion in 2007. On the other side, the capital account deficit reached $14.0 billion, which was lower than the deficit in 2008 ($24.8 billion) and 2007 ($22.1 billion). This performance generated a reduction in the central bank's stock of international reserves to $35.0 billion at the end of 2009. Finally, the parallel exchange rate was 2.8 times over the official exchange rate, as a result of the reduction imposed by CADIVI (the Venezuelan Commission for Currency Administration) on hard currency disbursements during the year.

Chile

Due to the international financial crisis, the Chilean economy, in terms of GDP, contracted by an estimated 1.7% in 2009 compared to growth of 3.1% and 4.7% in 2008 and 2007, respectively. This contraction in 2009 is explained by a 6.8% decrease in domestic demand, mainly caused by a 16.4% decrease in investment and an historical reduction in inventories. Employment contracted by an average of 0.7% in 2009 resulting in an average unemployment rate of 9.7% (with a peak of 10.8% in the first half of the year) compared to 7.7% and 7.0% in 2008 and 2007, respectively. In the worst phase of the recession, economic activity plunged 5.1% year-on-year in April 2009. A $4 billion (2.8% of GDP) stimulus program that included temporary tax cuts, cash bonuses, and employment subsidies was implemented by fiscal authorities to avoid a further decline. The Chilean central bank, on its side, cut its monetary rate by 775 basis points down to 0.5% in an effort to ease local financial conditions. Both, monetary and fiscal measures fueled activity in the second half of 2009. Inflation, as measured by the CPI, which was the main concern in previous years, dropped sharply and decreased by 1.4% compared to 2008, the first negative data in 75 years. Despite a reduction in export volume, the trade balance had a surplus of $13.3 billion in 2009 (compared to $8.8 billion in 2008 and $23.6 billion in 2007), mostly explained by the strong increase in cooper prices (a commodity that represents approximately half of Chilean total exports) and a fall in imports (volume and prices). The fears of a sudden stop of financial inflows receded quickly as foreign direct investment net inflows for 2009 reached $4 billion, an amount that, however, represents less than a half compared to $9.9 billion and $9.6 billion in 2008 and 2007, respectively. At the end of 2009, the nominal Chilean peso to U.S. dollar exchange rate was 506.7, an appreciation of 20% with respect to the exchange rate at the end of 2008 (629.1 pesos per U.S. dollar), that was driven by copper prices, growing opportunities derived from the strong recovery of shares and the fiscal funding needs (mostly satisfied with dollar selling in the local market). For the first time since 2003, the country had a public deficit of around 4.5% of GDP, mostly explained by the countercyclical measures implemented to mitigate the recession as previously mentioned. As a proof of its solid financial position the Chilean government financed this deficit almost exclusively with savings, its sovereign Economic and Social Stabilization Fund was reduced by an aggregate amount of $9 billion, from an initial balance of $20 billion.

Argentina

Argentina's GDP grew 0.9% in 2009 according to official statistics, although private estimates suggest that GDP contracted 4.3% in the period. This data contrasts with the average annual growth rates of approximately 8.5% achieved during each of the six preceding years (from 2003 through 2008). The Argentine peso depreciated 10.1% relative to the U.S. dollar, closing at 3.8 Argentine pesos per U.S. dollar at the end of 2009 compared to 3.45 Argentine pesos per U.S. dollar at the end of 2008 and 3.15 Argentine pesos per U.S. dollar at the end of 2007. The official CPI increased 7.7% in 2009 (compared to 7.2% in 2008 and 8.5% in 2007), although private entities estimate that the true increase was 14.3%. The current account balance showed a surplus of $11.3 billion in 2009, which is 60.5% and 52.9% higher compared to 2008 and 2007, respectively. The trade balance contributed significantly to this result since imports decreased 31.9%, more than the 20.4% decline in exports over the same period. Economic conditions also affected unemployment, which increased to 8.4% at the end of 2009 from 7.3% at the end of 2008 and 7.5% at the end of 2007.

Colombia

After the deceleration in GDP growth in 2008 (2.5% year-on-year compared with 7.5% year-on-year in 2007), in 2009 the Colombian economy entered into a recession as a result of the global financial crisis, an upsurge in its trade deficit and deterioration of neighboring economies. In particular, industry and retail sales were especially affected. The unemployment rate averaged 12% in 2009, moderately higher than the average rate in the prior two years (11.3% in 2008 and 11.2% in 2007). For 2009 analysts forecast GDP growth near 0.1% which may be explained by a better than expected last quarter. The incipient recovery is dependent upon a recovery in consumer confidence, a strong decrease in the CPI year-on-year (which increases real income), expansionary monetary policy implemented by the Colombian central bank in 2009 and further decreases in imports to lower trade imbalances. The current account deficit dropped from 2.8% of GDP in 2008 (same level in 2007) to 2.0% of GDP in 2009. During 2009, the Colombian peso appreciated relative to the U.S. dollar by 8.9% compared to a depreciation of 11.4% in 2008 and an appreciation of 10% in 2007. This appreciation was supported by a smaller than expected decrease in foreign investment (especially in the mining and oil sectors) and U.S. dollar inflows from the central government and Ecopetrol. The deceleration in the rate of annual CPI growth was partially explained by the weak aggregate demand in 2009 compared to 2008. In addition, food and regulated sector inflation moved prices below the low band of the Colombian central bank's target of 4.5%. Year-on-year CPI dropped from 7.7% for 2008 compared to 2007 to 2.0% for 2009 compared to 2008.

Table of Contents

Peru

During 2009, the Peruvian economy, in terms of GDP, grew by 0.9% compared to 9.8% in 2008 and 8.9% in 2007, well-above the region's results. The deceleration in GDP growth was mainly driven by a fall in domestic demand of 2.9%, with a significant decrease in private investment of 15.2%, while private consumption grew at only 1.9%. However, the fiscal stimulus implemented by the Peruvian government in 2009 contributed significantly to economic activity, with government spending growing 16.5% in 2009. Consumer prices, as measured by the CPI, increased by 0.3% in 2009, 0.7 percentage points below the lower limit of the central bank's target, compared with 6.7% in 2008 and 3.9% in 2007. The fiscal deficit was 2.1% of GDP, compared to the surplus of 2.1% in 2008, and a surplus of 3.1% in 2007, while net foreign direct investment decreased by 30%, compared with a gain of 14% in 2008 and 56% in 2007. In the foreign exchange market, the Peruvian nuevo sol appreciated 8% against the U.S. dollar in 2009, reaching 2.89 Peruvian nuevo sol per U.S. dollar at the end of the year, compared with a depreciation of 4.8% in 2008. Country risk, measured by the J.P. Morgan Emerging Markets Bond Index (EMBI Peru), fell 344 basis points to 165 basis points in 2009, explained by a gradual decrease in risk aversion to emerging markets, mainly in the first half of the year. Finally, Moody's Investors Service assigned investment grade status to Peruvian Long Term Foreign Currency Debt (BBB-/outlook stable), due to solid macroeconomic fundamentals, highlighted by sound public finances, financial markets dynamism, and a reduction of external vulnerabilities.

Ecuador

Ecuador's real GDP growth reached approximately 0.98% in 2009, compared to the growth of 6.5% in 2008 and 2.5% in 2007, as a result of the underperformance of several domestic demand components, primarily private consumption and investment. Consumer prices, as measured by CPI, rose 4.3% in 2009 (8.8% in 2008 and 3.3% in 2007), explained by lower food and beverages prices. In the external sector, the trade balance reached a deficit of $332 million in 2009, almost $1,240 million less than the surplus 2008, mainly as a result of the sharp correction in oil prices during the first half of 2009 and due to global economic slowdown, which had a negative effect over the country's non-oil exports. Ecuador's non-oil trade deficit grew by 34% to $4.9 billion in 2009 from $7.5 billion in 2008 and $4.3 billion in 2007. Consequently, the dollarization regime under which the country has operated since 2000 will likely be under stress during the beginning of 2010 and for as long as the still uncertain external environment (volatility in commodity prices and global economic weakness) affects Ecuador's external and fiscal accounts. During 2009, Ecuador lost $0.7 billion of its free disposable international reserves. Nevertheless, Ecuador's public finances have been supported by an improvement in tax revenues, multilateral agencies' loans and bilateral investment agreements. Finally, country risk, measured by J.P. Morgan Emerging Markets Bond Index (EMBI Ecuador), fell 3,962 points to 769 points during 2009, due to an improvement in the country's external net debt position and to a gradual reduction in the risk aversion to emerging markets.

Exchange Rate Fluctuations

We publish our Consolidated Financial Statements in euro. Because a substantial portion of our assets, liabilities, revenues and profit are denominated in currencies other than the euro, we are exposed to fluctuations in the values of these currencies against the euro. Currency fluctuations have had and may continue to have a material impact on our financial condition, results of operations and cash flows.

We estimate that in 2009 variations in currencies increased our consolidated cash flows by approximately €269 million and decreased our consolidated revenues by approximately 3.1%. Currency fluctuations can also have a significant impact on our statement of financial position, particularly equity attributable to equity holders of the parent, when translating the financial statements of subsidiaries located outside the euro zone into euro. For example, in 2009 equity attributable to equity holders of the parent increased by €2,238 million due to the translation of the financial statements of our foreign subsidiaries, principally due to the appreciation of the Brazilian real and the pound sterling relative to the euro, and the effect of the devaluation in Venezuela.

We estimate that in 2008 variations in currencies decreased our consolidated cash flows by approximately €302 million and decreased our consolidated revenues by approximately 3%. Currency fluctuations can also have a significant impact on our statement of financial position, particularly equity attributable to equity holders of the parent, when translating the financial statements of subsidiaries located outside the euro zone into euro. For

Table of Contents

example, in 2008 equity attributable to equity holders of the parent decreased by €3,708 million due to the translation of the financial statements of our foreign subsidiaries, principally due to the depreciation of the pound sterling and Brazilian real relative to the euro.

We estimate that in 2007 variations in currencies decreased our consolidated cash flows by approximately €261 million and decreased our consolidated revenues by approximately 1.2%. In addition, in 2007 equity attributable to equity holders of the parent decreased by €1,427 million due to the translation of the financial statements of our foreign subsidiaries, principally due to the depreciation of the dollar and pound sterling relative to the euro and the appreciation of the Brazilian real and the Czech crown relative to the euro.

The table below sets forth the average exchange rates against the euro of the dollar and the key currencies that impacted our consolidated results of operations for the periods indicated. Positive percentage changes represent a decline in the value of the applicable currency relative to the euro, and negative percentage changes represent increases in the value of the applicable currency relative to the euro.

	2007(1) Average	2008(1) Average	2009(1) Average	% change 2007 to 2008 Average	% change 2008 to 2009 Average
Pound Sterling	0.68	0.79	0.89	16.12%	12.04%
U.S. Dollar	1.37	1.46	1.39	6.94%	(5.00)%
Brazilian Real	2.66	2.66	2.76	(0.09)%	3.68%
Argentine Peso	4.26	4.63	5.17	8.67%	11.70%
Peruvian Nuevo Sol	4.28	4.29	4.18	0.29%	(2.56)%
Chilean Peso	714.64	758.73	775.80	6.15%	2.25%
Mexican Peso	14.95	16.24	18.78	8.60%	15.63%
Venezuelan Bolivar fuerte	2.94	3.15	2.99	6.98%	(5.00)%
Czech Crown	27.76	24.97	26.44	(10.04)%	5.87%
Colombian Peso	2,837.13	2,873.56	2,985.07	1.15%	3.88%
Guatemalan Quetzal	10.50	11.07	11.33	5.40%	2.37%

Source: Central treasury bank of the respective countries.

(1) These exchange rates are used to convert the income statements of our subsidiaries from local currency to euro.

In the comparison below of our results of operations, we have provided certain comparisons at constant exchange rates in order to present an analysis of the development of our results of operations from year-to-year without the effects of currency fluctuations. To make such comparisons, we have converted into euro certain financial items for the relevant year using the prior year's average exchange rate. We refer to such comparisons as being made on a "constant euro basis" or "excluding foreign exchange rate effects".

We also make certain comparisons on a local currency basis. To make comparisons on a local currency basis, we compare financial items in the relevant local currency for the periods indicated as recorded in the relevant local currency for such periods.

We describe certain risks relating to exchange rate fluctuations in "Item 3. Key Information—Risk Factors", and we describe our policy with respect to limiting our exposure to short-term fluctuations in exchange rates under "Item 11. Quantitative and Qualitative Disclosures About Market Risk".

Regulation

We are subject to regulation in the different markets where we operate, particularly with regard to the prices we can charge for certain of our goods and services in certain jurisdictions as well as our need to comply with certain obligations, which has a significant effect on our profitability. For more information regarding regulation in the markets in which we operate, see "Item 4. Information on the Company—Business Overview—Regulation".

Table of Contents

Group Results of Operations

A summary of our results of operations for 2007, 2008 and 2009 and certain consolidated revenue and expense items as a percentage of revenues for the periods indicated is shown below.

	Year ended December 31,					
	2007		2008		2009	
	Total	Percentage of revenues	Total	Percentage of revenues	Total	Percentage of revenues
	(in millions of euros, except percentage of revenues)					
Revenues	56,441	100.0%	57,946	100.0%	56,731	100.0%
Other income	4,264	7.6%	1,865	3.2%	1,645	2.9%
Supplies	(17,907)	(31.7)%	(17,818)	(30.7)%	(16,717)	(29.5)%
Personnel expenses	(7,893)	(14.0)%	(6,762)	(11.7)%	(6,775)	(11.9)%
Other expenses	(12,081)	(21.4)%	(12,312)	(21.2)%	(12,281)	(21.6)%
Operating income before depreciation and amortization (OIBDA)(1)	22,824	40.4%	22,919	39.6%	22,603	39.8%
Depreciation and amortization	(9,436)	(16.7)%	(9,046)	(15.6)%	(8,956)	(15.8)%
Operating income	13,388	23.7%	13,873	23.9%	13,647	24.1%
Share of profit (loss) of associates	140	0.2%	(161)	(0.3)%	47	0.1%
Net financial income (expense)	(2,844)	(5.0)%	(2,797)	(4.8)%	(3,307)	(5.8)%
Corporate income tax	(1,565)	(2.8)%	(3,089)	(5.3)%	(2,450)	(4.3)%
Profit for the year from continuing operations	9,119	16.2%	7,826	13.5%	7,937	