



2011

Sustainability Report

Together transforming
...development

Telefonica



**2011
Sustainability
Report**

Telefonica

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The Company's Vision



Dear Friends,

At Telefónica, our calling to become a strategic ally for the technological, economic and social development of the communities in which we operate is built into our DNA. We are convinced that our sector can provide solutions to the most important problems faced by the planet: wherever information and communication technologies (ICT) are implemented, productivity rises, education improves, health and energy costs fall and inclusion is promoted. To put it another way: wherever ICT are found, there is development.

At Telefónica, as a leading telecom, we want to contribute to that development with two approaches to our work. With the first, we hope to drive corporate sustainability, understood as a strategy based on the creation of long-term value, by seizing opportunities and by efficaciously managing the risks inherent to economic, social and environmental development (in line with the Dow Jones Sustainability Index's definition of this concept)¹. With the second, and through the Fundación Telefónica, we strive to promote community work and cultural endeavours, and, especially, through educational programmes that eradicate child labour and facilitate access to knowledge and the use of ICT².

In this document, the reader will find an executive summary of our activity in 2011. In preparing this summary we have focused on the three basic dimensions of sustainability: the economic dimension (supply chain, codes of conduct, child protection and privacy); the social dimension (climate and commitment, safety and health, diversity, digital inclusion and social projects); and the environmental dimension (energy efficiency and green services), as well as the references to each of the 10 Principles composing the UN Global Compact.

We are firmly convinced that we can be an engine of development and progress in the societies and countries where we work. Our challenge is to be a little better every day.

César Alierta
Chairman and CEO of Telefónica

¹ The Corporate Sustainability Report is available at: <http://www.rcysostenibilidad.telefonica.com/es/>
² The Fundación Telefónica Report is available at: http://www.fundacion.telefonica.com/es/conocenos/informe_anual/index.htm

7.13
Customer Satisfaction Index,
same level as 2010

8.1%
of revenue
invested in technological
innovation

€66.7
million
invested in training our professionals



About the report



Principles for the 2011 Sustainability Report



Following is Telefónica's 10th annual Sustainability Report. This report discusses the progress made in social, environmental and good governance issues throughout 2011 and the objectives for 2012.

Telefónica is one of the world's leading integrated telecommunications operators, providing communication, information and entertainment solutions, with operations in Europe and Latin America. Telefónica operates in 25 countries and as of December 2011 had more than 306.6 million customers. Incorporated in Spain in 1914, Telefónica is a totally private company, with more than 1.5 million direct shareholders. Its shares are traded on the continuous market on the Spanish Stock Exchanges (Madrid, Barcelona, Bilbao and Valencia) and on those of London, New York, Lima and Buenos Aires. Telefónica ranks seventh in the telecommunications sector worldwide by market capitalisation. It is Europe's leading integrated operator and ranks seventh in the Eurostoxx 50 index of Eurozone blue chip stocks at 31 December 2011.

Telefónica boasts one of the industry's most international profiles, generating more than 60% of its business outside its home market. Movistar, Vivo and O2 are the main brands under which Telefónica markets its products in the various countries: Vivo in Brazil, Movistar in Spain and Latin America, and O2 in the UK, Ireland, Germany, the Czech Republic and Slovakia.

According to the Global Reporting Initiative (GRI)

Principles for defining Report content:

The 2011 Sustainability Report was prepared in accordance with Sustainability Reporting Guidelines version 3.1 issued by the Global Reporting Initiative (GRI). This chapter provides a brief explanation of how the GRI-G3.1 reporting guidelines were applied in preparation of the Report and lists the principles for defining report content and the principles for ensuring report quality.

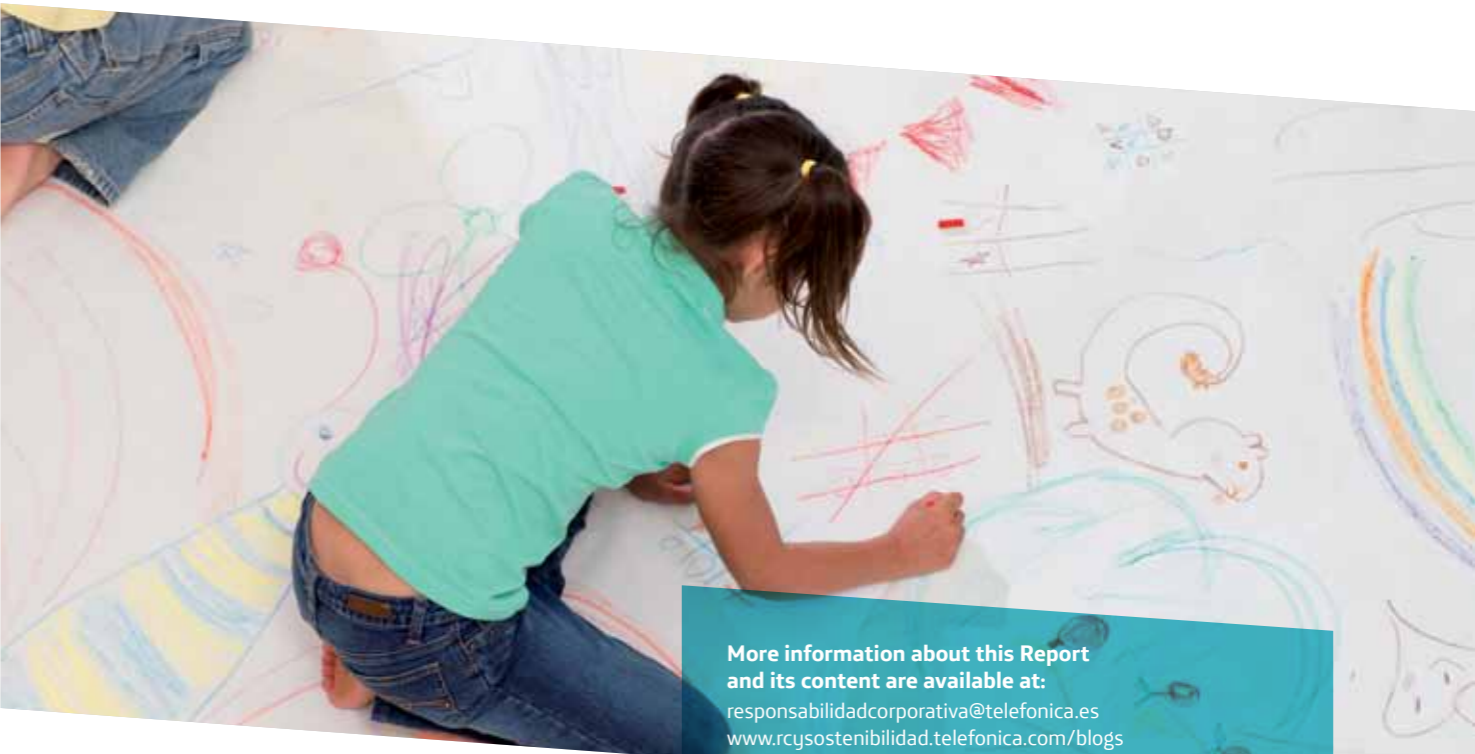
In order to ensure a balanced and reasonable representation of the organisation's performance, a determination was made about what content the report should cover. This was made considering Telefónica's purpose and the interests of our stakeholders.

- **Materiality:** The information in the Report covers the topics and indicators that reflect Telefónica's significant economic, environmental and social impacts or that would substantively influence the assessments and decisions of our stakeholders, based on a combination of internal and external factors.
- **Stakeholder inclusiveness:** Telefónica has identified its shareholders and explained in this Report how it has responded to their reasonable expectations and interests.

The qualitative and quantitative information in this Report was gathered using internally- and externally-developed IT tools; e.g. eSIF for human resources-related issues, Credit 360 for customer- and community-related issues and SAP for environmental-related issues. Use of these tools enabled us to self-declare and assure each figure from its source division, and monitor its traceability, any deviation and confidence at different levels of aggregation, with two check and verification processes, both internal (Management Control/CFO in some countries and Corporate Environment and Sustainability departments) and external (Ernst & Young, Aenor).

The Report has been externally assured and is based on the principles of the Global Reporting Initiative (GRI) and AA1000 (APS) for disclosure, the most widely recognised and used standards in the preparation of this type of report, with the overriding aim of facilitating understanding, comparability and maximum transparency with respect to our stakeholders.

- **Sustainability context:** Telefónica presents its performance in the wider context of sustainability. Telefónica presents its understanding of sustainable development and draws on objective and available information as well as measures of sustainable development for the topics covered in the Report, its sustainable development conditions and goals, how sustainability topics relate to the Company's long-term strategy, risks and opportunities, debates with stakeholder groups on this issue and Telefónica's performances in the various geographical areas where it operates.
- **Completeness:** Coverage of the material topics and indicators and definition of the Report boundary are sufficient to reflect significant economic, environmental, and social impacts and enable stakeholders to assess Telefónica's performance in the reporting period.



More information about this Report and its content are available at:

responsabilidadcorporativa@telefonica.es
www.rcysostenibilidad.telefonica.com/blogs
www.youtube.com/rcysostenibilidad
www.twitter.com/rcysost
www.facebook.com/rcysostenibilidad

Requests by mail should be sent to:

Reputación y Sostenibilidad Corporativas
Telefónica S.A. - Distrito Telefónica
Ronda de la Comunicación S/N - Edificio Oeste 2. Planta 1
28050 Madrid

Principles for defining Report quality:

- **Balance:** the Report reflects positive and negative aspects of Telefónica's performance to enabled a reasoned assessment of overall performance.
- **Comparability:** the Report and information contained within can be compared on a year-to-year basis through tables and charts, with identification of any significant variations between reporting periods in the boundary and scope. In addition, ATLAS RC facilitates comparability of key performance indicators in Telefónica's sustainability performance.
- **Accuracy:** the Report information is sufficiently accurate and detailed (data, sources, measurement techniques, bases for calculation, underlying assumptions and estimates) for our stakeholders to assess Telefónica's performance. This information is compared with an independent report by Ernst & Young.
- **Timeliness:** reporting occurs on a regular schedule for stakeholders to make informed decisions.
- **Clarity:** the report presents information in a way that is understandable, accessible and usable by our stakeholders with respect to risks and opportunities and other stakeholders.
- **Reliability / assurance:** the information and processes used in the preparation of this Report were gathered, recorded, compiled,

analysed and disclosed in a way that could be subject to external examination.

According to AA1000 (APS)

AA1000AS (2008) was developed to assure the quality of an organisation's sustainability reporting and the processes, systems and competencies to execute them throughout the organisation. Assurance was performed by Ernst & Young in accordance with the principles defined in the Standard:

- **Inclusivity:** the participation of stakeholders in developing and achieving an accountable and strategic response to sustainability.
- **Materiality:** Telefónica has determined the relevance and significance of an issue to its stakeholders.
- **Responsiveness:** this Report offers Telefónica's response to demands of stakeholders in terms of the Company's sustainability objectives and targets included herein.

Report boundary

The 2011 Sustainability Report describes key information on Telefónica's sustainability performance over the year in terms of the economic, environmental and social impacts in the countries where Telefónica has telecommunications operations.

Telefónica is a global company, with operations in 25 countries and around 307 million customers. It has over 286,000 employees, nearly 15,000 suppliers and more than 1.5 million shareholders.

Several structural changes took place at Telefónica in 2011. The business in Spain was included in the Europe region, while two large areas were created to respond to the global opportunities presented to Telefónica: Telefónica Global Systems and Telefónica Digital. However, as these changes came towards the end of 2011, we have decided to maintain the reporting structure for Spain separate from the rest of Europe to maintain criteria of transparency and comparability with 2010 so stakeholders will not miss any information.

In the 2011 Sustainability Report, we attempt to describe clearly the boundary of operations considered to give stakeholders a clear understanding of Telefónica's sustainability performance.

Since Telefónica published its the first Sustainability Report in 2002, the Company has presented itself to stakeholders as a global benchmark in the telecommunications industry. This is why we have included data on our operations in each country where Telefónica does business since then.

Local sustainability reports are prepared for the following countries:

Germany	(since 2006)	Spain	(since 1999)
UK	(since 2006)	Guatemala	(since 2006)
Czech Republic	(since 2006)	Mexico	(since 2006)
Argentina	(since 2006)	Nicaragua	(since 2006)
Brazil	(since 2003)	Panama	(since 2006)
Colombia	(since 2006)	Peru	(since 2003)
Ecuador	(since 2006)	Uruguay	(since 2009)
El Salvador	(since 2006)	Venezuela	(since 2006)

The 2011 Sustainability Report includes economic, environmental and social information from all countries where Telefónica operates. To provide this information, Telefónica has an on-line system for co-ordinating and consolidating the information received from each country and each qualitative and quantitative indicator. With this system, activities in each country can be assessed in a comparable, weighted and measurable way for use as a management tool. The start-up of this corporate system also helps improve external assurance of the report.

The sources of information for each chapter of the 2011 Sustainability Report are as follows:

- ↳ **Economic and financial information:** the same sources as those used for the 2011 Financial Report audited by Ernst & Young. The report boundary includes all the financial statements of Telefónica, bearing in mind that EBITDA data of the businesses are shown before brand and management fees and, for Spain, include a provision of 2,671 million euros for workforce adjustments in Spain in the third quarter of 2011. CapEx figures include spectrum acquisition in Brazil, Colombia and Costa Rica. Telefónica Latin America's figures from the second quarter of 2011 include the full consolidation of TVA (with retrospective effect from 1 January 2011), which was already included in the Telefónica scope of consolidation since the fourth quarter of 2007.
- ↳ **Corporate governance and shareholders:** the same sources as those used to prepare the Annual Report on Corporate Governance. The boundary in this report relates to the Telefónica Group.
- ↳ **Innovation:** (consolidated under the corporate innovation department of Telefónica S.A. in cooperation with Telefónica I+D). Procurement systems for data on investment in innovation. Data are consolidated without applying any criteria of proportionality. As this entails financial data, the boundary relates to the economic and financial data described above.
- ↳ **Customers:** Telefónica S.A.'s quality control systems and Telefónica Latin America's and Telefónica Europe's operations. It must be highlighted that Telefónica's total accesses do not necessarily have to coincide with the partial sum of accesses

country by country, as in accordance with standardisation criteria, the Corporate Control Management must standardise certain criteria for accounting accesses. The standardisation criteria used are: PSTN (including Public Use Telephony) x1; ISDN Basic Access x1; ISDN primary access, 2/6 digital access x30 including accesses for internal use and total fixed wireless accesses, VoIP and naked ADSL, treatment of ADSL, satellite, optical fibre, cable modem and broadband circuits as broadband, and as Pay-TV customers the sum of cable TV + IPTV televisions access + satellite TV accesses (DTH), ULL rented by T O2 Germany and wholesale line rental (WLR) in Spain.

- ↳ **Employees:** the Human Resources management systems. This Report uses the term 'people' rather than 'equivalent employee', as used in financial reporting. Where consolidated figures are shown, a proportionality factor based on employees is used. This chapter includes the Telefónica Group's entire financial boundary, although some performance indicators exclude Atento to prevent distortion from its business-related information, as Atento's business is considerably different to that of the provision of telecommunications services, which is the Company's core business. All indicators excluding Atento are clearly indicated in table footnotes.
- ↳ **Environment and climate change:** from the Environment and Operations departments in each country. The information is obtained from on-line questionnaires and other types of IT supports provided to the companies in each country. Data are consolidated by simple addition and for climate change by bearing in mind GHG Protocol emission factors. This chapter includes all telecommunications operators within the Telefónica Group's boundary, the corporate headquarters -Districto Telefónica- and Telefónica S.A.
- ↳ **Providers:** directly from the contract allocator through the procurement departments. Data are consolidated without applying any factor of proportionality and presented broken down by country or business line. This chapter includes the Telefónica Group's entire financial boundary. A distinction must be made between figures for "Cost of sales" in the consolidated financial statements (on an accruals basis and Telefónica, S.A.'s consolidation scope) and the criterion of "allocated purchases" used in various chapters in this Report related to purchases approved in the reporting period irrespective of whether they were accounted for and accrued as an expense.
- ↳ **Digital inclusion:** from the quality control, operations and regulation systems of Telefónica Spain, Telefónica Latin America and Telefónica Europe. Also included in the boundary are Telefónica I+D and Fundación Telefónica's social innovation initiatives.
- ↳ **Social action:** from Fundación Telefónica, ATAM, Telefónica S.A.'s sponsorship departments and the initiatives carried out by the Corporate Responsibility and Sustainability department. This information is assured in accordance with the London Benchmarking Group (LBG) international standard so readers can understand, compare and assess investment over time and performance more easily.
- ↳ **Exchange rates:** all figures in this Report are presented in current euros unless indicated otherwise. Average annual exchange rates for each period are used.

Services described in this Report

The 2011 Sustainability Report covers all the telecommunications services provided directly by Telefónica in the various countries where it operates and whose revenues are fully consolidated. The assessment of the impact of each business line on stakeholders shows that the fixed telephony and the mobile telephony businesses have by far the largest impact on stakeholders. Accordingly, all non-financial data for countries included in this Report relate to the fixed and mobile telecommunications businesses. In specific instances where the consolidated data cover more companies (e.g. Terra, Atento), this is stated expressly in the table footnote.

This year, for the first time, Vivo in Brazil is fully consolidated, for both the 12 months of 2010 and of 2011, as are the operations in Slovakia, where Telefónica now has more than a million customers, making it a relevant operator.

Exclusions from the Report boundary

This Report does not include information on the following telephony operators in which Telefónica's shareholding is below 50% and over which it does not exercise control:

- ↳ **China Unicom:** Telefónica's strategic shareholding is 5.38%.
- ↳ **Telecom Italia:** Telefónica's strategic shareholding is 10.36%.
- ↳ **Atento:** included in certain Human Resources indicators for its relevance on Telefónica's total employees. Nevertheless, as this activity is not related to telecommunications and could distort the transparency and comparability of Telefónica's core businesses with those of its peers and competitors, and as the Company has disclosed to the CNMV its intention of selling a controlling interest in this activity, we have decided not to include Atento in the analysis of certain indicators where the different nature of the business would distort comparison of Telefónica's past and future performance indicators with other industry companies.

Applying principles of materiality, Telefónica de Contenidos (Telefe, Telefónica Servicios de Música and Telefónica Servicios Audiovisuales), Telefónica I+D and T-Gestiona are not included in the Report except where mentioned explicitly or in reference to the Group. Other Telefónica companies not reported on are Lycos Europa (32.1% stake) and Amper (6.10% stake).

Exceptional inclusions to the Report boundary

An assessment was made of Telefónica Group units that could have a significant impact on stakeholders. The companies identified are as follows:

- ↳ **Telefónica I+D** in the chapter of Technological Innovation.
- ↳ **Atento** in the chapter of Employees.
- ↳ **Fundación Telefónica** and **ATAM** in the chapter of Community.
- ↳ **Telefónica S.A.** as the corporate centre in the chapters of Shareholders and Stakeholder Engagement.

Report structure

Telefónica presents its 2011 Sustainability Report, predicated on credibility, rigour and transparency.

The Sustainability Report is a management report that discusses the improvements and advances made in sustainability, monitors performance and assesses performance against the Company's targets and commitments.

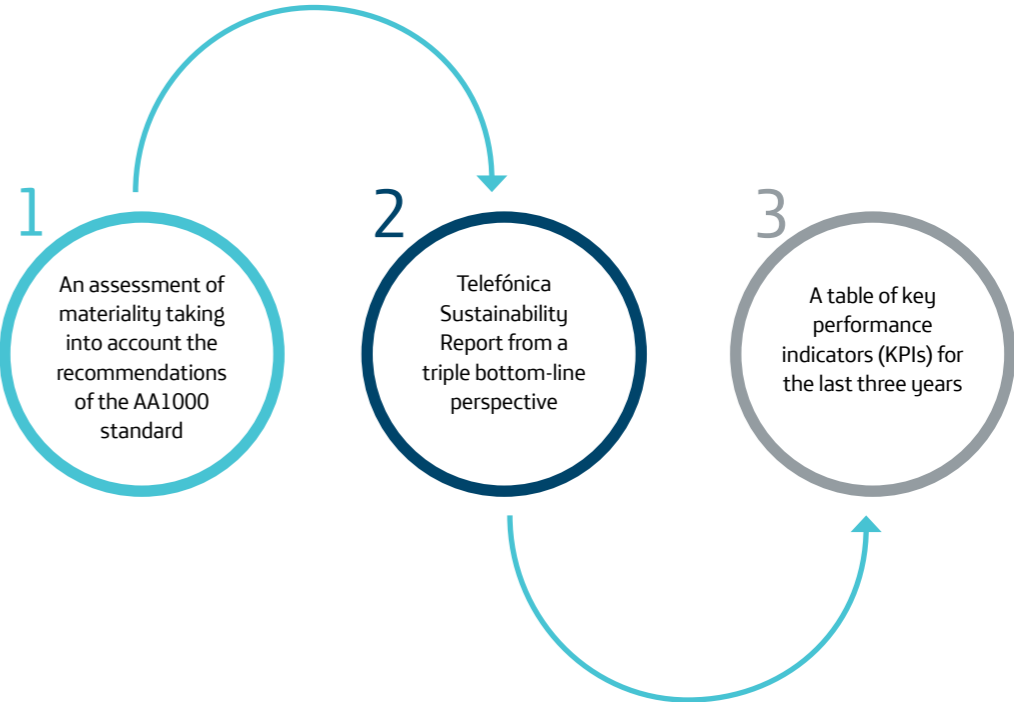
The Report first presents an assessment of materiality taking into account the recommendations of the AA1000 standard for identifying issues that are material for sustainability at Telefónica, the Company's strategic approach to sustainability and its global organisational structure.

We then present the Sustainability Report from a triple bottom-line perspective, providing performance indicators and reporting on the most significant advances made at the Company in the economic, environmental and social dimensions of sustainability. The categories and subcategories are organised in accordance with the standard SAM classification for the Dow Jones Sustainability Index (DJSI) for easier comparison by readers of their impacts with other leading sustainability-driven companies.

A table of key performance indicators (KPIs) for the last three years is included to summarise and provide a quantitative snapshot of the relevant topics at Telefónica in respect of economic, environmental and social sustainability.

As in previous editions of this report, included is communication on progress in implementing the principles of the Global Compact and the GRI indicators related to these principles. We attempt to maintain general, global and inter-sector criteria to allow for reader comparability, to improve transparency of the actions undertaken and to reflect progress in performance in the spirit of the Global Compact progress reports.

Assessment of all impacts is guided by the principles of inclusiveness, materiality and responsiveness (the AA1000 principles) and version 3.1 of the Sustainability Reporting Guidelines of the Global Reporting Initiative (GRI), which is attached to this report and refers to the answers given in the. Also attached are the external assurance letters of the information provided through this Report.



Telefónica 2011 Sustainability Report

Financial and management report
Corporate Governance Report
Material sustainability topics
Economic impact
Environmental impact
Social impact
GRI 3.1 AA1000
External assurance

Methodology for dialogue with stakeholders



The issues that most concern our stakeholders are the basis that we use at Telefónica to prioritise our Sustainability and Corporate Responsibility projects and to define and adapt our strategy concerning them.

Understanding the issues that most concern our stakeholders is the basis that we use at Telefónica to prioritise our Sustainability and Corporate Responsibility projects in the different markets where we are present, as well as to define and adapt our strategy concerning these issues. The standardised practice of dialogue with our stakeholders allows us to mitigate risks, identify new business opportunities and improve financial results. The result of these long-term relations established under the criteria of transparency and responsibility is one of the foundations that form the matrix of materiality of our company, which makes up this Report.

Among our stakeholders are all those people, associations and institutions that either affect Telefónica's social initiatives or are affected by them. Among these, we find our customers, employees, shareholders and suppliers, as well as different sector organisations and governmental and non-governmental organisations that we collaborate closely with, as is fit for an organisation as important as Telefónica, for the development of the communities where we operate.

You can find more detailed information about how actions for habitual dialogue with our stakeholders are pinpointed in the chapter entitled [Stakeholder Engagement](#), in this report.

Survey on material aspects for experts

In January 2012, an online survey of experts about matters relating to materiality at Telefónica took place in the Diario Responsable. For three weeks, it was made available to the readers of the newspaper and linked to all the communication channels and social networks for Sustainability and Corporate Responsibility at Telefónica in the different countries where Telefónica operates.

There were two main objectives of the project:

- To find out from the perspective of the experts their assessments and possible improvements in materiality indicators for Telefónica's 2011 report.
- To take advantage of the survey to obtain, from among these people, a global assessment of the whole of the 2010 report, as well as some open questions about other possible issues of interest.

As a result, we obtained a total of 334 questionnaires that had been fully or partially filled in by an expert public made up of: professionals from the field of Sustainability and CSR (32%), teaching professionals (22%), professionals in communication (21%) and Third Sector professionals, or NGOs (12%). Of these, 58% of the respondents answered from Spain, 27% from Latin America and the rest from other European countries.

The conclusions emerging from those questionnaires were that the indicators presented as the basis used to carry out our matrix of

materiality are in line with the level of relevance given by the experts consulted, and that the great majority of the subjects that we deal with are considered by a large percentage of respondents to be very or quite relevant. All these subjects are dealt with throughout this report.

The indicators considered to be most relevant by the expert public were, in the following order: child protection, transparency as regards rates, privacy and green ICT.

The proposed indicators that generated a lower degree of consensus were electromagnetic fields and responsible marketing.

As regards the un-suggested responses about Sustainability and Corporate Responsibility issues associated with Telefónica, the most noteworthy were transparency, aspects linked to employment policies at our company and other aspects relating to customer care.

Transparency was linked in the answers above all to the remuneration of the directors and senior management staff of the company. We give full information about this issue in the Corporate Governance Report and in the Report on Compensation Policy for the Board of Directors of Telefónica, which is attached to this Report and which you can view by clicking [here](#).

The aspects raised linked to employment policies were policies on job stability and maintaining posts of work, principally, the integration and achievement of a work/family balance, and the equality policies followed by the company. The answers to these points are contained in this Report, mainly in the chapters on [Diversity](#) and [Relations with our professionals](#).

Among the customer care aspects suggested in the surveys, the following stand out: specific action for the crisis period, improved management of claims, management of disconnections and special rates for groups with difficulties. The answers to these points are contained in this Report, in the chapters on [Social innovation](#) and [Relations with our customers](#).

We wish to highlight that, in the tag cloud arising out of sharing all the open suggestions that were made about the creation of the 2012 Report, the words used most repeatedly in the area of sustainability management were: transparency, protection, privacy and commitment.

diario_responsable

Stakeholders identified	Methodology of dialogue	Some examples of dialogue
Customers	Through the channels for dialogue that we establish at the time of sale and through our customer care service, the monitoring of customer satisfaction, the Customer Ombudsman Service (COS), as well as the marketing and market research divisions, forums for debate and areas for meeting, in order to find out the consumer experience of our products and services as regards Sustainability and Corporate Responsibility.	http://info.telefonica.es/es/servicio_defensa_cliente/html/ http://www.telefonica.com.br/residencial/atencaoaocliente/faleconosco/ombudsmen/ http://forum.o2.co.uk/ http://www.movistar.com.mx/Contacto-Foro-Conectados#ForoConectados http://www.movistar.com.ar/foro/web/guest/foro https://twitter.com/#!/search/users/Telef%C3%B3nica https://twitter.com/#!/search/users/O2
Employees	Through the annual survey for all our professionals, where there are specific sections on sustainability and ethical issues.	https://twitter.com/#!/UniversitasTef
Shareholders	Through ongoing individual and collective meetings with institutional investors and sector analysis, as well as online channels, to find out the issues that most concern the investing community and respond to their questions, so that we can establish direct communication channels that function on a continuing basis.	http://www.telefonica.com/es/shareholders_investors/jsp/home/home.jsp http://serviciosaccionistas.telefonica.es/Registro.do?idioma=es http://www.telefonica.com/es/shareholders_investors/html/presentaciones/confinversores.shtml http://www.telefonica.com/es/shareholders_investors/html/presentaciones/index_foros.shtml
Suppliers	Through the biannual survey on Supplier Satisfaction and the quality assessments included in the quality systems of the various operators.	http://www.telefonica.com/es/suppliers/html/mode-lo_compras/como_ser_proveedor.shtml
Sector organisations	We participate actively in forums and associations that debate on the particular issues of Sustainability and Corporate Responsibility that affect our sector, in order to improve measurements, standardise indicators and share best experiences	Global e-Sustainability Initiative (GeSI). GSMA and GSM Europe CSR Europe International Telecommunication Union (ITU) ETNO (European Telecommunication Network Operators)
Governmental organisations	Dialogue is mainly structured around geographical regions, grouping the different dialogue partners in accordance with their field of activity: local, regional, national and global. Within each field of activity, we maintain fluid dialogue with those in charge of telecommunications services, innovation, consumption, education, social areas, regulatory issues and economic issues, among others.	Through the Institutional Relations and Regulation units within the different Telefónica operations.
Non-governmental organisations and Foundations.	Collaboration agreements and ongoing dialogue. These are the main advocates of the products and services developed at Telefónica for people with some kind of disability.	ONCE and its Foundation ASPAYN Granada CNSE and its Foundation FIAPAS FAPS CERMI
Professional public	The opinion of those who are experts in sustainability and corporate responsibility issues is very constructive for identifying material matters. The professional magazine Media Responsable was commissioned to carry out a survey on this aspect, through which we received 334 questionnaires giving opinions on the materiality indicators at Telefónica and its transparency policy, as well as new areas of interest for these experts.	Click here to go to the following section which talks about the survey

Materiality matrix

We analyse key issues based on the sector, our strategy and stakeholder expectations. We then prioritise the results in accordance with the impact on our strategy, which has been strengthened by the new Bravo!+ programme.

To draw up the 9th Corporate Responsibility and Sustainability Report, and as a follow-up to the previous year, we created an analysis of material aspects (in accordance with standard AA1000AS) with the objective of focussing that new report on those issues that are relevant, thus responding to the demands and concerns of our Stakeholders¹.

The materiality study took place in two differentiated stages.

Firstly, there was initial identification based on an analysis of the telecommunications sector, our strategy as a company and the expectations of the stakeholders, which allowed up to 48 relevant points to be detected.

Many different sources were used for this analysis:

- Requirements and requisites of international bodies such as the OECD, ILO, European Commission and digital agendas
- Investment indexes like the Dow Jones Sustainability Index and FTSE4Good.
- Industry analyst reports.
- Telefónica risk analysis.
- Analysis of financial results
- Review of projects within the Corporate Business Principles Office and local offices.
- Survey on materiality with expert public.
- Dialogue with our stakeholders. In addition to the multi-stakeholder dialogue panels carried out in most of the countries about the Corporate Responsibility Report or other key issues, in 2010 the 2.0 dialogue channels (web², blogs, Twitter, YouTube, Flickr) were consolidated.

The second stage consisted of prioritising the results initially obtained according to two variables:

- 1. Real or potential impact on our strategy: The strategic priorities that have been reinforced with the new bravo!+ programme are:
 - Seizing digital opportunities
 - Strengthening the business's profitability and sustainability
 - Streamlining decision-making by simplifying processes

The transformation with bravo!+ is deployed around five new forms of conduct:

- +**Customer:** We offer the best customer experience and turn our knowledge of customers into an advantage for them as well as for Telefónica.
- +**Digital:** We adopt the most innovative technologies in order to seize future opportunities in our sector.
- +**Global:** We capture all of the advantages of our global scale.
- +**flexible:** We take decisions and implement them promptly and in a straightforward and focused manner. This allows for simplicity and clarity in our organisation and decision-making processes, as well as for less bureaucracy, and ensures that we have motivated and committed professionals.
- +**Leader:** We are setting trends in order to be the best global communications company in the world.

- 2. Level of interest of our stakeholders.

1. The origin of materiality analysis is found in the study "The contribution the ICT Industry Can Make to Sustainable Development" commissioned by the Global eSustainability Initiative (GeSI) and conducted by Business for Social Responsibility (BSR)
2. www.rcysostenibilidad.com

The prioritisation exercise was carried out with the units in charge of managing the initially identified material aspects, in addition to applying a country risk analysis filter, consisting of assessing impact on strategy and reputation.

The results obtained confirmed the importance for us of aspects such as privacy and data protection, safe use of the Internet by children and young people, and Green ICT.

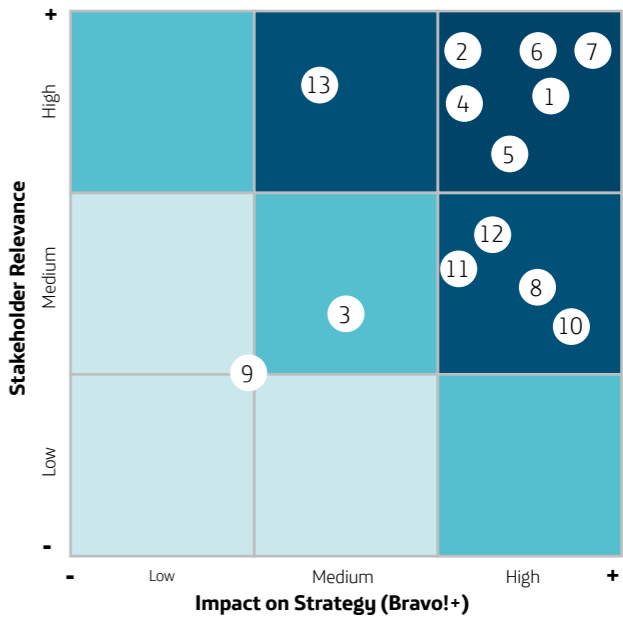
Those issues with a medium-high impact after the analysis, from the perspective of the expert public, appear in the materiality matrix shown. The discussion of these aspects can be found throughout this report.

Economic dimension:
Supply Chain Responsibility, Integrity and Codes of Conduct, Safe use of the Internet by children and young people, Data Protection and Privacy.

Social dimension:
Diversity, Health and Safety, Digital Inclusion.

Environmental dimension:
Energy efficiency, efficient services, Green Innovation, Environmental Management.

Materiality Matrix (*)



- 1 Privacy and Data Protection
- 2 Safe Internet Use by Children and Young People
- 3 Electromagnetic Fields
- 4 Green ICT
- 5 Code of Conduct
- 6 Transparency
- 7 Quality of Service
- 8 Supply Chain
- 9 Diversity
- 10 Responsible Marketing
- 11 Digital Inclusion
- 12 Accessibility
- 13 Environmental Management

* Survey on material topics for expert groups (334 surveys completed).

Sustainability at Telefónica



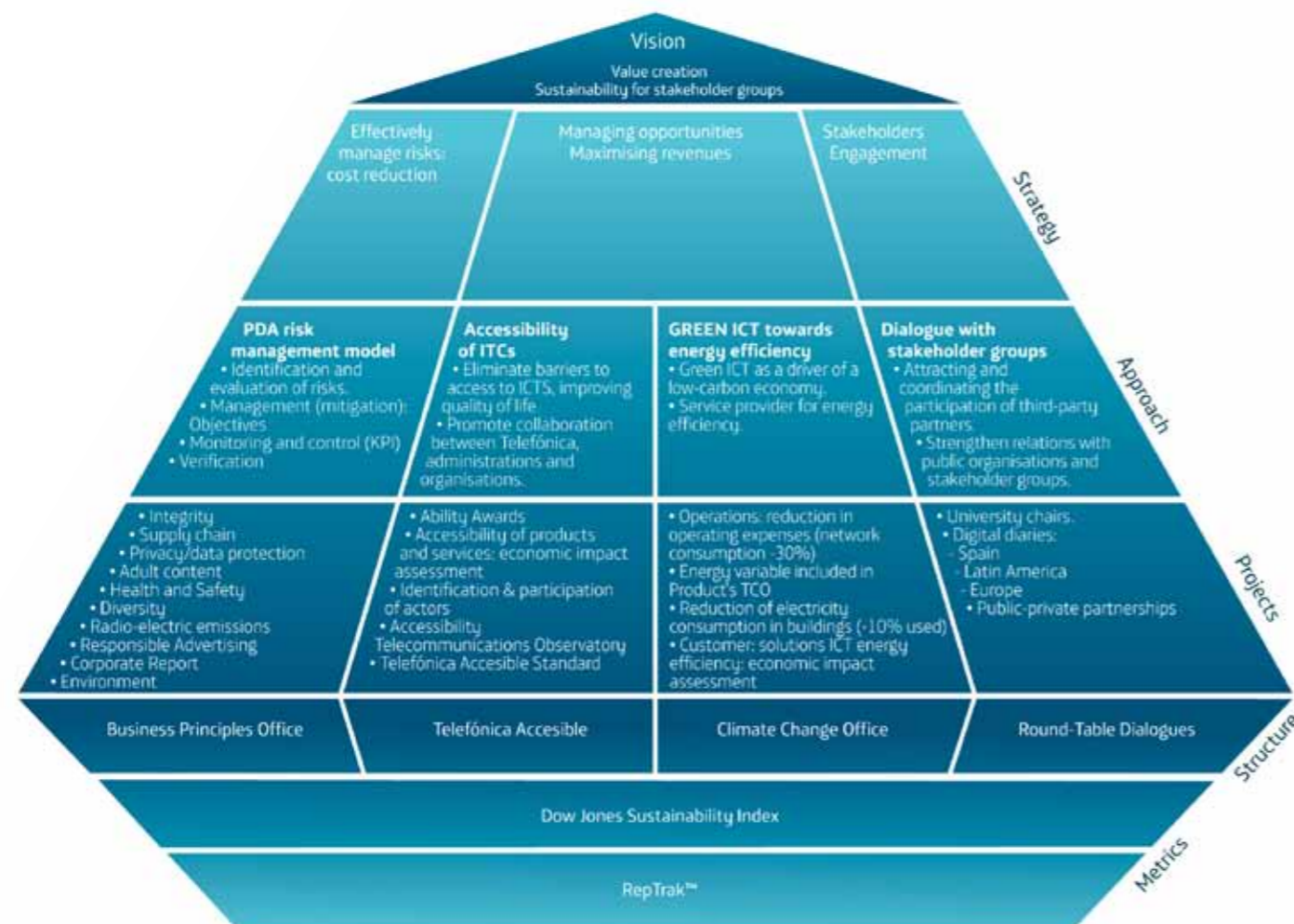
The Company has become more competitive thanks to 13 key projects linked to sustainability based on a two-fold approach consisting of proper risk management and the leveraging of opportunities.

In 2011, we made further progress with our sustainability approach, in line with the guidelines set forth in the leading index on responsible investment, the Dow Jones Sustainability Index (DJSI): "Corporate sustainability is a business approach that creates long-term shareholder value by embracing opportunities and managing risks deriving from economic, environmental and social developments".

At Telefónica, we show our commitment to sustainability as a key intangible asset for value creation, through our transparent management approach and our competitive spirit. Transparency allows us to earn the trust of the markets and, in general, to instil trust among our stakeholders. The Company has become more competitive by streamlining expenditures and generating higher revenue through 13 key projects linked to sustainability. This effort is based on a two-fold approach consisting of proper risk management and the seizing of opportunities".

We understand the need to manage risks associated with a failure to comply with Corporate Guidelines, which serve as the basic norm of conduct governing the Company's relations with its stakeholders, and to manage opportunities that allow us to maximise revenue and that are clearly intended to make a social contribution. In so doing, we reaffirm our commitment to stakeholders, which requires transparent communication and effective dialogue in order to construct trust-based relations. This, in turn, allows us to promote economic, technological and social progress by using ICTs and generating value for the Company.

This year we have made the transition to a reporting model based on a triple bottom-line perspective incorporating the economic, social and environmental dimensions. This model is fully compliant with the DJSI and GRI A+ and has been verified externally according to the AA1000 criterion.



Corporate structure

At Telefónica, managing Responsibility and Sustainability is one of the competencies of the General Technical Secretariat to the Chairman's Office, an area responsible for developing and managing the Company's intangible assets and which plays a role in the Executive Committee.

To strengthen these areas within the organisation and ensure that they are built into its DNA, the Company has established a Committee on the Board of Directors. In fact, Telefónica was the first Ibex-35 company to have such a body, which was created in June 2002. The Human Resources and Corporate Reputation and Responsibility Committee is made up of five board members (four independent and one proprietary), and meets periodically and whenever the Board asks it to intervene.

Board members

- ➔ **Javier de Paz Mancho***
- ➔ **Antonio Massanell Lavilla**
- ➔ **Alfonso Ferrari Herrero**
- ➔ **Gonzalo Hinojosa Fernández de Angulo**
- ➔ **Pablo Isla Álvarez de Tejera**

*Committee Chairman

Duties of the Committee

To promote the implementation of the Company's values

- To see that the values are aligned with Telefónica's identity.
- To oversee the incorporation of the values into the Company's operations, especially in the areas linked to management of intangible assets.
- To determine the extent to which stakeholders identify with the values.

To promote the development of the Corporate Reputation project

- To monitor reputational risks.
- To monitor stakeholder perception.
- To forward the findings of reputation studies to the Board of Directors.
- To foster Telefónica's participation in initiatives and forums, especially the monitoring of the Company's presence in socially responsible investment indices.

To ensure that Telefónica's conduct is ethical and responsible

- To supervise the dissemination and implementation of the Business Principles across all the business lines and in each country where the Group operates.
- To promote the adoption of common corporate sustainability policies, based on the Principles.

To promote the verification of the Sustainability Report and the Group's balance sheet of intangible assets

- To initiate the measurement of Telefónica's performance in the management of intangible assets (ethics, values, sustainability, identity, etc....).
- To promote transparency via Sustainability Reports, monitoring the scorecard for indicators that affect relations with Telefónica's stakeholders.
- To report the results to the Board of Directors, and to submit the report on those results to the governing bodies.
- To receive the opinions of the external consultants on the verification of the Sustainability Reports.



Triple bottom line



Triple Bottom Line
Economic dimension



Driver
of progress



In 2011, despite the macroeconomic turmoil, the role played by Telefónica as a driver of progress increased by 8.3% and contributed to the economic, technological and social development of the communities in which we operate.

The increase in revenues in 2011 was due both to customer revenue and strategic disposals.

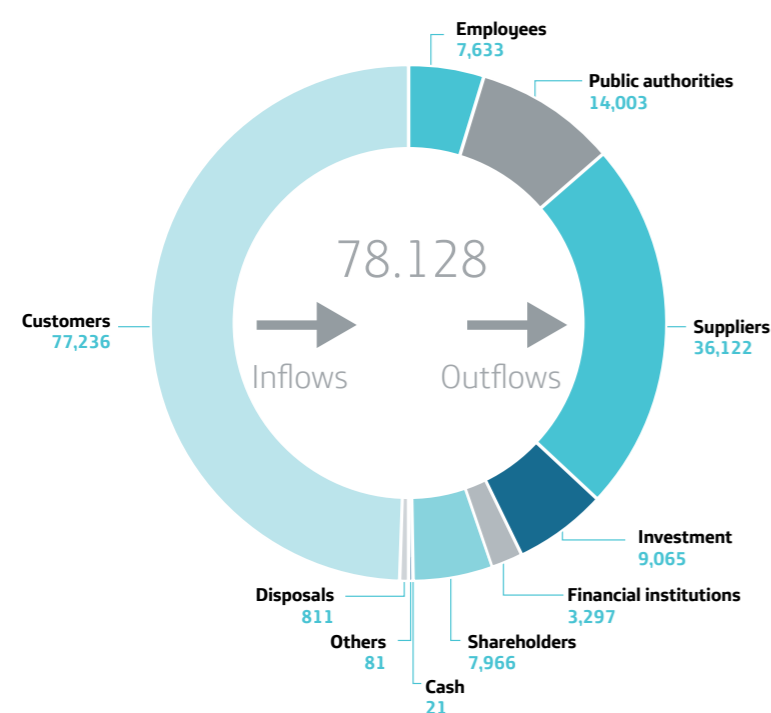
The strong performance in customer revenues (+6.0%) was a result of the extremely diversified range of services and of general expansion in Latin America, which has become the most important area for Telefónica in terms of growth. From the commercial point of view, there was a major increase in mobile data for all markets in the performance of customer adds.

Spain was the worst performer on the revenue side, where income fell by 7.6% as a result of fierce market competition and the worsening economic situation there. Nonetheless, despite these issues the company's clear commitment to sustainability means around €3 billion will be invested over this difficult year in the roll-out of high-speed broadband networks and the purchase of the best spectrum in the market, which equates to 17% of sales for the period.

2011 was noteworthy for the major increase in disposals (157.1%). This was mainly through the sale of non-strategic towers as part of a series of business initiatives to optimise the use of capital, a reduction in our economic exposure in Portugal Telecom and the sale of a number of non-strategic assets by Telefónica Spain.

The increase in revenues compared to last year, despite fierce competition and negative regulation, enabled the company to increase resources for all stakeholders: employees(+7.5%), shareholders (+11.7%), suppliers (+6.6%), financial institutions (+8.1%) and public administrations (+6.0%), and to devote more resources to investments that will ensure the company's future (+1.6%). Furthermore, €140 million was invested in the community, an amount that represents 0.18% of revenue for the period.

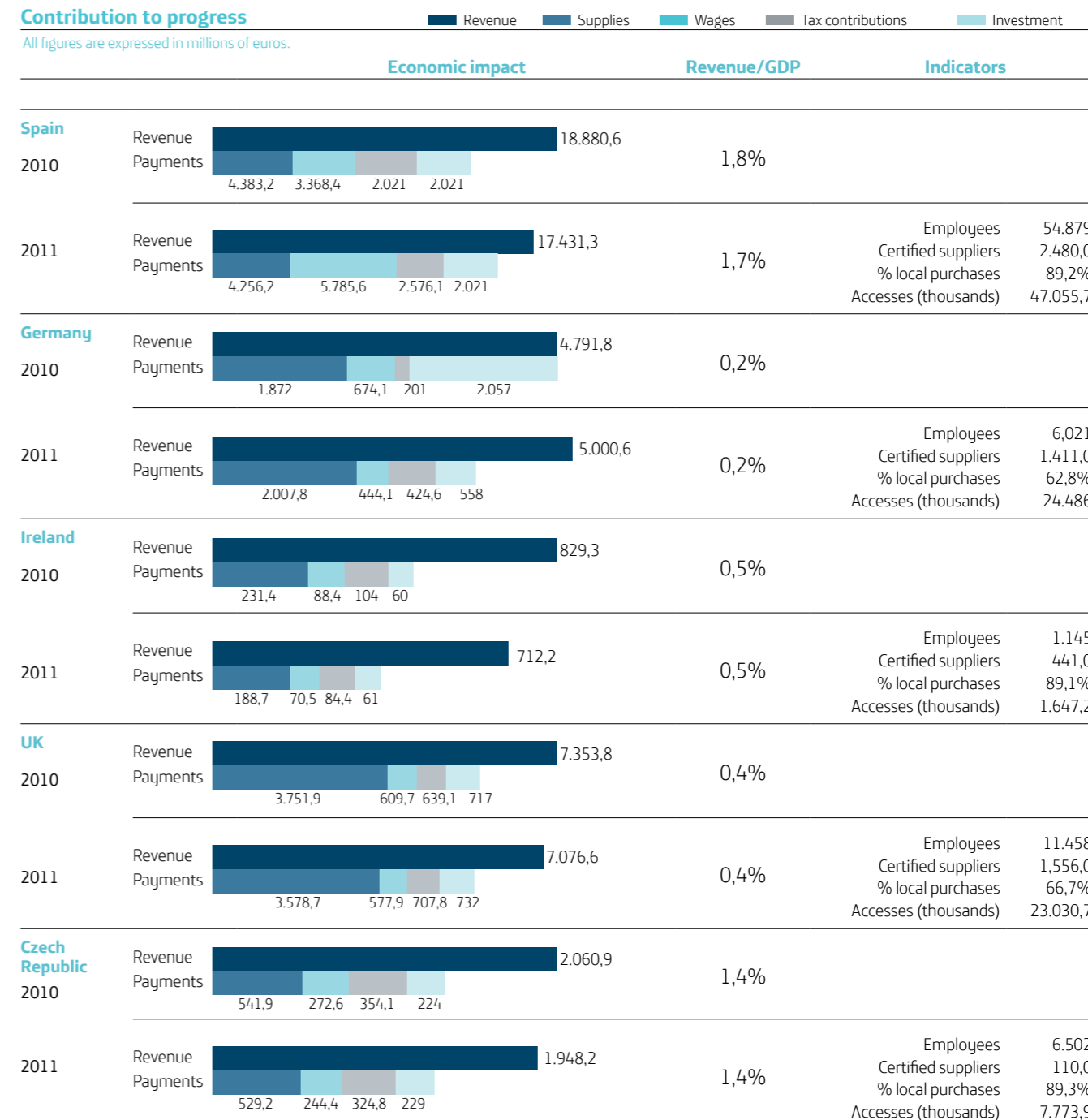
Driver of progress



Notes:
All figures are expressed in millions of euros.
The information in this chart has been calculated based on payment assumptions and taking into account the scope of consolidation in the financial statements of Telefónica.
Figures for employee salaries do not match those shown in the indicator table, in which they are given net of Social Security payments.

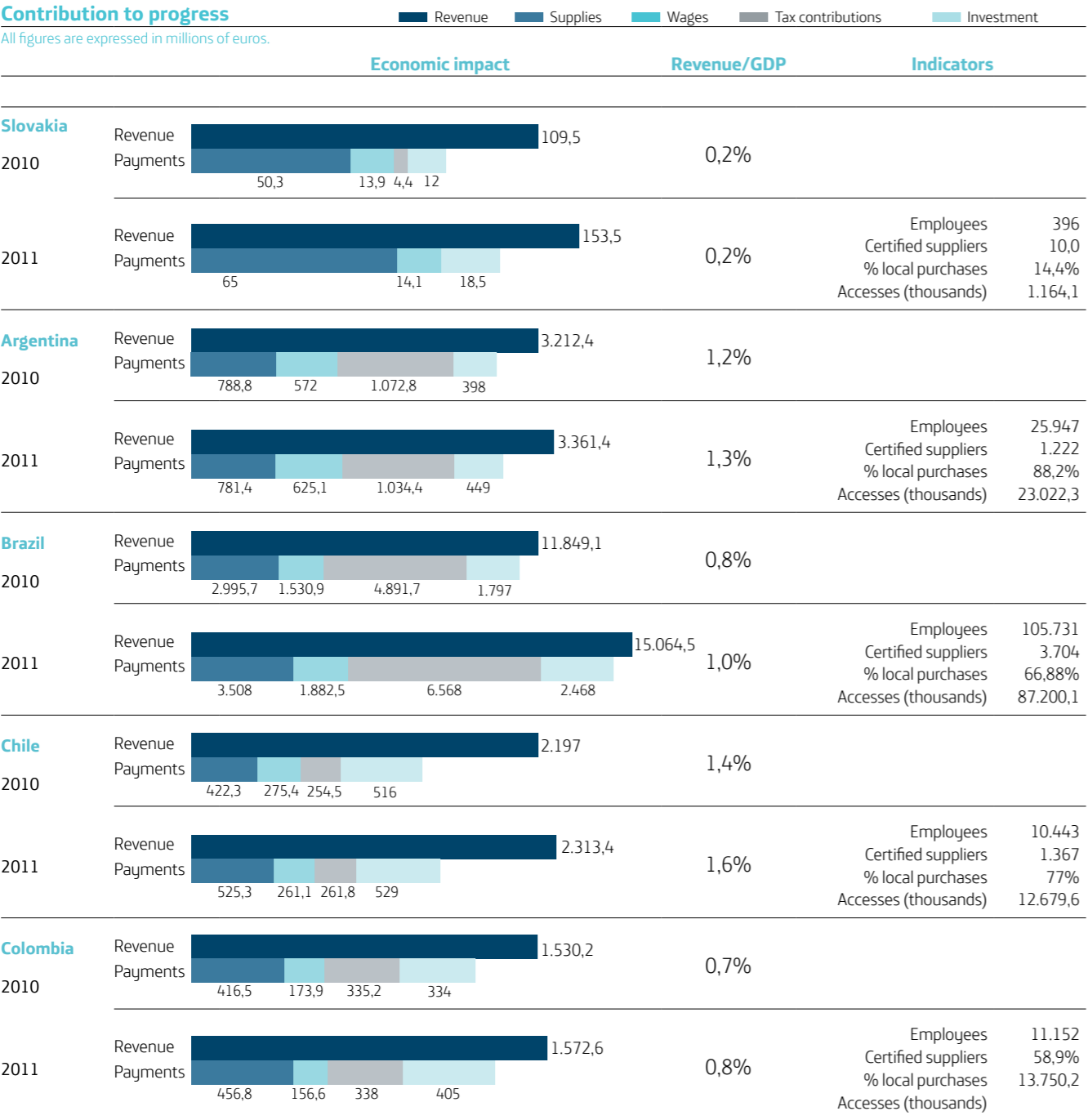
Contribution to progress

All figures are expressed in millions of euros.



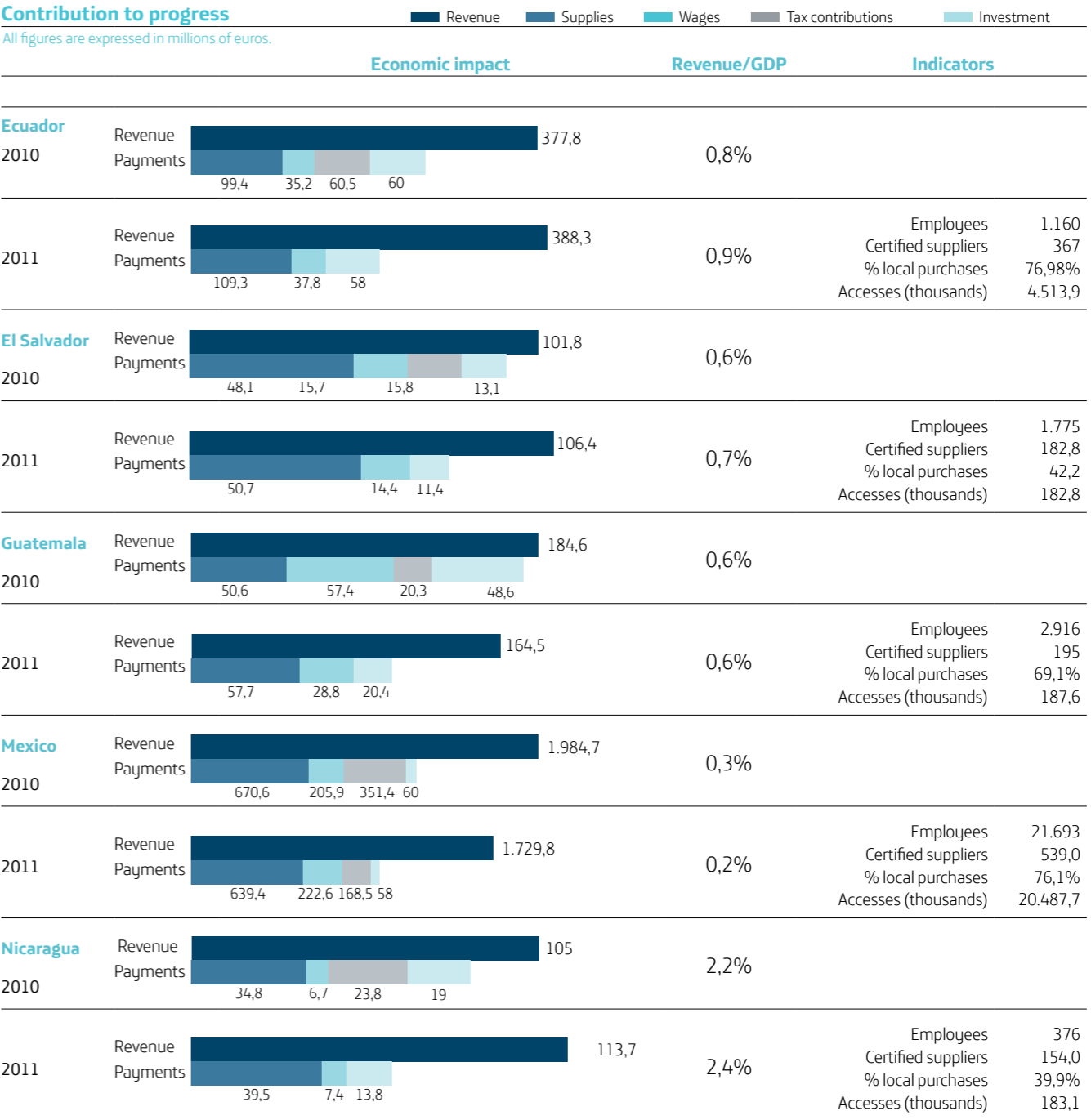
Contribution to progress

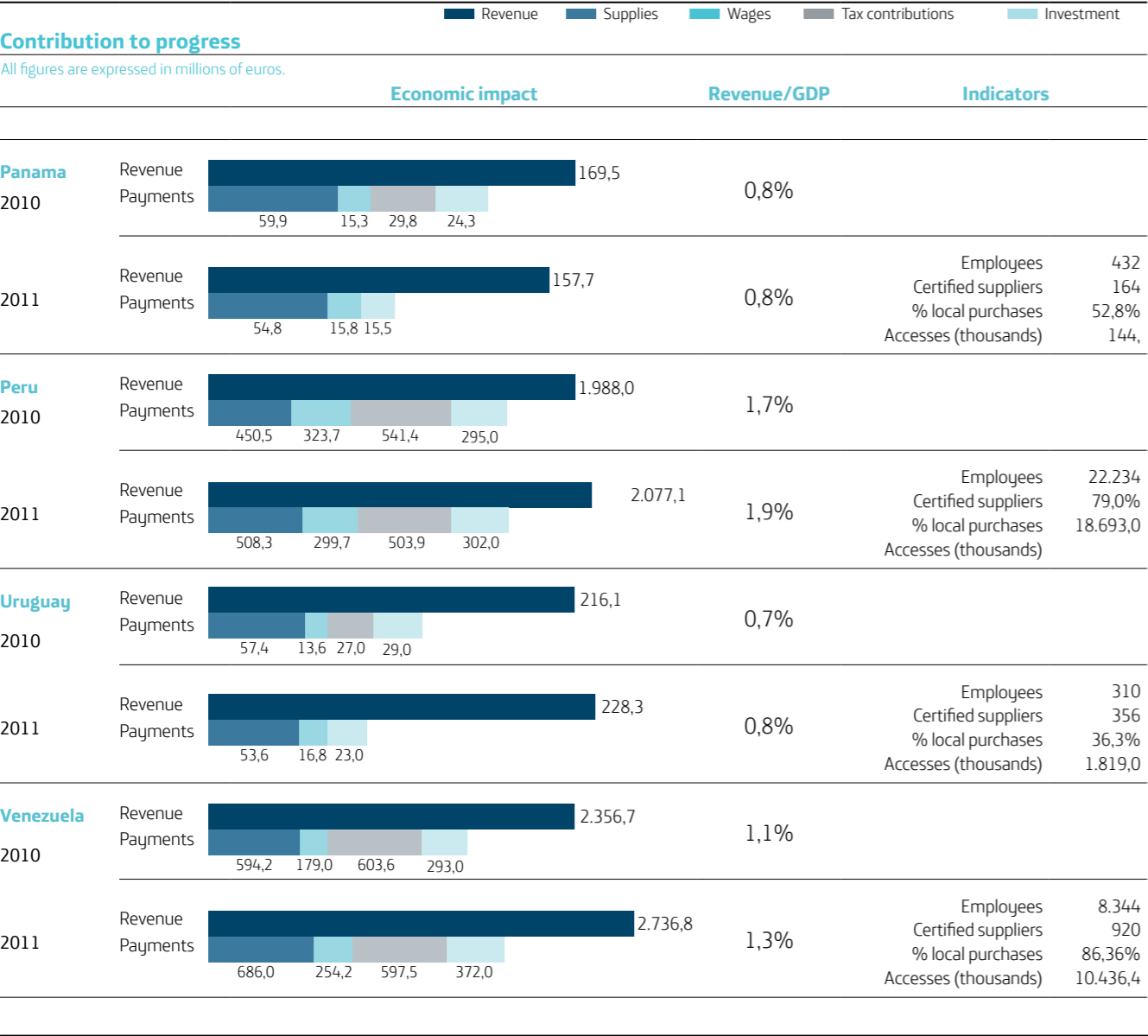
All figures are expressed in millions of euros.



Contribution to progress

All figures are expressed in millions of euros.





Telefónica as a responsible investor (SRI)

In the course of 2011, investments considered as SRI/ESG, with specific environmental, social and good governance criteria in the Telefónica employment pension funds, remained at around 2% of the securities portfolio, which is above the average offered by Spanish savings institutions. Most of these financial assets are direct investments in social rented housing societies, environmental and clean energy activities and ESG-criteria managed funds.

Fonditel Pensiones EGFP, S.A. manages the Telefónica Spain employee pension funds. It is one of the most important pension funds in its field and a founding member of SPAINSIF, the Spanish socially responsible investment forum which has the following lines of action:

1. The promotion of SRI to generate supply and demand in Spain.
2. The transmission of a wide-ranging and independent vision on the different issues that influence the promotion of SRI in Spain.
3. The drawing up of a strategic plan with three-year targets and annual reviews for the promotion of SRI in Spain.



Socially Responsible Investment

Valuation at 31/12/2011, in millions of € *

	ETE, F.P.	Fonditel B. F.P.	Total Pension Funds Telefónica Group
Lazora S.A.	13,45	=	13,45
Lazora II S.A.	20,45	1,51	21,96
Foresta individual I S.A.	2,22	2,22	4,44
Eolia Renovables	=	3,26	3,26
CA AM ActionsEurope ISR	7,30	=	7,30
CA AM Actions Durables	=	2,83	2,83
F. Sam Sustainability Water	6,38	=	6,38
F.PF (Lux) Water	5,13	=	5,13
Jupiter Ecology Fund	5,44	=	5,44
Total	60,44	9,83	70,27
Assets	2.836,03	271,07	3.107,09
% SRI	2,13%	3,62%	2,26%

Information according to the 2011 audited financial statements of pension funds.

Risk management



The model defined by the Telefónica Group supplies a high level of awareness and guarantees more efficient allocation of resources to manage the risks identified.

The Telefónica Group's Corporate Risk Management Policy and Procedure are based on a set of defined principles as the result of experience, best practices and Corporate Good Governance recommendations, and contribute to constantly improving business performance.

The Corporate Risk Management Procedure ensures the model is consistent throughout the operators of the Telefónica Group, and clearly establishes approval and reporting channels for information in connection with risk.

Four separate risk categories have been defined at the Telefónica Group: Business Risks, Financial Risks, Operational Risks and Global Risks.

Reputational Risks and risks associated with the breach of Telefónica's Business Principles form part of the fourth category and of the corporate risk management model, containing risk events which can affect Telefónica as a global company and which cut across the entire operation.

Reputational Risks

All risks identified may have a greater or lesser impact on reputation, depending on their origins and magnitude. We distinguish these firstly as "Pure Reputational Risks", which chiefly arise from

breaches of our Business Principles in the broadest sense. Secondly, "Derivative Reputational Risks" are operational risks that have an impact on the reputation of the company.

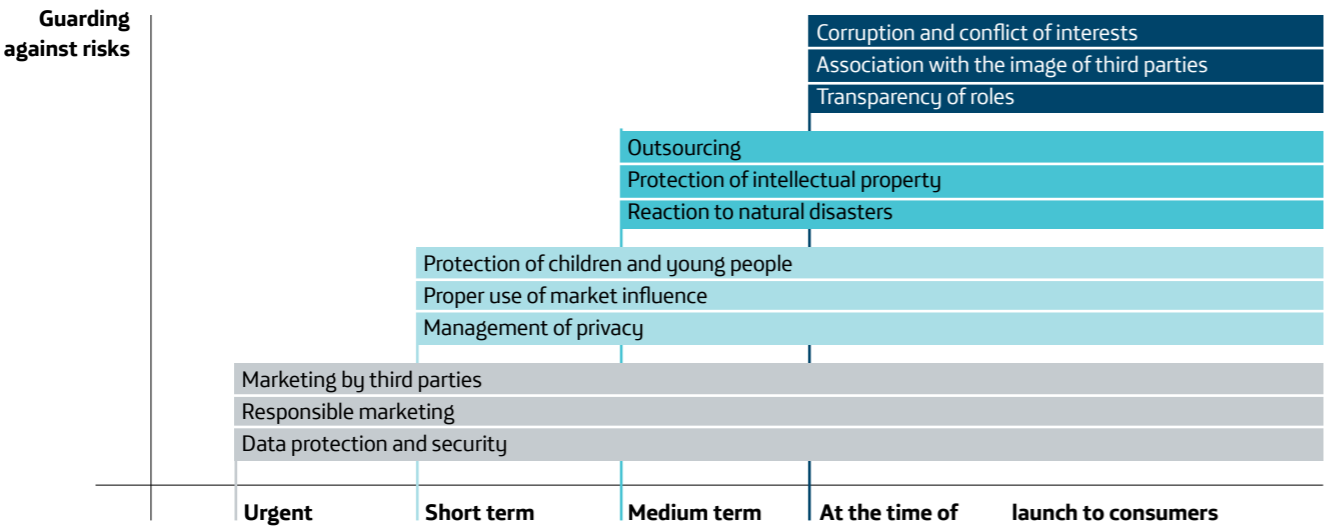
Pure Reputational Risks

We have a simple and effective management model to manage risks associated with our Business Principles (hereinafter BP) and their impact on reputation, based on identifying, evaluating and responding to risks, and following up projects relating both to them and to reputation management.

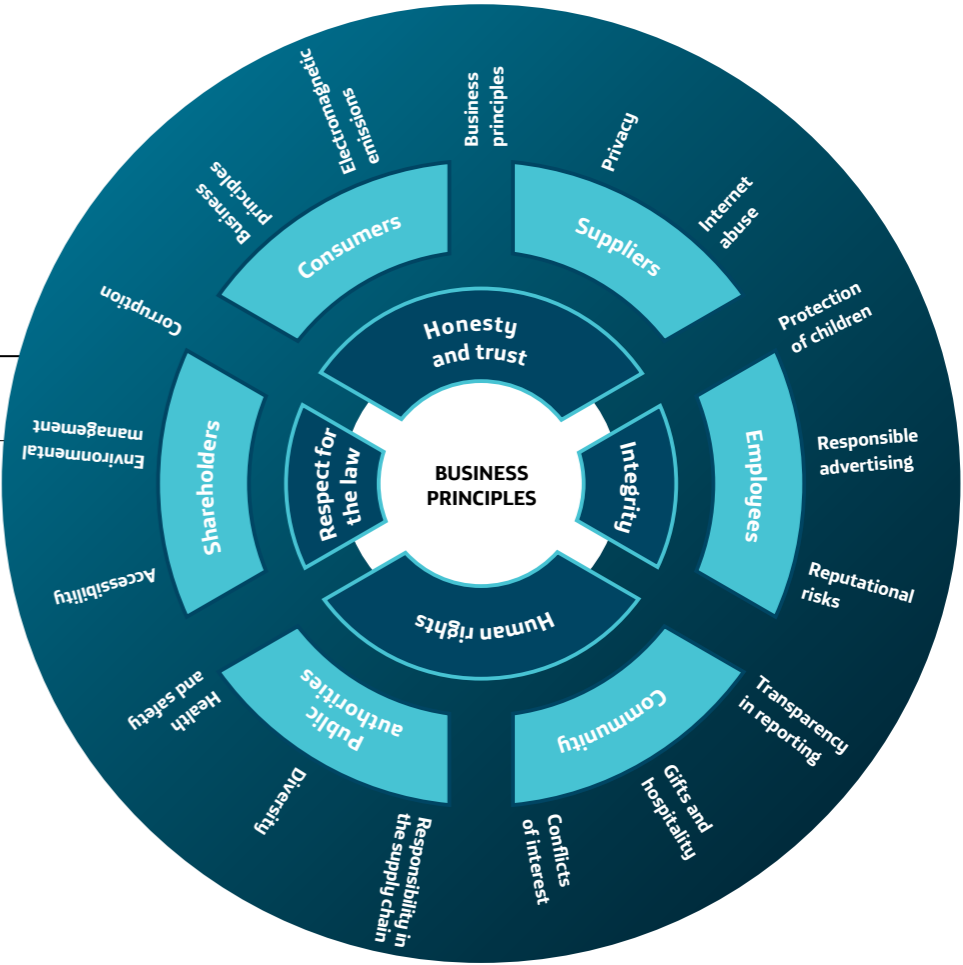
Our Business Principles Office, set up in 2006, is in charge of ensuring that these principles are met, and of developing policies and procedures to prevent risks. It is composed of representatives from the Human Resources and Internal Audit divisions, the General Secretary's office and the General Technical Secretariat for the Chairman's Office, and has a representative from each of Telefónica's operating regions (Spain, Latin America and Europe). In order to carry out its work, it is supported by similar structures in each of the countries in which we operate.

The Business Principles Office, as part of its role of day-to-day management of the code of conduct, is responsible for identifying and evaluating risks associated with breach of the principles from the point of view of both economic impact and reputational impact.

Priorities for management of Reputational Risks



1. Priority to these three blocks would become immediate following the definition and launch of services subject to major alliances with other companies or official bodies in the various countries in which the company operates. If the products were defined today and launched in the short term, this block would move to the "Urgent" zone.



Courses of action taken by the Business Principles Office

The Business Principles Office implements policies and procedures to prevent risks

This process, in coordination with the global risk area, is carried out on a global basis and also locally through the Business Principles Offices in each country.

In 2009 a specific projects unit was set up with the functions described to globally manage identified risks, define improvement plans and risk-mitigation projects, and draw up regulations and procedures to ensure proper management and consistency of terms and plans. This company-wide and cross-disciplinary unit, which works with and coordinates different areas of the company, is responsible for defining external positioning, standardising and setting out procedures, in addition to implementing proper internal conduct relating to responsibility in the supply chain, human rights, integrity, privacy and data protection, health and safety, electromagnetic fields, protection of children, responsible advertising and diversity.

A number of key performance indicators relevant to all projects are included so that they can be monitored by the Office. A half-yearly report is made to the BP Office on the monitoring and progress of projects, to enable performances to be monitored and evaluated.

Reputational Risks as a result of operations

In 2011 we continued to analyse the company's reputational risks, with a particular focus on those which could arise as a result of offering our new digital services, in due consideration of the strategic value of the services for Telefónica's future.

The main aim of the analysis was to obtain information that would help us to reduce as much as possible the company's reputational risk from the outset, by identifying events that could arise as a result of the company's own operations and that could be avoided at source (design of the services and accompanying processes, business models and relationships with partners).

The risk groups covered by the detailed analysis were: privacy and data protection, protection of children, protection of intellectual property, proper use of market influence, corruption, outsourcing, reaction to natural disasters, responsible marketing, responsible marketing by third parties, transparency of the role and responsibilities of Telefónica and its partners, and risks of being associated with the image of third parties.

Depending on the likelihood and ultimate impact of the different risk groups on the company's reputation, the following prioritisation was given to projects to prevent reputational risks from the outset.

In the course of 2012, this project produced a work procedure which enables the systematic analysis of reputational risks to be implemented during processes creating new services, thus automatically strengthening risk prevention from the outset.

Code of Conduct

The Company's code of ethics, expressed in its Business Principles, has governed Telefónica's internal operations and relationships with its surroundings since 2007 and has also served as a key feature of staff training.

At Telefónica we remain committed to full and transparent management through our Business Principles, a code of ethics that inspires and defines the way in which we carry out our business and our relationship with all stakeholders.

These principles form the basic standards from which defined policies and regulations to be observed in our daily activities emerge.

Our Business Principles

Since they were approved in 2007, our Business Principles have enabled us to respond to the ever-growing concerns over matters related to integrity and transparency vis-à-vis institutions and official bodies, and to compete in socially responsible investment indexes such as, among others, the Dow Jones Sustainability Index and the FTSE4Good Index.

From an internal point of view, our Business Principles have also been a "guide" which helps us in our day-to-day business, and strengthens the feeling of belonging to a great organisation that is ethical and responsible, helping to create a better place to work.

In the course of 2011, work was carried out with the Telefónica Brazil team to integrate Vivo's code of ethics into Telefónica's Business Principles. To this end a team was created with a defined work schedule for approval in 2012.

An exhaustive analysis was undertaken of the two codes (the Business Principles and the Vivo Code of Ethics), with the aim of identifying synergies between the two, and also areas where they could act as complements.

Projects being developed at the corporate and local Business Principles Offices include: the use of the Business Principles as the code of ethics in Brazil, under the Telefónica brand name; further development of the Business Principles in relation to dress code, exclusivity, collaboration and leadership, through regulations at country level; and the development of aspects regarding diversity at a country level under the umbrella of Business Principles.

These will be approved in the course of 2012 by the corporate Business Principles Office, the local Business Principles Office and the corresponding management bodies.

Business Principles Training

In 2011 Telefónica continued instructing its professionals in connection with the Business Principles through its *online training course*. The aim of this compulsory training course is to make all employees aware of the company's code of ethics and for them to reflect on the importance of the Telefónica Group having ethical standards that help it carry out its day-to-day work.

By December 2011 almost 56,000 employees had received training, representing 19% of the total headcount² of the Telefónica Group.

Employees trained in Business Principles

	December 2009	December 2010	December 2011
Telefónica Spain	34,3%	34,88%	48,36%
Telefónica Europe	80,1%	89,58%	90,54%
Telefónica Latin America	67,2%	69,32%	38,19%

Confidential Hotline

All Telefónica employees have the chance to ask questions, seek advice and make enquiries, either anonymously or in person, on matters relating to compliance with Business Principles and associated policies through confidential help channels on the website. Suppliers and other interested parties can also access confidential channels through portals set up for relations with the various stakeholders.

Since the channels were set up, they have received 264 communications, largely concerning work-related complaints. These were all sent to and dealt with by the Business Principles Office and, if any irregularities were identified, by the Audit and Control Committee.

In 2011 a total of **91 complaints** were filed. Of the 73 cases now closed, 11 were found to be valid, and the measures taken included 5 punitive dismissals and 2 official warnings.



Business Principles Office

At Telefónica, the Business Principles Office safeguards the implementation and observance of the code of ethics, identifies and develops regulations, and supports employees by answering their doubts, complaints or allegations.

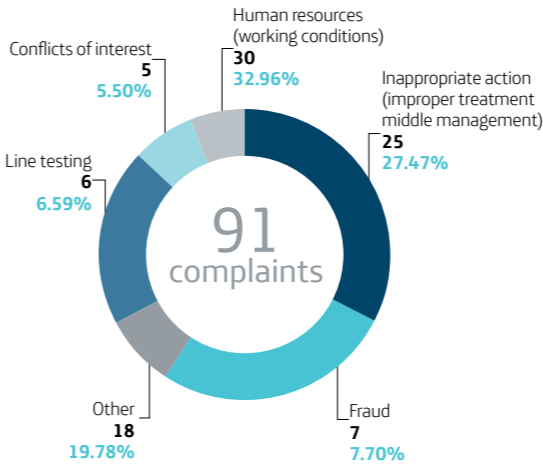
The Office, which reports to the Board of Directors via the Human Resources and Corporate Reputation and Responsibility Committee, comprises representatives from the business areas of Human Resources, Internal Audit, General Legal Secretariat and General Secretariat to the Chairman's Office at Telefónica. It also has a representative from each of the regions where the Telefónica Group is present: Spain, Latin America and Europe.

In addition to this Office, in order to assist implementation of the Principles, Latin America has offices in Argentina, Brazil, Chile, Colombia, Ecuador, El Salvador, Mexico, Panama, Peru, Uruguay and Venezuela, with the same composition as the Corporate Business Principles Office. Europe has a Compliance Officer for all Telefónica Europe's operations as the person responsible for ensuring compliance with the Principles in each country.

Functions of the Business Principles Office:

- ➔ **Day-to-day management of the Code of Ethics** through training, communication and the resolution of communications received via confidential channels.
- ➔ **Identification and evaluation of risks associated** with the Business Principles in the Global Risk Management Model.
- ➔ **Definition of action plans** for the main risk areas identified, via the Projects Unit created in 2009 as part of the Business Principles Office. In addition to deploying proper internal conduct measures (rules, procedures etc.), it also defines the Telefónica Group's position on these issues (statement or policy).

Distribution of complaints



1. raining information is an estimate of fixed and mobile business in accordance with the average headcount with the number of employees trained in the past. The lower figure in Latin America was due to the inclusion of a new company, Vivo, in the measurement.



In 2011 the Office held four meetings, which were attended by representatives from all the departments and areas involved, regional representatives and those responsible for the areas of identified risk. At the meetings, an update was given on the training situation, the main complaints and questions of employees, the ratification of regulations resulting from the Business Principles and the monitoring of defined objectives for each of the areas of identified risk.

Integrity and Transparency

At Telefónica we have developed a series of organisational, policy-related and monitoring features that comprise a proper control environment which does not tolerate corruption.

Our Business Principles cover the principles of conflict of interest, corruption, the prohibition on accepting gifts or bribes and the principle of political neutrality. Concerning the principle of political neutrality, an analysis of payments made reveals no records of any donations to political parties in 2011.

On the basis of the United Nations Convention against Corruption, which the Telefónica Group has signed, we consider the following to be corruption:

- **The deliberate falsification of financial-accounting** information (failure to record accounts in books, failure to record transactions or recording them incorrectly, recording non-existent expenditure, recording expenses but incorrectly identifying the purpose thereof, the use of false supporting documents or the intentional destruction of bookkeeping documents before the earliest legal destruction date provided by law).

- **Moneylaundering.**
- **Giving or receiving bribes.**
- **Illicit enrichment or embezzlement** of company funds or assets.
- **The acquisition,** use, transfer or concealment of assets in full knowledge that they are the proceeds of crime.
- **Assisting in committing crimes** or concealing them.
- **Obstruction of justice.**

Almost 1,000 Internal Audits and Inspections were carried out at the Group in 2011. Of these, approximately:

- 21% partially or fully analysed the processes involved in the expenses and investment cycle (purchases, payments to third parties, payments to employees, logistics and warehouse management, the investor process and asset management, discounts and customer returns) which are the processes in which the greatest portion of risk discussed is found.
- 22% were financial audits or audits of information systems aimed at reviewing the existence and effectiveness of controls on the disclosure of information process in business processes that feed the main accounts of the Group and in accounting processes. The Telefónica Group is legally obliged to carry out these reviews each year, as it is listed on the New York Stock Exchange and must apply the Sarbanes-Oxley Act. This means the Group has issued a certification without significant flaws or weaknesses and that the External Auditor has borne witness to both the results and effectiveness of the review process.

Telefónica's Business Principles contemplate conflicts of interest, corruption, non-acceptance of gifts and bribes, and political neutrality

- 10% of operations were directed specifically towards preventing fraud, investigating complaints and reviewing personal conduct.
- 6% of reports were aimed at verifying compliance with other legal obligations (employment, data protection, taxation etc.).

This audit work was carried out in all companies and countries in which the Group has interests, mainly in Spain, the UK, Germany, Republic of Ireland, Czech Republic, Slovakia, Brazil, Argentina, Chile, Peru, Colombia, Venezuela, Ecuador, Mexico, El Salvador, Guatemala, Nicaragua, Panama and the US.

The audit work revealed 66 cases of abuse or appropriation of company assets, which resulted in 79 dismissals. They were all of relatively minor significance and none involved senior executives of the Group or management of the companies concerned.

In general, management response was appropriate and was forthcoming within a reasonable timeframe, which encourages a good, ongoing, general atmosphere of internal control.

Training in anti-corruption policies and procedures

All Group employees know and/or have access to the Business Principles text (with values approved by the Board of Directors) and the corporate and individual regulations of the companies which set out the rules governing decision-taking processes, purchases and contracting, payments, warehouse management etc.

Furthermore, the general atmosphere of control is an aspect that has been highlighted by the professionals who work at Telefónica. It must be emphasised that the Group has a number of features producing a suitable control environment, in which the institutional message leaves no doubt that it will not tolerate corruption or illegality. Specifically:

- **Board Committees:**
 - An Audit and Control Committee reporting to the Board of Directors of Telefónica S.A. and others at listed companies. The Committee receives information from the External Auditor, the Internal Auditor and the Finance and Management Control department.

- A Human Resources and Corporate Reputation and Responsibility Committee reporting to the Board of Directors of Telefónica S.A.

Specific Organisational Units:

- A Centralised Inspection Unit specialising in fraud prevention and investigating complaints and other situations.
- Audit Units in all countries where the Group has significant interests.
- The Executive Commission of the Board of Directors approved the Audit Function statute as express recognition of its role and explicit support of its responsibility, independence and adequate resources.

Pursuant to the list of tax havens stipulated in Additional Provision One of Law 36/2006 on measures for the prevention of tax fraud and and following the changes arising as a result of the entry into force of double taxation and tax information exchange agreements, Telefónica conducts no business activity in tax havens.

2011 Corporate Sustainability Report

Indicator	GRI	Scope
Nº employees dismissed for breach of the Business Principles (on the basis of complaints received through the Confidential Hotline)	S04	5
Total complaints through the Confidential Hotline in relation to the Business Principles, and measures adopted in relation to those admitted	S04	91
Nº of corruption incidents investigated by the Business Principles Office	S04	2
Nº of incidents of discrimination by the Business Principles Office	HR4	There were no cases of discrimination

Management of sustainable relationships with our customers



Improving the customer experience and increasing the customer's emotional attachment to our brands is one of the fundamental strategic initiatives we have undertaken to establish ourselves as a world leader in communications in the digital world.

The effort we have made to improve the customer experience and increase their emotional attachment to our brands is one of the fundamental strategic initiatives we have undertaken to establish ourselves as a world leader in communications in the digital world. These initiatives have culminated in the launch of a number of proposals aimed at offering a fair deal and distinguish us in the way we relate to our customers, in addition to initiatives to continuously improve our customer service.

Campaigns such as "Thinking of You" (UK) or "We are changing for your Business" (CZ) are just a few of the examples demonstrating how we focus our value proposal on transparent communication, simplified offers, launch of competitive flexible rates, and priority to our existing customers.

These value proposals have been accompanied by a number of plans to continuously improve customer service. One good example is the implementation of tools to measure customer satisfaction when they interact with our contact channels, in shops, customer service centres and websites. This year we also introduced a web chat support tool which is showing very positive results. Once the emotional attachment with the customer had been built through the brand developed by the Customer programme throughout 2010, we gained a better understanding of our customers in 2011 through Business Intelligence and CRM with the intention of anticipating customer needs, sending a single consistent message through our channels, and making an offer to fit the customer's requirements.

At Telefónica we have cemented a culture of sharing and working together, which in 2011 enabled us to exchange best working commercial practices with customer experience, and export them to the countries where we operate.

In **Latin America** a number of models have been set up aimed at predicting claims, optimising the selection process for areas to improve, channel management, Mobile Technical Service, management of claims and the methodology to optimise Internet investment.

With respect to Business Intelligence in Latin America, we have standardised a management model that allows us to have all

operators working in the same way (it was rolled out in Mexico, Colombia - fixed line and mobile - Venezuela, Central America and Ecuador, and it will be implemented in other countries in the region in 2012). We have also continued to work on the Consolidated Customer Register which allows rapid access to the 360° profile of the convergent customer, and on the Campaign Manager solution. In 2011 we rolled out the same out-bound mass campaign management solution in Argentina, Colombia mobile, Peru mobile, Central America and Venezuela. We have also started to define and plan the deployment of optimisation modules for basic campaigns and in-bound campaigns.

Our customers by numbers

In an environment marked by difficult macroeconomic conditions, fierce competition and the adverse effects of regulation, Telefónica continued to increase its customer base, especially in the second half of the year, as a result of the business re-focusing measures we introduced in the main countries where we operate.

The number of customers grew by almost 7.0% year-on-year in organic terms, standing at 306.6 million at the end of 2011, significantly boosted by contract and mobile broadband customers.

In 2011 we consolidated a work culture based on cooperation and sharing that enabled us to exchange the best commercial practices and customer experiences

By regions, the main highlight was Latin America, which, with year-on-year organic growth of 10.0% in terms of accesses, consolidated its position as the main contributor to the expansion of Telefónica's accesses.

There were 238.7 million mobile customers in 2011, which represents year-on-year organic growth of 8.0%. Growth in this division speeded up in the second half of the year, nearly doubling that of the first half (13 million new customers).

The importance that Telefónica attaches to sustainable relationships with our customers is reflected in a sustained increase in the contract area (+11.0% year-on-year), which accounted for almost a third of total wireless accesses and net additions were almost 40.0% in 2011, with more than 100.0% increases in Spain and Europe as a whole. In Latin America we still lead the sector in the number of contract customers.

The number of broadband mobile customers, one of the market sectors likely to show the most future growth, stood at more than 38 million at the end of 2011, meaning year-on-year growth of 61.0%, and represents average penetration of 16.0% of the total number of our mobile customer base, 31.0% in Europe and 10.0% in Latin America.

Retail fixed broadband customers reached a total of 18.0 million at the end of 2011 (up 5.0% year-on-year). The strategy of bundling voice services, wide band and television has proven to be a key lever in retaining our customers, which in Spain and Latin America is leading to sustained growth in the percentage of fixed broadband accesses with bundles of two or three offer packages.

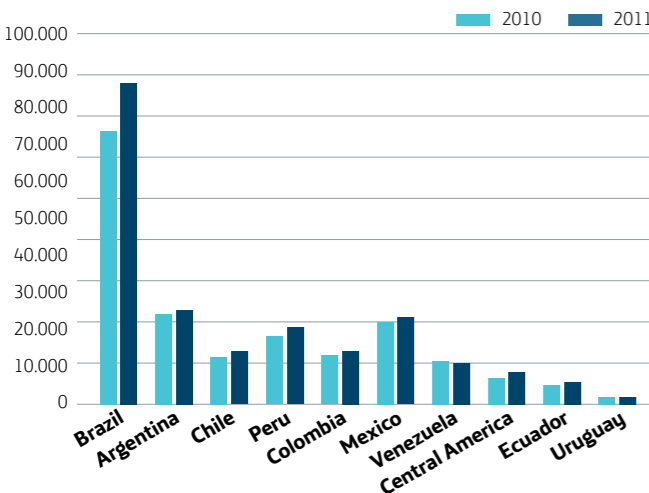
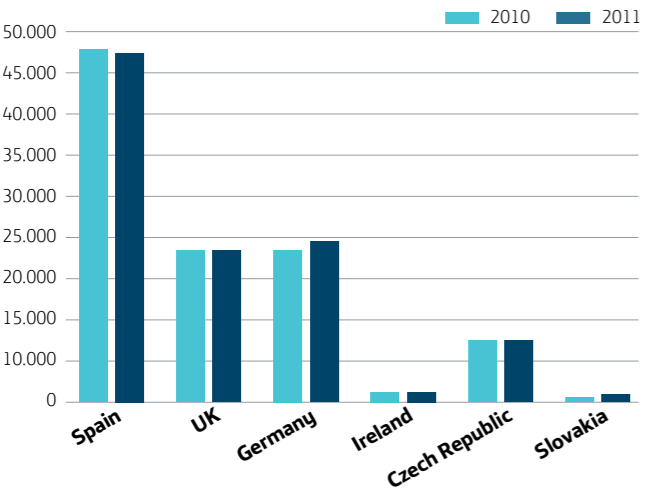
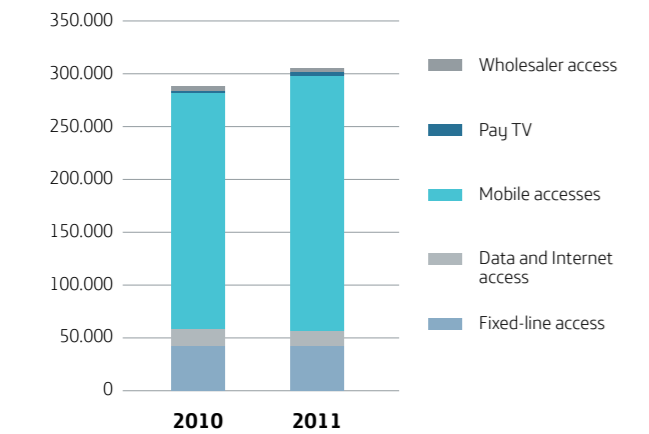
The number of Pay TV accesses stood at 3.3 million in 2011 (+19.0% year-on-year), a figure representing a pick-up in the growth rate, chiefly due to successful commercial repositioning in the Latin American market, where net additions in 2011 tripled those in 2010, thanks to the inclusion of TVA's Brazilian customers as of June and the upbeat commercial performance in Spain during the second half of the year.

Traditional fixed line accesses totalled 40.1 million, down 3.0% year-on-year. This decline remained stable throughout the year.



In thousands	December		
	2011	2010	% Chg.
End customer accesses	301,311.8	282,994.9	6.5
Fixed line accesses (1)	40,119.2	41,355.7	(3.0)
Data and internet accesses	19,134.2	18,611.4	2.8
Narrow band	909.2	1,314.1	(30.8)
Broadband (2)	18,066.3	17,129.6	5.5
Other (3)	158.7	167.8	(5.4)
Mobile accesses	238,748.6	220,240.5	8.4
Prepay	162,246.9	151,273.9	7.3
Contract	76,501.7	68,966.6	10.9
Pay TV (4)	3,309.9	2,787.4	18.7
Wholesale accesses	5,296.0	4,637.4	14.2
Leased loops	2,928.7	2,529.2	15.8
Shared loop	205.0	264.0	(22.3)
Unbundled loop	2,723.7	2,265.3	20.2
Wholesale ADSL (5)	849.3	687.4	23.5
Other (6)	1,518.0	1,420.7	6.8
Total Accesses	306,607.8	287,632.3	6.6

Notes:
- Year-on-year access growth has been affected by the inclusion of HanseNet accesses from March 2010 and the exclusion of Manx Telecom accesses from 1 July, 2010.
(1) PSTN (including Public Use Telephony) x1; ISDN Basic Access x1; ISDN Primary Access and Digital Accesses 2/6 x30. Includes access for internal use. Includes the total number of "fixed wireless" accesses. Includes VoIP and Naked ADSL.
(2) ADSL, satellite, fibre-optic, cable modem and broadband circuits.
(3) Rest of retail circuits that are not broadband
(4) Includes 151,000 TVA clients from June 2011.
(5) Includes rented loops by T. Germany and T. UK.
(6) Circuits whose end customers are operators. Includes Wholesale Rental of Telefónica Line (AMLT) in Spain.



Customer Satisfaction

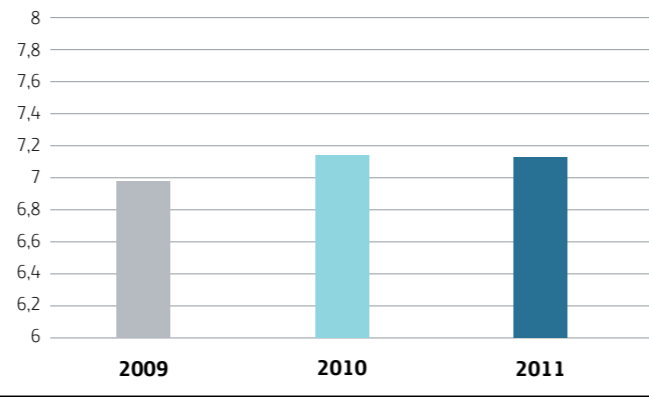
At Telefónica we attach a great deal of importance to the Customer Satisfaction Index. This is reflected at the highest echelons of the Company, as it is the Board of Directors which monitors its monthly trajectory at meetings. The Telefónica Customer Satisfaction Index (CSI) stood at 7.13 in 2011, and was unchanged from 2010. Telefónica thus ended the year as the market leader in customer satisfaction, with a 0.04 point advantage over our closest competitor.

Businesses where customer satisfaction levels improved the most in 2011 were corporate services in Brazil, followed by mobile business in El Salvador and Guatemala. Business performance in Panama and Venezuela fell.

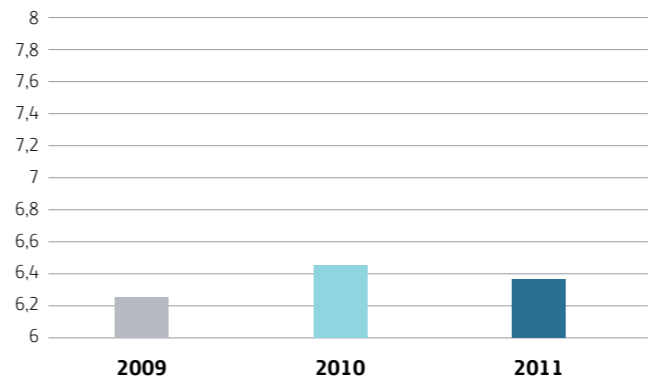
In **Europe**, the CSI stood at 6.76 points, giving us an advantage over our closest competitor of +0.12 points. We should point out that this figure is not comparable with the figure published in 2010 (7.39) after Spain was included in the European area following the restructuring carried out at Telefónica. If we make a pro-forma comparison, European CSI, including Spain, remained practically unchanged, falling slightly by 0.08 point. In **Latin America** figures also stayed stable, actually rising slightly by 0.06 point compared to the previous year. Some mention should be made of the sound performance by the company services index in Brazil.

The percentage of unsatisfied customers rose by 0.75 percentage point to 11.06%. It must be said that this number varies greatly from country to country, Slovakia providing a better indicator (1.2%) and Spain the worst (15.7%).

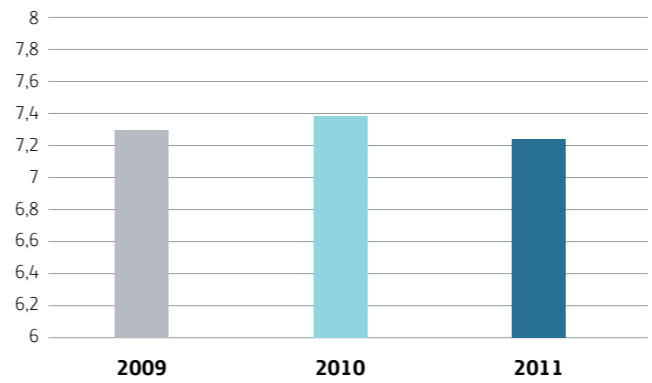
Telefónica



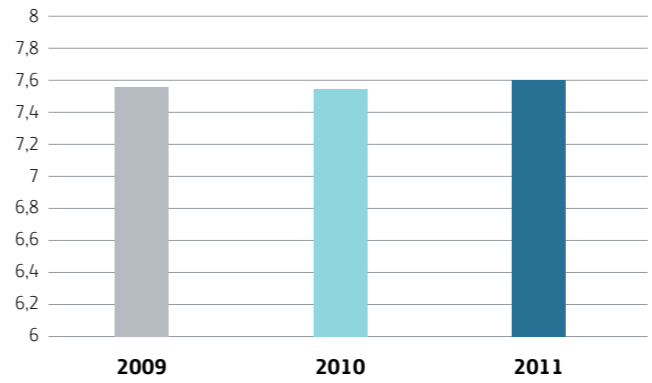
Spain



Europe



Latin America



The areas of business in which our customer satisfaction increased most in 2011 were services for companies in Brazil, followed by mobile business in El Salvador and Guatemala

Claims and the customer ombudsman service

Management of claims

Resolving claims satisfactorily is crucial to the company's reputation, and is a decisive factor when it comes to our customers rating our services. For these reasons, Telefónica has teams of people who are exclusively dedicated to take care of any claim in all countries where we operate, either by phone or mail.

It is important to remember that each country has very different criteria for measuring claims and as such are not comparable or amalgamable. The difference is due to the fact that data is verified according to different criteria used by different regulators in their respective countries, and they vary greatly from country to country. Whilst some countries only take into account second-resort claims (as in the UK, where they represented 0.2% of the customer base in 2011), others consider all calls to customer services centres have required action by the company (as in Spain, where they represented 4.1% of the customer base in 2011). According to data supplied by Spain's Telecommunications User Care Services, Movistar is the most highly valued broadband operator, with a claim index of only 1.56 for every 10,000 subscribers. This is half the figure recorded for the second-placed operator.

Click here for further information on claims in each country in which we operate. The trend in the number of claims in 2011 was affected by a number of factors:

- The increase in the use of Smartphone handsets meant that clients came into contact with services that were more complicated than those to which they were accustomed.
- The increase in our customer base and the catalogue of products and services we have launched on the market.
- The difficult general economic situation, which has led to customers scrutinising much more closely what they spend on our services.
- Increased customer awareness of their consumer rights in all markets where we operate.



Shops belonging to Telefónica's three brands (Vivo, in Brazil; O2 in Europe, excluding Spain; Movistar, in Spain and Latin America).

We have drawn up simple pricing plans, customised our offers, and dispensed with small print on bills



Customer Ombudsman Services

At Telefónica we make this department available to customers as an independent unit, for use by customers who have not received a satisfactory response from our business service areas. The decisions of the Customer Ombudsman Service are based on the principles of fairness and independence, and are binding for the business.

Customer ombudsman services are being implemented more or less rapidly in the different countries where we operate. In 2011, at the behest of the **Spanish** Customer Ombudsman Services office, the first Group Ombudsman meeting was held, with representatives from countries such as Brazil, Venezuela and Argentina. The aim was to share our best practice measures with everyone.

The most important step taken in this direction in 2011 was the extremely successful implementation of the POTR programme **in the Czech Republic** to improve the quality of customer-service operations. Following deployment of the programme, the number of complaints fell by 35.0% and claims in the Consumer Division fell by 54.0%. Customer satisfaction improved at the end of the year due to changes in the service model, the elimination of the customer services automatic answering machine, and an increase in communication campaigns. The Business Division showed the greatest improvement, with a 57.0% drop in the number of complaints and a 61.0% fall in the number of claims compared to 2010.

The implementation of POTR in the Czech Republic began with a full and detailed study of the main reasons for complaints and claims received. The analysis involved 250 employees, and identified 23 claim categories and 11 areas of top priority. Next a full and unified programme was implemented via the Telefónica Czech Republic customer service departments. From the simplification of the catalogue of services to improving the payment system, the POTR programme was one of the company's Executive Committee's top priorities in 2011. The results of the programme surpassed targets set at the start of 2011, and having found out the final figures, 86.0% of employees feel that POTR has significantly improved the treatment of Telefónica Czech Republic's customers.

Telefónica is the only telecommunications operator **in Spain** that has voluntarily created a second-instance facility with the characteristics of our Customer Ombudsman Service (COS). At COS Spain we handled 6,072 cases in 2011. 85.0% of the cases were settled in favour of the client. The main functions of COS are split into two parts: Claim management and the drawing up of business recommendations.

With regard to claim management, the SOC has improved its procedure for urgent resolutions in order to deal with cases that need to be handled more rapidly, establishing direct communication mechanisms with the relevant areas so that they may rapidly provide the customer with a satisfactory answer.

In 2011, customers who filed their claim using the electronic formula available on the website (approximately 30%) had the chance of receiving correspondence from the COS via email instead of a written letter.

Also, following requests from physically or technically challenged customers, an ocular channel has been opened providing a wealth of options for customers to send their claims.

The SOC, through the design and implementation of communication events, intended to provide an up-to-date vision of the relationship between Telefónica and its clients in various consumer forums. It participated in meetings organised by consumer bodies in a number of Spanish cities (Valencia, Huelva, Córdoba, Madrid, Asturias ...).

In its role of providing recommendations for improving the business, the SOC has concentrated this year on Fibre Optics, Mobile Broadband (both for Smartphones and other handsets) and on customer retention offers for mobile business. The SOC has taken an interest in information sent out to customers, clarity of billing and the effectiveness of retention processes, as they are sensitive issues that have a direct impact on customer satisfaction.

The SOC has kept the Quality & Customer Service Committee of the Board of Telefónica, S.A. abreast of its activities.

In Argentina, some of the initiatives worth highlighting are: The restructuring of the service model for Consumer organisations through the assignation of specialist executives, internal management of the root causes of the most frequent user claims, the implementation of prioritising systems for extremely serious cases and the introduction of controls and satisfaction surveys to ensure the quality of the initiatives.

Finally, in Venezuela we created the Customer Ombudsman portal for claims previously sent through normal customer service channels without receiving a satisfactory answer.

Tariffs and Bills

Throughout 2011 Telefónica continued to work on simplifying tariffs and clarity of bills with the aim of improving the customer experience, and thus correct the negative impact of customer dissatisfaction in these areas.

Having listened to customers' suggestions, we simplified the products and services portfolio, created easy pricing plans, personalised offers, and dispensed with the small print on the bill.

In Spain we made a new commercial offer to customers under the "single customer" concept which simplifies our offer and provides all the communication requirements. The new commercial strategy



is based on five principles that we conceived in the Company with the assistance of customers: Freedom of choice, transparency, personalisation, fair treatment and flexibility, so that customers may change tariffs as and when they wish.

In Ireland, we have drawn up competitive mobile tariffs of a modular structure for businesses. We also launched a new contract offer focused on simplicity, clarity, transparency, flexibility, and monetisation of the data service.

In Germany, we took note of the results of customer surveys to improve tariffs.

At Telefónica we know that our clients demand tariff structures that are not only simpler, but also more comparable between countries. For this reason we have drawn up an initiative at group level, and are increasing efforts to simplify tariffs that are offered in different countries, so that our clients can perceive better value. For example, Movistar Spain offers a tariff which includes 150 minutes of voice, unlimited SMS and 500MB of mobile broadband for €30/month, whilst O2 UK offers a tariff that includes 200 minutes of voice, unlimited SMS and 500mb of mobile broadband for £27/month, and O2 Germany

offers a tariff that includes 100 minutes of voice, 100 SMS and 300MB of mobile broadband for €24.99/month. Furthermore, best pricing practices have been shared to offer more attractive tariffs and products in all countries where we operate. An example could be the "Talk and Browse" tariffs that Movistar launched in Venezuela, and was then extended throughout the group. In general it is very difficult to compare products and tariffs between countries because the tariff structures are affected by numerous local factors, beyond Telefónica's control; competitors' operations, social and economic factors, regulatory factors, different cost structures, variety of services etc. On the basis of these restrictions, we are working to improve product and tariff consistency within the group.

Voluntary information codes

Telefónica Spain is a member of SELF, which means that in all its communications it complies with the SELF Code of Advertising Conduct, based on the Code of Good Advertising practises of the International Chamber of Commerce, certifying the Company's Corporate Social Responsibility in this area and that it has not been sanctioned in relation to compliance with the SELF Jury of Advertising resolutions.

The Gurus programme in the UK, dovetailing in all other European countries

To implement this project we selected specialists to help our clients resolve any kind of doubts related to the use of handsets, products and services. This service is available in both shops and on-line Telefónica channels, and also on social networks. The objective was to create a multi-channel guru community.

These new technology gurus deal with Telefónica customers and non-Telefónica customers, and their presence has grown in shops throughout Europe thanks to their popularity with the public and the positive effect that it has had on the customer satisfaction experience.

A guru is someone who shares his passion and enthusiasm for new technologies, and is able to inspire the customer through practical examples of their use, offering a great experience, generating confidence, and able to explain complicated products and services in a simple and understandable manner for all.

This experience was highly rated by our customers and boosted their satisfaction - our brand positioning benefited from it against our competitors. Another important aspect is that it has become a communication and feedback channel between Telefónica and its customers, users and suppliers, which gives our customer a larger say in developing products, services and handsets.

Projects to reduce claims

At Telefónica we know that complaints and claims are a major source of customer dissatisfaction. For this reason, in 2011 Telefónica Czech Republic deployed a scheme to reduce the number of complaints and claims. The new claim management model, involving 17 initiatives, affected the whole company, and enabled us to identify the root causes of claims, and also simplify and speed up the process of solving them. It also enabled us to implement a comprehensive communication plan to improve promotions and products, simplifying the product portfolio, increasing the clarity of bills and increasing the transparency of the value proposal.

Apart from reducing the number of claims by more than 50%, we have managed to avoid repeat claims as well, thus improving efficiency and the client experience.

The claims reduction plan deployed in the Czech Republic managed to post a 50.0% reduction

Privacy and data protection



Telefónica specifically analyses privacy risks arising from digital products and services.

Universal use of Internet and its functionalities have changed social and commercial relationships, and the public's ability to express itself; furthermore, the amount and types of information to which both companies and users have easy access have multiplied.

The abundance of information concerning people, together with the ease and speed with which it can be sent between different networks, companies and countries, is a great opportunity for progress for consumers and operators, but it is also a great responsibility for companies that manage personal information on a daily basis. A proper definition of the game rules will depend to a large extent on achievement of future objectives by societies (The Lisbon Council video <http://youtu.be/3EtMC2Q3lbc>).

At Telefónica, we understand that in the digital world respecting the privacy and intimacy of people is even more critical than in traditional services, and so we try to specifically analyse risks related to digital products and services, identifying and correcting the main causes from the outset.

We are conscious of our responsibility and the continuous importance of privacy in new digital services. For this reason, in 2011 we conducted a specific analysis on the Reputational Risks of Privacy and Data Protection of the digital services being launched, following the Telefónica Group Methodology for Risk Assessment and the directives of the COSO II report.

The results of this analysis enable us to protect our clients' privacy from the outset, introducing data protection guarantees and privacy options "from the design stage" of new digital services launched by the company.

The analysis served as a reference point to focus all the company's efforts on privacy matters, among which:

Consolidation of the Telefónica Group security policy:

At Telefónica we respect data protection quality and security standards, and we use this data in accordance with the legislation in force, in compliance with our Business Principles and as required by our customers, employees and shareholders. To this end, in 2011 we carried out 100% more data protection audits than in 2010.

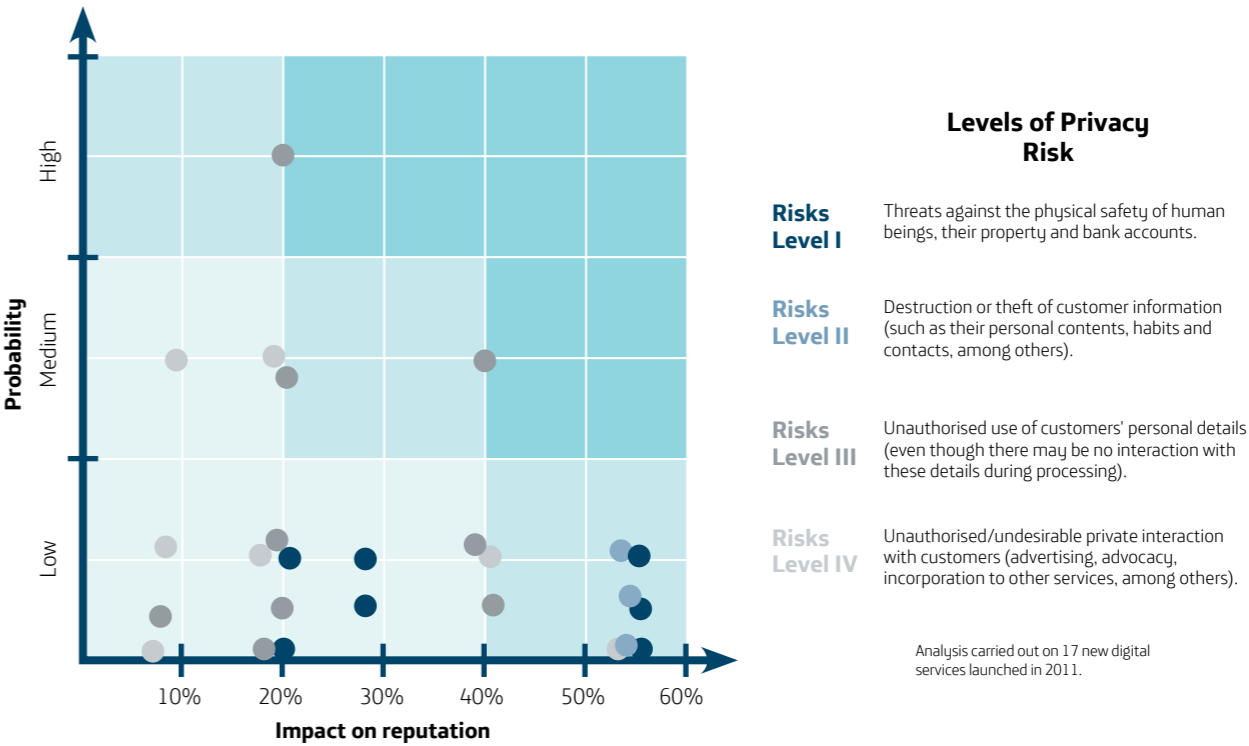
The most important aspects we reviewed were: application of security measures for handling personal data, controlling access to the data, data quality, consent of those concerned to handle their data and the possibility they may exercise their rights to access, rectify, cancel or object to their data.

Telefónica makes a great effort to ensure the security of its own communications and data and that of customers. To this end we have implemented an Information Security Policy in all our operations, based not only on our own experience but also on the main international standards. The Policy defines the necessary courses of action to protect our information and that of customers, rolling out security operations and a global extension to the system.

Furthermore, Telefónica's Operations Centres are configured with redundancies in line with the Corporate Security Policies and other international regulations such as ISO and British Standards. This type of reinforcement increases the level of security to guard against possible natural or deliberate disasters in all countries where the company operates.

At Telefónica, we manage local security solutions and critical infrastructures worldwide. We also work with governments and international security bodies, on the exchange of know-how and the protection of services from cyber-threats.

Privacy Risk Matrix



This strong international and national partnership is the result of years of research and development in order to understand these threats, against which we protect ourselves through multiple Security Operations Centres, special response teams for systems emergencies, and for which we have added resistance mechanisms to our networks and services, in the interest of our public and private sector customers.

We not only comply with the legislation of the Protection of Critical Infrastructures, but we also help our clients comply with the legislation, as we are part of the value chain of other companies through the provision of their services.

Training and awareness

In 2011, over 30,000 Telefónica employees received training in data protection. This accounts for more than 90% of employees targeted by the training course. This figure included 26,000 European employees, in Spain (13,800), the UK (5,068), Germany (4,500), Czech Republic (2,000) and Ireland and Slovakia (1,000 employees between the two countries).

In Latin America we continue to bolster our work on employee training and awareness, with projects such as the information security and data protection courses in Chile (1,154 employees on the eLearning course) and Ecuador (142 executives attended the training course in person).

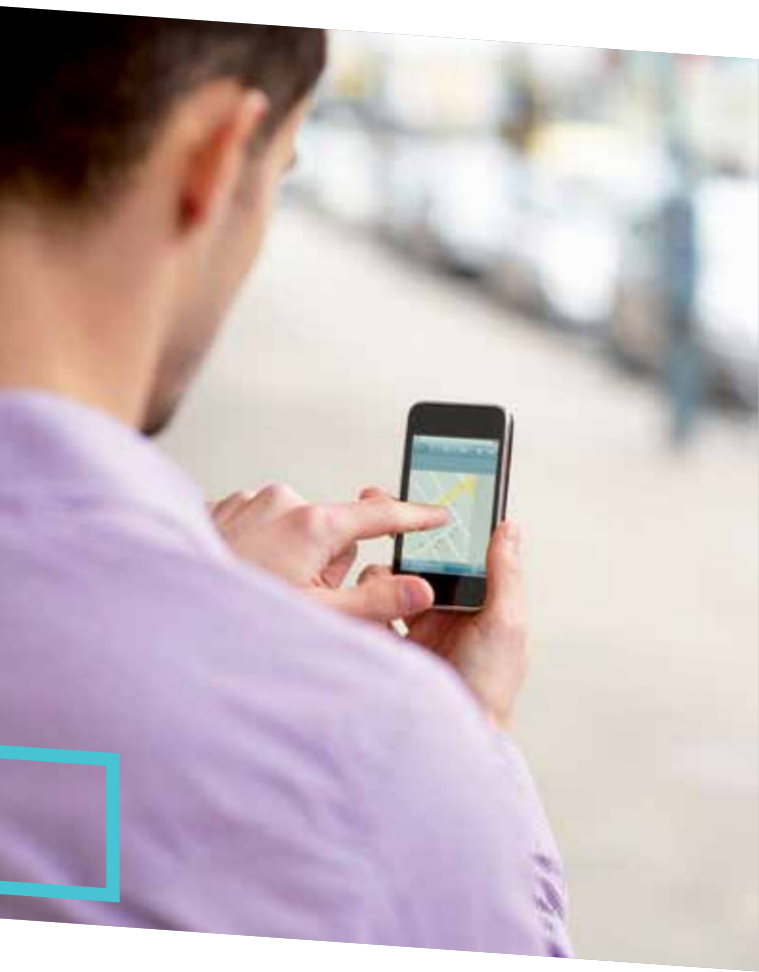
In Brazil, 137 courses were arranged, attended by 3,130 employees of our partner suppliers, working in the area of customer service and technical call centres. More than 80 dealers were also trained.

In Uruguay these courses were extended to all company personnel, both internal and external, on 16 courses spread over 4 months, and a training module on data protection was included in the induction course for new employees.

In Mexico, training was given to both internal and external personnel, to a total of 1,565 people trained. This was supplemented with on-screen messages from management, messages on the phones of each employee, internal communications projects and triptychs.

Mexico also undertook a communication campaign, aimed at the public through messages and privacy notices on web pages, announcements to customers on their bills, poster notifications and privacy notices in the reception areas of company buildings.

It should also be pointed out that the Dedicated Internet and Fixed Data service in Ecuador was awarded the ISO 27000 standard certification in 2011. In 2012, the Electronic Recharging process is also expected to be awarded ISO 27000 certification.



risks, as at their age they are more inclined to share and disclose personal information with no thought to the possible future use of this data by others.

We understand that protection of privacy in this area is a theme that goes beyond Telefónica, and for this reason we actively participate in sector initiatives which encourage the protection of personal information and the privacy of children and adolescents such as, for example:

ICT principles of the ICT Coalition for a Safer Internet for Children and Young People

Telefónica is one of the 25 European ICT companies that have created the very first **Principles** to improve the security of children and young people on Internet, in such a way as to enable them to avail themselves of its advantages without exposing themselves to other possible uses which so concern their parents.

Launched in January 2012, the ICT Principles are a guide for the deployment of products and services aimed at improving the online security of minors, based on key themes such as content, parental control, management of abuse or improper use, child pornography content, privacy control, education and awareness.

The difference between this initiative and others on the market is that it offers a long-term agenda which guarantees secure development and covers all aspects of access and use of the Internet and its services.

For further information, see the attached document (ICT Principles).

CEO Coalition

A coalition set up in August 2011 by EU Commissioner Neelie Kroes to make the Internet a safer place for children, an initiative forming part of the European Digital Agenda framework. The Commissioner sought to implement services and tools to encourage proper utilisation of Internet and prevent any risks arising from misuse. With respect to privacy, the idea is to find solutions to manage privacy for these age groups by default. This initiative was finally announced on 2 December last year with the support of Telefónica and Tuenti.

Digital Trust projects to promote choice and control over customer privacy.

As of the end of 2011 we have been working to create a Privacy Centre to offer a service to all geographical areas, business units and company stakeholders, as the main Group privacy reference. We have also been showing great transparency with regard to the privacy of new digital services for our customers, such as Priority Moments and O2 Wallet in the United Kingdom, and through the Company's commitments to its services (<http://www.o2.co.uk/thinkbig/blueprint/commitments>).

A review of the Group Commitment to privacy and the launch of the Privacy Centre are the main challenges facing us in 2012, with a major role to be played by the Telefónica Group's corporate personal data protection policy.

Privacy of children and adolescents

Telefónica is committed to guaranteeing protection of the privacy of the most vulnerable groups, such as children and adolescents.

These groups fully exploit the network's potential in view of their status as digital natives, but they are also highly exposed to privacy



The members of the coalition undertake to allocate resources to achieve the five goals proposed by the Commissioner:

- ⇒ Simple and robust reporting tools for users.
- ⇒ Implementation of age-appropriate privacy settings.
- ⇒ Use of content classification.
- ⇒ Provision of parental control tools.
- ⇒ Improve procedures to remove images of sexual abuse of children.

For more information:

- ⇒ Companies forming part of the Coalition:
<http://europa.eu/rapid/pressReleasesAction.do?reference=IP/11/1485&format=PDF&aged=0&language=ES&guiLanguage=en>
- ⇒ Declaration of intent of the signatories:
http://ec.europa.eu/information_society/activities/sip/docs/ceo_coalition_statement.pdf

- ⇒ Initiatives by the Group in relation to education and encouragement of the proper use of ICT:
(See chapter 4.6: Protection of children)

GSMA - Mobile Privacy Principles

GSMA² announced the publication of its Mobile Privacy Principles on 27 January 2011. In February 2012, the GSMA, which represents the interests of companies belonging to the mobile ecosystem throughout the world, published the principles which describe the way in which mobile consumers' privacy should be respected and protected when consumers use mobile applications and services, with the ultimate aim of giving users increased transparency, alternatives and control over the applications' use of their personal data.

2. GSMA represents the interests of mobile operators around the world. Present in more than 220 countries, it accounts for around 800 mobile operators and more than 200 companies in the mobile ecosystem. For more information: www.gsma.com.

We have worked alongside international institutions to create a new regulatory framework to cover all the needs of consumers and the industry with respect to privacy and data protection



These principles have a special section on the protection of children and minors, which chiefly operates on four fronts:

- **1. Tailor applications to age groups:** Applications for children and adolescents should be appropriate for their age group, and ensure that users understand the consequences of installing or using an application or service.
- **2. Set default configurations:** Applications aimed at children and adolescents should have default configurations to prevent users from releasing their location automatically.
- **3. Comply with child protection laws:** Applications should at all times comply with legal requirements put in place for the protection of children.
- **4. Verify age where necessary:** Under certain circumstances, age verification could be necessary (for example, when applications have a social network function or allow access to adult content).

For more information on GSMA or directives on privacy design, see: <http://www.gsma.com> y <http://www.gsma.com/Mobile-Privacy-Design-Guidelines>

Cooperation with international institutions:

The regulatory privacy and data protection framework is fully operational in the two main regions in which we operate.

Telefónica has worked both individually and through sectoral associations with international institutions towards the creation of a regulatory framework that takes account of the needs of all consumers and the industry as regards privacy and data protection.

We were particularly active in Europe in 2011, participating in all discussions in the review of the European regulatory framework on Privacy and Data Protection. These discussions culminated in the presentation of a proposal by the European Commission on 25 January 2012.

In January 2011 we responded to the European Commission consultation on Data Protection, and other consultations by the Commission on Cloud Computing and notification of security incidents. The debate on Cloud Computing was a priority on the agenda for the presentation of the European Strategy of Cloud Computing in 2012. We played an active role in an audience organised by the Commission specifically for the Telecommunications and Webhosting industries in November.

We were also in regular contact with major stakeholders, not only as an individual company, but also in a leadership role among industry associations. Telefónica chaired the ETNO Working Group* on Data Protection, Trust and Security, one of its seven strategic groups. Also, like ETNO, we are heading a sectoral coalition composed of the principal European associations (GSMA Europe, EuroISPA, ECTA, CableEurope and ETNO), which represents the entire European electronic communications industry: fixed-line and mobile telecommunications operators, Internet service suppliers and national and pan-European operators.

The coalition has issued several joint declarations in which they have stressed concerns and opportunities in the current process to review EU Data Protection laws. These joint declarations have been greatly appreciated by the Commission, Members of the European Parliament and other stakeholders, as they give the industry's opinion with a single voice concerning an issue that is so important for EU competitiveness.

(*) ETNO: European Telecommunication Network Operators Association.

In Latin America regulatory changes are occurring in some countries, such as:

- Brazil, which at the end of January 2011 closed the public consultation process on the draft Personal Data Protection Law. This law will be the country's first effort in this field, as currently there is no national law in this respect.
- Mexico, which recently approved its first Federal Law of Protection on Personal Data Held by Private Parties.
- Colombia, which recently added a law on personal data protection to the constitution, complementary to Law 1266 on Habeas Data.
- Chile, which changed its data protection law, focusing on economic, financial, banking and commercial data.

Safe use of the Internet by children and young people



Telefónica is aware of the importance of new information technologies in daily lives and the education of new generations, which is why it has developed tools and participated in different programmes that encourage safe use of ICT in a safe environment for children and young people.



Strategy for safe and responsible access to Internet by children and young people based on:

- 1. Self-regulation
- 2. Education
- 3. Products and services
- 4. Strategic alliances

Information and communications technologies contribute to the development of the younger generations and are playing an increasingly central role in everyday work, study and leisure activities. In particular, they are key elements of modern educational projects and in the intellectual growth of young people and children. Telefónica is aware of this reality and is endeavouring to promote and take part in innovative projects aimed at ensuring that children and young people extract maximum benefit from these technologies while avoiding inappropriate use.

In pursuit of this goal, Telefónica realises the value of collaborating with a wide range of bodies, civil organisations and other sector companies, and in 2011 was involved in numerous initiatives in addition to those in which it has participated for many years.

To achieve its goals, Telefónica has evolved a strategy which enables it to offer its customers safe access to ICTs while fostering their safe and responsible use by minors.



This strategy is based on four pillars around which the Company has developed different initiatives aimed at fostering the appropriate use of its services: self-regulation, education, products and services and strategic alliances.

1. Self-regulation

1.1. Regulations Governing the Provision of Adult Content

Telefónica, as a supplier of services and content, must put in place control mechanisms to ensure that minors do not access age-inappropriate content.

To this end, the Company approved the Regulations Governing the Provision of Adult Content in 2005. Under these regulations, all group operations offering such content must provide clear and unequivocal notification of its unsuitability for under 18s, and the option of restricting access at the request of the customer or even with access blocked by default, in which case the customer him- or herself must request access having identified him- or herself as an adult.

In some countries, scheduling restrictions are also in place and adult content may only be offered after a watershed time.

Pay television services in countries where Telefónica provides adult content can only be accessed using a parental PIN code, i.e. by a parent who knows the PIN.

With the aim of ensuring maximum compliance, these regulations apply both within the Company and to our content suppliers, which have been notified of their content and application.

Revision

Since these regulations were approved, the production and distribution of content has assumed increased significance within Telefónica's business strategy.

Telefónica has increased its activity and its range of content services via its various platforms. Content affects the brand image that Telefónica wishes to project and also helps to shape the perception that consumers and potential users have of the Company.

The impact of content produced under the Telefónica brand is generally greater than that generated by distribution and it has therefore been afforded special treatment in the revision of the regulations. Moreover, there is also a growing focus on the production of own content which is distributed via Telefónica's platforms.

As a result, the Company is striving to promote the adoption of standards that ensure content is provided in accordance with the Company's objectives and which at the same reflect the values set out in Telefónica's Business Principles.

An exhaustive review of the regulations was carried out in 2011 as a result of which they were extended to encompass all the new businesses that have evolved in recent years.

These revised regulations are scheduled to be approved in the first half of 2012 and will then be applied over the 2012-2013 period.



Internet content

The aforementioned regulations do not apply to Telefónica in its role as a service provider for the information society whereby Telefónica facilitates access to content without intervening in the creation, modification or selection of the recipients of such content.

To ensure that children do not access Internet content for which Telefónica does not bear responsibility, the Company offers parental filters which can be configured in the home, allowing parents to decide which content categories their children must not access or view.
(For further information, please read the Social Innovation report).

Other types of content

Telefónica is radically opposed to other types of content that may be deemed illegal and to the use of its services for their distribution or any other kind of illicit behaviour.

Moreover, the Company does not permit activities relating to, among other things, child pornography, drug trafficking, discrimination, terrorism, xenophobia, and human and illegal arms trafficking and undertakes to make available and to provide information on the use of channels via which customers can report conduct likely to encourage the consumption of illegal content.

1.2. Mobile Operator Alliance

In 2008, Telefónica was a founder member of the Mobile Alliance Against Child Sexual Abuse Content, due to which it proactively obstructs the use of the mobile environment by individuals or organisations wishing to consume or profit from child sexual abuse content. The Alliance follows the guidelines of, and uses the lists provided by, the Internet Watch Foundation (www.iwf.org.uk).

1.3. National Code of Conduct

In 2007, Telefónica signed the European Framework for Safer Mobile Use by Younger Teenagers and Children. This agreement was also defined in national Codes of Conduct, which Telefónica abides by in each of the European countries where it operates.

In February 2011, Telefónica joined the leading Spanish operators and the NGO Protégeles in providing an icon on their websites which makes it easier for customers to report potentially illegal content found when browsing the Internet. The icon is linked to the NGO's reporting page, where customers can both report potentially illegal content and seek assistance if they are suffering abuse of any kind or require professional advice.

1.4. CEO Coalition

In December 2011, the Vice President of the European Commission, Neelie Kroes, announced the launch of the CEO Coalition to make the Internet a better place for kids. This initiative is a call for the CEOs of the leading companies in the new ICT industry to promote activities in favour of better Internet use by children, working in five separate but interconnected areas.

The members of the coalition have undertaken to dedicate resources to achieve the five goals proposed by the Commissioner:

- Simple and robust reporting tools for users.
- Age-appropriate privacy settings.

Together with leading Spanish operators and the NGO Protégeles, in 2011 Telefónica included an icon on its websites to make it possible for customers to report potentially illegal content found on the Internet

- Wider use of content classification.
- Wider availability and use of parental control.
- Effective take-down of child abuse material

Over an 18-month period, and with input from civil society, measures will be adopted to attain the five objectives set by the European Commission.

This cooperative voluntary industry intervention will facilitate the joint search for solutions and involves all actors in the value chain. It will forge stronger links between the sector and organisations whose goal is to defend the needs of children in the digital environment, build on established projects and good practices and deliver innovative products and services to provide a safer experience on Internet capable devices (e.g. PC, TV, tablets, smartphones, etc), and available to all types of Internet access services (e.g. fixed and mobile Internet accesses). The initiative will also foster more effective relationships with law enforcement agencies.

1.5. The Coalition of ICT Companies

In January 2012, around 30 companies from the Information and Communication Technologies sector announced the launch of the ICT Coalition for a Safer Internet for Children and Young People.

In 2011, the leading companies from the new technologies sector met periodically to draw up a draft of guiding principles which have been reviewed and approved by civil society.

Companies from across the information and communications technology sector – from network operators through device manufacturers, content providers, search engines and beyond – are signatories to the principles, which focus on the key areas of content, parental controls, dealing with abuse/misuse, child sexual abuse content or illegal contact, privacy and control, and education and awareness.

The principles differ from other ongoing initiatives because they provide a long-term roadmap for safer development and cover all aspects of accessing and using the Internet and its services. There is a particular focus on the need for education and training in appropriate use of the Internet to avoid the potential associated risks.

The signatories pledged to:

- Develop innovative ways of enhancing online safety and encouraging responsible use of the Internet and Internet access devices by children and young people;
- Empower parents and carers to engage with and help protect their children;
- Provide easily accessible, clear and transparent information about online safety and behaviour;
- Raise awareness of how – and to whom – to report abuse and concerns.



2. Education

2.1. Interactive Generations Forum

In 2008, Telefónica joined forces with Navarra University and the Inter-American Organization for Higher Education to create the Interactive Generations Forum to learn more about how children and adolescents use new technology in order to draw up educational programmes for encouraging safe use of ICTs.

In 2011, the platform interviewed 127,154 school children in 2,900 schools across 10 countries: Spain, Mexico, Ecuador, Brazil, Argentina, Chile, Colombia, Peru, Venezuela and Guatemala.

Another milestone last year was the presentation of “La Generación Interactiva en Iberoamérica 2010. Niños y adolescentes ante las pantallas” (The Interactive Generation in Ibero-America in 2010. Children and Teens in front of the Screen), a book written by Xavier Bringué, Charo Sádaba and Jorge Tolsá. This second report focused on the reality in Ibero-America, in which over 78,000 children aged between 6 and 18 took part. It highlights the myriad educational and social challenges raised by intensive use of the new technologies and evidences the important of teaching young people how to use them properly. The book was presented in five countries (Colombia, Guatemala, Mexico, Chile and Argentina) in November and December of last year.

This study was also carried out and published for Madrid, Andalusia and Ecuador. The Forum also published new editions under its “Children and the Social Networks” series.

Broadband customers in Spain, Argentina and Colombia enjoy Aula 365, a free schooling aid leveraging multimedia content for all the family

Following a period of investigation, the Forum has developed a series of educational initiatives: courses for teachers and educators, parent workshops, hands-on activities for children, etc. Since 2008, some 50,000 people have received training on the proper use of new technologies in Spain and Latin America.

In 2011, the Interactive Generations Forum's volunteer team gave a total of 32 training sessions in schools and institutions.

Together with Foro Generaciones Interactivas and Pantallas Amigas, Telefónica also launched Childhood and Technology last year, a new online educational platform aimed at boys and girls aged between 6 and 11 and their parents and teachers. By means of three cartoons, the platform tackles issues relating to the safe and healthy use of Internet, videogames and mobile phones.

The purpose of the website is to provide children with criteria for using all this technology wisely and safely while they have fun and to give adults a close-up and positive view of what this technology can do. The cartoons are intended to teach kids in an entertaining environment while the educational guides are targeted at parents and teachers. Users can also download the cartoons onto mobile handsets.

One of the new developments pursued last year in terms of specifically protecting children and fostering the safe use of Internet related to the negotiations concluded in Colombia for the development and launch (during the first half of 2012) of the first hotline in Latin America following the INHOPE guidelines.

Telefónica, together with the Interactive Generations Forum, the Information and Communications Technologies Ministry, the ICBF (the Colombian Family Welfare Institute), Fundación Telefónica and Red Papaz (the Mothers and Fathers Social Network), has laid the foundations for this body, which will deal with the complaints of users who have encountered potentially illegal content whilst surfing the Internet.

INHOPE is a body co-funded by the European Commission which coordinates internet hotlines throughout Europe, supporting them in responding to reports of potentially illegal content. This network has now extended its operations beyond Europe and around 40 countries worldwide currently have hotlines that belong to INHOPE. INHOPE members share a tried and trusted methodology and exchange best practice.

Colombia has spearheaded efforts to improve online safety and has been involved for many years in initiatives such as the “Healthy Internet” project in partnership with the country's police force.



3. Products and services

3.1. Aula 365

Aula 365, first launched in Argentina, then in Spain and Colombia, has revolutionised the promotion of positive online content.

Aula 365 is a free learning services portal with multimedia content for the entire family. Through this educational portal, Telefónica provides its broadband subscribers with advanced Web 2.0 tools to help their children's learning: multimedia educational films, blogs, wikis, infographics, biographies, photo galleries, master classes, etc.

This service helps raise school performance among students of all ages, with the support of a virtual teacher who resolves doubts and questions.

All this is done in a safe environment in which children cannot disclose personal details or post photos and which is constantly moderated to ensure that they do not access inappropriate content.

In keeping with our commitment to social responsibility, we endeavour to foster the responsible use of new technologies by children while encouraging them to extract full benefit from the possibilities they offer. To this end, we strive to provide our customers with products that fit their profile and to launch educational initiatives that demonstrate how to take full advantage of them while avoiding their inappropriate use.

This concern for the safety of its services has led Telefónica to offer, together with its broadband Internet service, security

packages including anti-virus and anti-fraud software, advanced child security and mail, application and parental content filters to protect customers from viruses, information theft and inappropriate content.

In addition, the Sustainability sections of Telefónica's website contain tips and recommendations on appropriate use of new information and communications technologies and a blog, where experts write about the latest trends and news in areas relating to children and new technologies.

Alliances

Telefónica is aware of the need for strategic allies, such as civil organisations, to promote the responsible use of new technologies and is working at the national level with partners such as INHOPE, Insafe, Protégeles, Childnet, and other non-governmental organisations with goals similar to its own, including FOSI. In addition, the Company is involved in initiatives promoted by the telecommunications industry (see section 1. Self-regulation), the European Commission and the International Telecommunications Union, among other key players.

Without these alliances it would not be possible to carry out as wide a range of educational and awareness-raising initiatives, while the ICT sector would not be in a position to ensure that users can extract maximum benefit from their services whilst avoiding inappropriate use.

This pillar is absolutely central to the Company's strategy because it enables all the initiatives undertaken to attain the desired outcome.

Innovation at Telefónica

We telecommunications operators are in the vanguard of the digital revolution, a phenomenon which is changing how we communicate, inform ourselves and relate to one another and bringing about advances in a multitude of areas (commerce, education, health, government, etc.).

Telefónica is in a privileged position to leverage the opportunities that are arising in this new environment. In order to do so, we are forging ahead with the transformation underway at the Company and launched numerous initiatives in 2011.

With regard to organisation, we created a global business division, Telefónica Digital, which strives to take full advantage of all opportunities for growth in the digital world, driving innovation, strengthening our product and service portfolio and maximising the benefits of the Company's large customer base.

In addition, we are strengthening our steadfast commitment to technological development via BlueVia (the Company's platform for developers), Movilforum and Wayra, an initiative unveiled in 2011 to help talented entrepreneurs to accelerate their business ideas in the sphere of ICTs.

Technological innovation

Our innovation model at Telefónica was evolving throughout 2011. We boosted collaborative models and created one of the largest innovation networks in the global ICT sector, a key sector for the sustainable development of the communities we are part of. We focused technological innovation on digital construction so as to harness the opportunities offered by new production tools and technologies in the development of software and creative talent.

ICTs are a fundamental tool for economic and social development and at Telefónica we are aware of the role of innovation as a driver of growth. Therefore, in collaboration with INSEAD and the OECD, we have promoted the creation of the InnovaLatino Report to discover the technological innovation trends in Latin America.

Telefónica continues to believe that technological innovation is the key to achieving sustainable competitive advantages by staying ahead of market trends, enabling us to differentiate the products we develop. Applying this belief, in 2011 Telefónica increased its technological innovation efforts, investing €5,090 million, which represents 8.1% of our consolidated revenues in 2011. The accumulated investment over the last three years in R&D represented 7.9% of revenues.

R&D

Telefónica considers differentiating its products from the competition to be an important strategy to improve its market position, and that this cannot be based exclusively on acquired technology. For this reason, we believe in promoting research and development (R&D) activities in an effort to achieve this

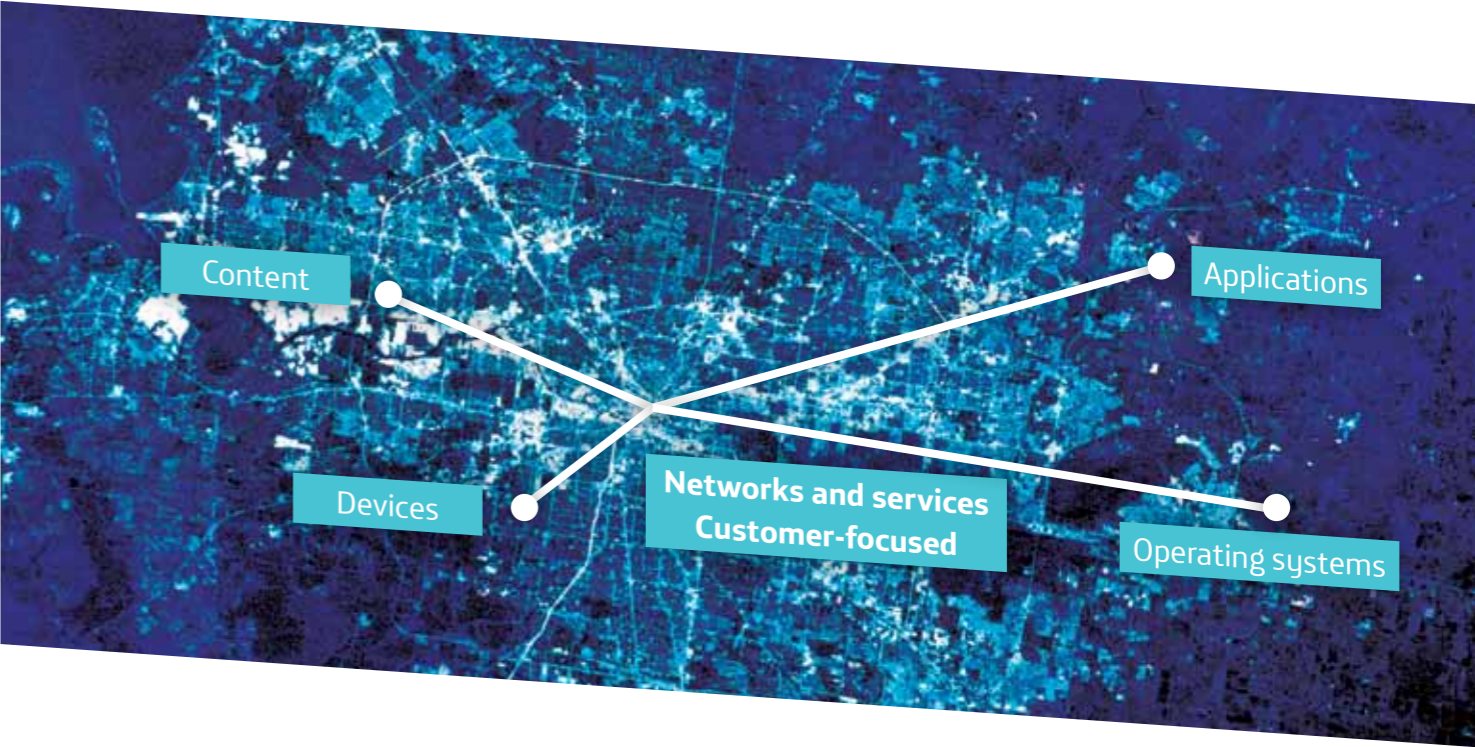
differentiation and make progress in other areas of innovation. Accordingly, in 2011 Telefónica dedicated a budget of €983 million to R&D, 23% up on 2010 and representing 1.6% of revenues (1.4% of accumulated revenues for the last three years).

At Telefónica, we believe in an "open innovation" model, and thus this research and development effort was undertaken not only through Telefónica I+D, but also sharing work with a large variety of collaborating companies, constituting one of the largest innovation networks in the global ICT sector. This R&D model has already become a global innovation model benchmark. It was recognised as such by the OECD itself, when it selected Telefónica to be one of the three companies invited to participate in the seminar on R&D and innovation in the new economic environment, held in Paris in December 2011.

Furthermore, this open model has allowed us in recent years to open the Company's platforms to collaboration with third parties, to support technology companies through venture capital initiatives, to invest in companies of technological interest and to promote initiatives such as *Campus Party*.

Telefónica I+D's research and development activities in 2011 concentrated mainly on the following areas:

- Interpersonal communication in the future in a natural manner, through the use of the Internet and smartphones.
- Video and multimedia services (combining text, audio, images and video) with a user experience on all connected devices.
- Advanced solutions in emerging ICT businesses, such as tele-health, remote surveillance and support platforms for patients or platforms for monitoring.
- Management services between machines (M2M) related to energy efficiency and the mobility of persons.
- Cloud computing that makes intensive use of resources available on the Web in order to publish, market and distribute applications.
- Analysis of users' profile according to their use of communications, providing opportunities for business models and services (marketing campaigns, targeted advertising and personalised contextual services, lower turnover, cross-selling, etc.)
- Evolution of the network and services in a new global infrastructure, common to all of the business lines, in order to reduce operating and maintenance costs, offering more capacity in response to the explosion of mobile data, video content and the evolution from an Internet of People to an Internet of Things.



Telefónica also develops global innovation initiatives with a clear commitment to adapting them to meet regional and local needs. In 2011, one of the reasons for the reorganisation of Telefónica was to relocate most internal R&D for developing new networks to the Global Resources division, and to place R&D for developing products and services in the new digital environment with Telefónica Digital. This dovetails with Telefónica's strategy of going beyond the operation of networks and providing complete technology services to business customers and individuals to achieve higher added value than that offered by fixed or mobile connectivity alone.

In 2011, Telefónica headed up several projects related to developing the Internet of the future, organised by the European Commission within the Seventh Framework Programme for Research. These projects, a joint collaboration with the main companies, research institutions and universities in Europe, were developed through the PPP (Public Private Partnership) model and were partially funded by the European Commission. In these projects, we understand the Future Internet Public-Private Partnership in a practical manner, as focusing on creating services for citizens, developing "Smart City" concepts in stages, as well as the step-by-step development of other services to improve citizens' lives.

The most significant project in this area was the FI-WARE project. The project, which is central to the Future Internet Public-Private Partnership, is going to develop a reference architecture, as well as practical implementation, for an open platform for creating, deploying and providing services in different areas relating to the future of Internet. Therefore, the FI-WARE platform has become the central element of the European Commission and the various PPP members' support for the progress of this type of solutions in

Information and communication technologies are a fundamental tool for economic and social development

Europe. Telefónica is the leader of this project, which involves more than 25 additional partners and is, as we have stated, a central element of the Future Internet Public-Private Partnership, which is linked to more than 158 companies and entities and boasts a total investment of around €600 million in five years.

Managing Telefónica's Intellectual Property

Three years ago, Telefónica established the Telefónica Patent Office, currently part of Telefónica Digital, with the objective of creating sustainable value in the Company through protecting the products under development and identifying new technological assets. This unit advises on how to protect the results and identifies the possible parents, while promoting the generation of new return-on-investment policies by marketing patents or incorporating them into technological standards.

Thanks to this structure, we have generated a portfolio of patents and protected products that has allowed us to register 95 patents, 57 of which were registered at the Spanish Patent and Trademark Office and the remaining 38 at the European Patent Office, at the US Patent and Trademark Office or on international registers.

Cases of Innovation at Telefónica

Telefónica and Campus Party

Movistar deployed the new IPv6 technology for the first time at Campus Party. This new Internet protocol allows for recovery of end-to-end connectivity, enabling the development of the "Internet of Things" through which machines and numerous currently-existing or future devices, such as computers, smartphones, PDAs, cars, refrigerators, washing machines or any other appliance, will offer data and Internet connections.

Movistar, once again supporting Campus Party as its primary sponsor, was showcasing other key strategic projects for the Company, such as

Wayra (linked to the best talents with entrepreneurial spirit); Bluevia (applications developers) and an innovative agreement with Arduino (the leading platform in free hardware).

Campus Party was one of the events chosen to draw up the shortlist of projects, given the conjunction of innovation, talent and entrepreneurial spirit that comes together at this technological event and allows many of the participants to realise their dreams.

At Campus Party Valencia 2011, the Fundación Telefónica presented the EducaParty project. At this event, hundreds of technology teachers, innovators and enthusiasts took part in debates and workshops to analyse the development and benefits of technology in education.

Movistar has, since *Campus Party* began fifteen years ago, continued providing support which has contributed to making this Internet gathering a technological reference worldwide, enabling parallel projects such as Wayra, Bluevia or EducaParty to become sources of innovation and success for participants' projects.

In addition, Telefónica I+D and the Arduino free hardware platform presented *Arduino Shield*, a product containing a modem that can connect to Internet, the fruit of months of collaboration between the two companies. The users of *Campus Party* were invited to try it and give their impressions, to help with future versions.

It was the fifteenth anniversary of *Campus Party*, which it celebrated with a definitive shift towards educational content, with over 300 hours-worth of workshops, conferences, competitions and activities. In line with this schedule, Movistar's offering at that edition also included the participation of a master of gastronomy, Ferran Adrià, who explained his personal vision of creativity and the importance of considering young people as real innovators.

10 Fridays

Telefónica I+D has rolled out the *10 Fridays* programme, through which the Company's engineers can use up to ten Fridays to develop their own ideas during time that is not necessarily part of their daily routine at the Company. The purpose of this initiative is to encourage engineers' creativity and to motivate them by allowing them to work on topics that they put forth in areas of their interest.

The *10 Fridays* programme is the first of its kind in Spain and covers projects as varied as e-health, analysis of psychometric data, game development in HTML5 or projects with fashion and advertising firms.

In addition, some ideas that prove successful may receive financing, be turned into prototypes and even become final

Campus Party celebrated its fifteenth anniversary with a definitive shift towards educational content, with over 300 hours-worth of workshops, conferences, competitions and activities

products. In fact, the Company has already had some interesting results, such as start-up projects, patents and new relationships with external companies.

El Bulli Foundation and Ferran Adrià innovating with Telefónica

Telefónica and Ferran Adrià have launched the *Ideas for Transformation* contest, in which MBA students from ten of the world's top business schools will design proposals for the new Bulli starting in 2014, to be known as the elBullifoundation.

The schools chosen for this first edition of the contest, to be held during the 2011-2012 school year, were Harvard University (Cambridge - Boston, USA), Columbia University (New York, USA) and Berkeley's Haas School of Business (Berkeley - California, USA), the London Business School (London, UK) and ESADE (Spain). Another five prestigious centres based in areas such as Latin America or China will take part in the 2012-2013 contest.

Telefónica I+D is one of the Telefónica units most actively involved in the creation of elBullifoundation. The Company's research and development department is working with Ferran Adrià to set up a research laboratory heralded as the new Mecca of creative gastronomy. Internet may be the vehicle for the next culinary revolution, clearing the way for a new wave of innovation, for instance, by allowing Ferran Adrià to share his creativity with the world in real time, and designing new experiences where video, immersion and the simultaneous participation of millions of viewers will lead to new ways of experiencing cooking.

The use of data mining to unravel the DNI of foods and create new sensations, the installation of multimedia technology and cutting-edge communications at the building where elBullifoundation will be housed, including kitchen sensors and robotics, 3D printers and smart tools etc. will lead, in short, to a revolutionary new computerised and hyper-connected kitchen.

Telefónica I+D's objective is to support Ferran Adrià with the most modern - and yet discreet - technology so that his creations are always the real stars of the show. The Telefonica I+D research and development centre in Barcelona will provide Ferran Adrià with cutting-edge technology and Internet solutions to make elBullifoundation a key player in the new era of innovative cuisine.

Innovation Week

For an entire week, Innovation Week was held in Madrid. This initiative has been exported directly from Argentina, where three editions have already been held and in which professionals from several of the Group's companies have participated. Among the events on offer were talks aimed at making the audience reflect on the great opportunity to develop small innovations on a daily basis, thus intensifying Telefónica's innovation culture.

The concept was born in 2006, beginning in Buenos Aires and benefiting 250 Telefónica employees. The event quickly became a hit, and it was decided to re-launch the concept, refocusing the goal on stimulating lateral thinking so as to awaken employees' curiosity



and stimulate innovation in their day-to-day working lives. The concept has been brought to several countries in Latin America, such as Colombia, Peru, Ecuador, Chile, Mexico, Venezuela and Uruguay, and is beginning to be rolled out in Europe.

This has been a positive experience, which offers the opportunity of exporting the innovation model to all the countries where Telefónica is present. The importance of this type of projects is that they are developed through our own know-how, thus sharing successes globally and seeking to improve the management of innovation indicators within the Group.

Movistar Innova in Chile

In August 2011, Telefónica gave shape to its desire to bring together and structure its efforts and initiatives regarding innovation and entrepreneurship in Chile under a new single architecture. Movistar Innova, which had already become the country's leading business incubator, had three cornerstones:

- ➔ **Entrepreneurship.** This initiative gives continuity to what had from the beginning been known as Movistar Innova, a project launched in 2009 by the mobile telephone division and supported by the Chilean Economic Development Agency, Corporación de Fomento de la Producción (CORFO) and which became the top business incubator and private business accelerator in Chile. Its mission is to make the channels, platforms and knowledge of the Telefónica Group available to entrepreneurs in order to promote, support, exploit and commercialise entrepreneurial initiatives with high economic potential, which lead to the creation or consolidation of successful, innovative firms that make their mark on the market.
- ➔ **Innovation.** This began with the Telco Innova project, which aimed to implement an Innovation Management System. It was sponsored by CORFO and its goal was to identify, foster and systematise innovation in all corporate areas and to collaborate with strategic allies, focussing especially on products, services and processes that

strengthen customer relations. The final goal was to develop an innovation culture throughout the organisation. The Telco Innova Project, which was launched in December 2009, was conceived as an innovation eco-system, and therefore companies collaborating with Telefónica also took an active part.

- ➔ **Spaces.** This covers the creation of physical spaces where those who wish to tackle projects with Telefónica can meet and interact, fostering innovation and entrepreneurial initiatives in what has been called the Movistar Innova Centre.

Movistar Innova, in the area of Entrepreneurship, has reached a significant level of maturity and already has achieved tangible results: more than 2,000 business ideas in five calls for proposals, with projects that have raised €0.72 million in private capital and €288,000 in seed capital from CORFO. In addition, seven companies are already doing business in Chile and two of these are already in Silicon Valley, as is the case with SmartBoxTV.

SmartBoxTV is an endeavour which develops applications for interactive digital TV in social networks, delivering interactive sporting statistics, messaging and games, among other things.

Another venture that is worthy of mention is Baytex, which is a web (SaaS, or Software as a Service) system to build and administer interactive Magazines and Catalogues on tablet devices (iPad/Android).

Furthermore, with 20 projects in its portfolio and more than 30 entrepreneurs working hard, Movistar Innova will continue to grow through its internal innovation, incubation and acceleration processes for businesses.

In 2011, Movistar Innova was recognised for the creation of the Movistar Innova Centre, a shared space which brings the entrepreneurs together, favouring co-working.



Wayra is a comprehensive Latin American project which was born in Latin America and aims to identify ideas with the greatest potential in the field of ICT

Support for new ideas: Wayra

Wayra is a comprehensive project that was born in Latin America in April 2011, as a *startup* within Telefónica itself. This project aims to identify ideas with the greatest potential in the field of ICT and to boost their development, providing them with the technology, tools, mentoring and financing they need to bring them to life.

Wayra, which means 'wind' in Quechua, was born with the aim of becoming an incubator for the development of future 'Silicon Valleys' in the countries where Telefónica operates. The Company has demonstrated through this initiative that its leadership in the markets where it operates manifests itself in commitments to society and support for innovative talent.



Its first objective was to find a system that could enable it to capture the greatest number of emerging ideas in a sector, like the technological sector, which is constantly evolving and where there are constant changes in consumer habits, opportunities and the demand for services. This system consists of a competition model for each country, whereby entrepreneurs with ideas and projects focusing on different areas of digital innovation are found through social networks and contacts with universities and development centres. The only requisite is that the project is related to the world of ICT.

So far, Wayra has already invited proposals for its competitions from entrepreneurs from the ICT world in nine countries, in both Latin America and Europe. More than 5,000 technological projects have been submitted to the competitions in Colombia, Spain (Madrid and Barcelona), Mexico, Argentina, Peru, Brazil, Chile and Venezuela, making Wayra one of the best detectors of innovative talent on two continents.

At the Wayra Academies, the best technological innovation business projects will take shape and be fast-tracked. These projects are selected over the *Wayra Weeks* which follow each competition, during which an independent jury, adopting common selection criteria, selects the best start-ups for fast-tracking.

The Academies are meeting and work spaces, architecturally designed in accordance with the latest trends in co-working, with access to the best technology and mentoring, where participants can interact with other projects and use connectivity facilities for connecting with the other countries where Wayra is present. The goal is to capture talent and support its growth, providing entrepreneurs with a comprehensive model for fast-tracking technological projects.

Telefónica's commitment to the creators of start-ups is not limited to financing. Instead, it accompanies the entrepreneurs from the very beginning, identifying their needs and helping them to cover them through administrative support, legal advice, training in the different areas of a business and top-level technological support, which one of the world's best telecommunications companies can provide through its R&D team. It does all this with the goal of making these start-up projects commercially viable.

The greatest distinctive factor of Wayra as an accelerator of the digital world is found in its comprehensive entrepreneur support model and its global footprint, providing beneficiaries not only with financing, but also with expert advice from mentors, specific training for their business sector and a space at the Wayra Academies, as well as access to Telefónica's world-wide customer base of over 300 million customers.

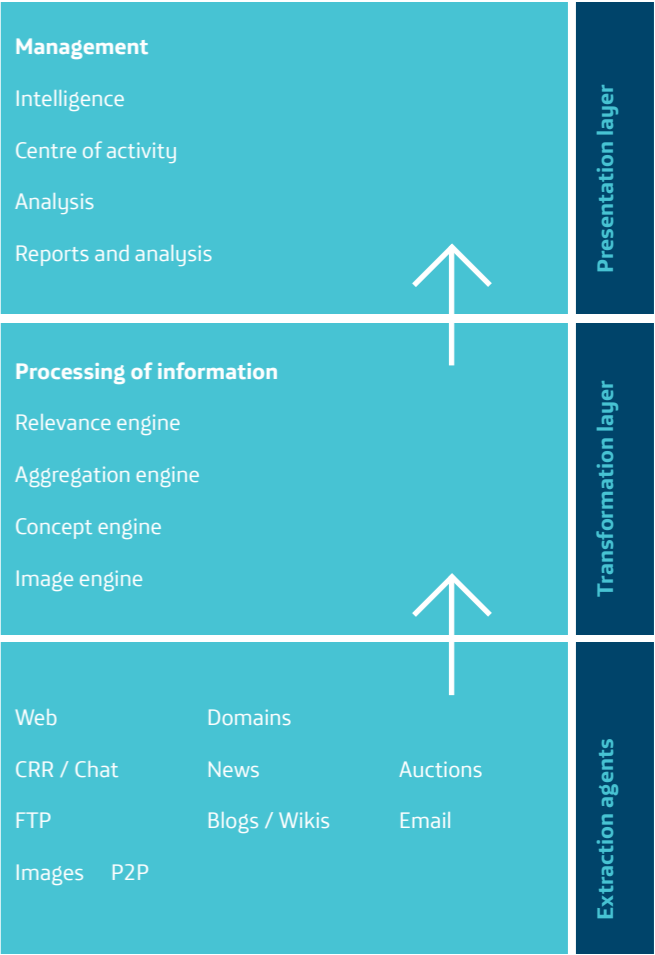
Network security

At Telefónica, we are fully committed to providing a reliable and secure environment for our customers, employees and any other stakeholders that are related to the Company.

In this respect, we have been developing different initiatives aimed at strengthening the digital trust which must arise among users of the services. Telefónica's Security Committee has been fostering the constant improvement and modernization of the technical testing of the telematic network and of the services in general that we provide, using a two-pronged approach based on the services for identification and management of threats on Internet.

Since its creation in 2005, the objective of SIGA, the Corporate Security Service, has been to identify threats and relevant information that could have an impact on the security or value of Telefónica and its customers: fraud, cybercrime, threats against the company or its workers, inside information about the company published on the Internet, the fight against child pornography and others of a diverse nature. The service addresses common Internet security problems that can affect both our customers and our professionals and the reputation of the Company. Some of its responses are:

- **Mitigating fraud**, through identifying information aimed at creating fraud against the Company, through the fraudulent sale of Telefónica products or services or other actions that harm it or its products.
- **Preventing "cybersquatters"**, by registering and maintaining web sites with names that bring to mind Telefónica commercial brands, products or services and that could confuse customers or represent indiscriminate criticism of Telefónica.
- **Analysing the Indirect Channel of sales**, by identifying the degree to which the style guide is followed by authorised distributors and identifying non-authorised or fraudulent distributors.
- **Fighting cybercrimes and cyberterrorism**, by identifying actions and information both in Telefónica websites and in external web pages.
- **Identifying confidential information and customer information**, by identifying confidential information belonging to the company, or to its customers, located on the Internet.
- Protecting children and fighting against child pornography, by identifying on Telefónica sites information referring to illegal actions associated with children about bullying, content about minors and child pornography. Identification results in the immediate reporting and withdrawal of the information.



- **Reinforcing corporate and brand reputation**, by safeguarding the proper use of the brand on the Internet, identifying when it is being used against the company and identifying variables that define the positioning and value of the company with respect to internal systems, based on Reprack methodology.
- **Helping the business**, by identifying the correct performance of the online indirect sale channel and including the monitoring of distributors and offers, also identifying false distributors and/or products.
- **Allowing greater cooperation with judges and state security forces**, by extending Telefónica's security services to the Spanish state security forces, maintaining a cordial and effective relationship consisting of exchanges of information about identified offences that affect the company or society.

Responsability in the supply chain



Telefónica creates a framework that promotes the sustainability of its suppliers, thus multiplying the positive impact of our activity. This is in response to its commitment to generate improvements in the living and working conditions of the people participating in our supply chain.

At Telefónica we are aware of the impact of our supply chain, a supply chain which in 2011 had a purchasing volume of €27,295 million assigned to over 14,500¹ suppliers in more than 80 countries. Therefore, more than 243,000 people from allied suppliers² were key in our customer care and support operations, working in direct contact with our customers.

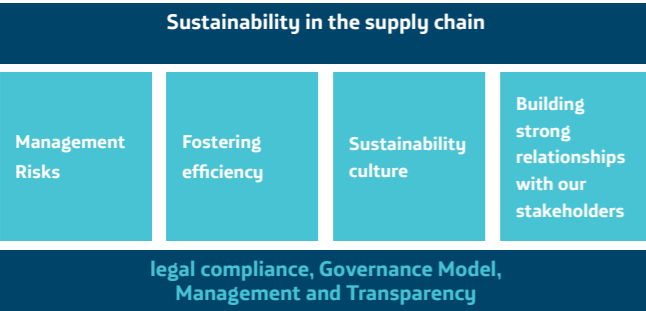
All these factors lead us to continue promoting and ensuring compliance with the sustainability criteria contained in our Business Principles, thus multiplying the positive impact of our activity. This attitude is not due to business compliance factors, but to our commitment to generate improvements in the living and working conditions of the people participating in our supply chain.

Based on the commitment assumed with the **Global Compact** and the **Millennium Development Goals**, we are looking for more efficient and innovative production processes that help achieve a better, more sustainable world.

Objective

To manage the main pillars of sustainability in the supply chain, on the basis of the Group's purchasing management model, legal compliance and transparency. These pillars allow us to minimise our negative impact while at the same time fostering innovation and efficiency:

- ➔ **Risk management.**
- ➔ **Promoting efficiency.**
- ➔ **Sustainability culture.**
- ➔ **Building relationships with our stakeholders.**



Applicable Regulations

Our frame of reference is the public commitment made in 2010, which is published in the Supplier Portal (<http://www.telefonica.com/es/suppliers/html/home/index.shtml>). That commitment is developed on two levels:

- ➔ **External:** through the Supply Chain Responsibility Policy, which describes the attitude and standards that we expect from suppliers. Furthermore, the policy is an awareness-raising tool which helps us to foster sustainable behaviour within our suppliers' own supply chains.
- ➔ **Internal:** through internal standards, such as the Rule of Extending the Business Principles to the Supply Chain, Purchasing Instructions, Corporate Regulations on Control and the Environmental Management Requirements for Suppliers³, where the processes, indicators and tools to monitor the suppliers' level of compliance are stipulated.

Lines of initiative pursued in 2011

Governance Model and Transparency

Telefónica carries out its purchasing operations using a common management model which is based on the following principles: competition and equal opportunities; transparency in the process and in decision-making; objectivity and unanimity in decisions to award contracts; commitment to serving internal and external customers; mutual fulfilment of commitments with suppliers.

In the last few years, we have witnessed the advantages that can be achieved through electronic management of the purchasing and supply chain. In 2011, 91% of negotiations were carried out electronically and 18% of these were auctions. We issued orders and award letters electronically for more than €8,500 million and received electronic invoices amounting to over €7,400 million.

In 2011, our main suppliers by volume awarded were Apple, Ericsson, Huawei, Samsung, Nokia, Atento, Nokia Siemens, Rim, Alcatel-Lucent and Sony Ericsson.

Within the Group, there are two key companies involved in managing the supply chain:

- ➔ **Telefónica Compras Electrónicas (TCE)** is in charge of managing the e-commerce platform and deploying electronic tools in the purchases of all the products and services in all the Group's companies.
- ➔ **Telefónica Global Services (TGS)** is responsible for encouraging global management of the main purchases of the Telefónica Group, through its provision of value-added services focusing on strengthening and simplifying relations with our main suppliers. In 2011, in addition to its previous management scope, which included purchases of network infrastructures, customer devices and information systems, TGS incorporated the purchasing of services.

In 2011, we negotiated more than 18,000 purchasing processes amounting to over €13,300 million euros through TGS.

Risk management

We carry out periodic assessments of our suppliers' risk levels, according to the product and service they provide, so as to define a strategy that is commensurate with the risk detected:



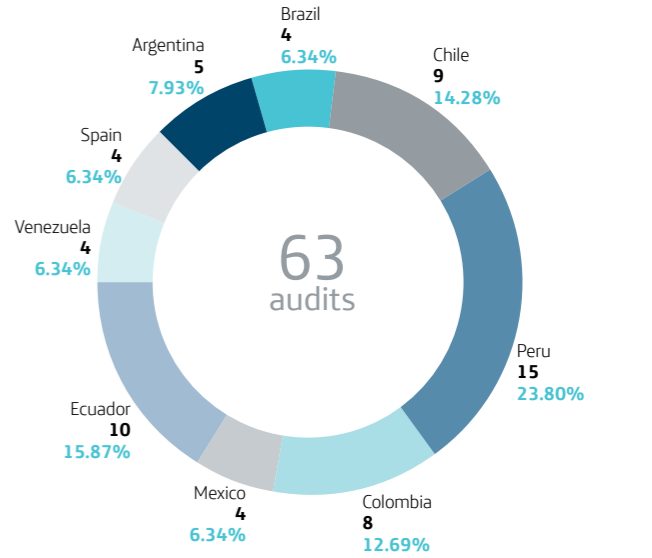
Different risk levels are identified for our suppliers, in accordance with the geographical region:

- ➔ **Europe:** Manufacturers of network infrastructure equipment and terminals.
- ➔ **Latin America:** Outsourcers and call centres (both technical and commercial).

As a result of this assessment, the Annual Audit Plan for the Group in 2011 was made up of more than 1,770 audits on at-risk suppliers.

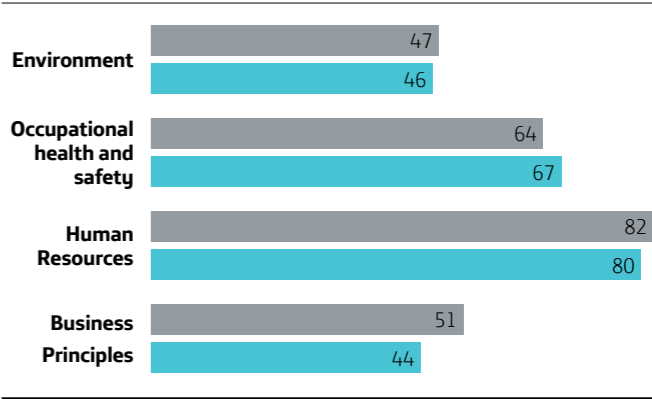
We also progressed in the use of the global check-list, with 63 audits throughout the Group (70% more than the 2010 Annual Audit Plan). The check-list allows us to compare the performance of suppliers based on the same criteria. The following graphs contain the work undertaken by country and the compliance levels observed in those audits:

Distribution of audits by country (*)



(*) Audits corresponding to the 2011 Annual Plan

Level of compliance observed



1. At Telefónica, we have carried out an in-depth review of our corporate catalogue of suppliers, closing 2011 with 14,529 certified suppliers in accordance with the Group's integrated systems.
2. In 2008, the Telefónica Group launched its Allies in Latin America programme ("Programa Aliados en Latinoamérica") to work in close collaboration with suppliers that provide services through direct contact with its customers.
3. ICC-001 *Instrucción Conjunta Corporativa* (Corporate Joint Instruction) for the monitoring of labour risks when contracting goods and services
NCC - 003 *Normativa de Criterios Generales* (General Criteria Regulations) on contracting goods and services

EUROPE

Telefónica UK led the process. It carried out eight on-site audits of key suppliers in the sector, undertook assessments of potential suppliers and monitored improvement initiatives at 15 large suppliers.

The most significant points of the audits were as follows:

- ↳ The majority of suppliers complied with the stipulations of the Group's Supply Chain Responsibility Policy.
- ↳ In the event of a failure to comply, all the suppliers put in place improvement plans. There are currently 15 plans underway.
- ↳ The weakest aspect that we found in those companies was the lax management or total lack of management of their own supply chain.
- ↳ Other relevant aspects, although uncommon, related to unacceptable working policies, such as withholding ID cards or setting fines as disciplinary measures.

As part of the 2011 Annual Audit Plan, Spain carried out four audits, in accordance with standardised Group methodology, on suppliers of market products, network infrastructure, call centre services, and advertising and publicity. The following graph shows the level of compliance.

Spain - 2012 Audit Plan. Level of compliance



LATIN AMERICA – ALLIES PROGRAMME

We consolidated this programme as one of the best practices in the Group for Supplier Management, something which takes on even more relevance when it is noted that the number of Allies in the region increased by 18.5% compared to the previous year.

This is why we maintain our ambition of being recognised for our sustainable model of strategic alliances with our third-party suppliers which allows us to provide our customers with an excellent and coherent service.

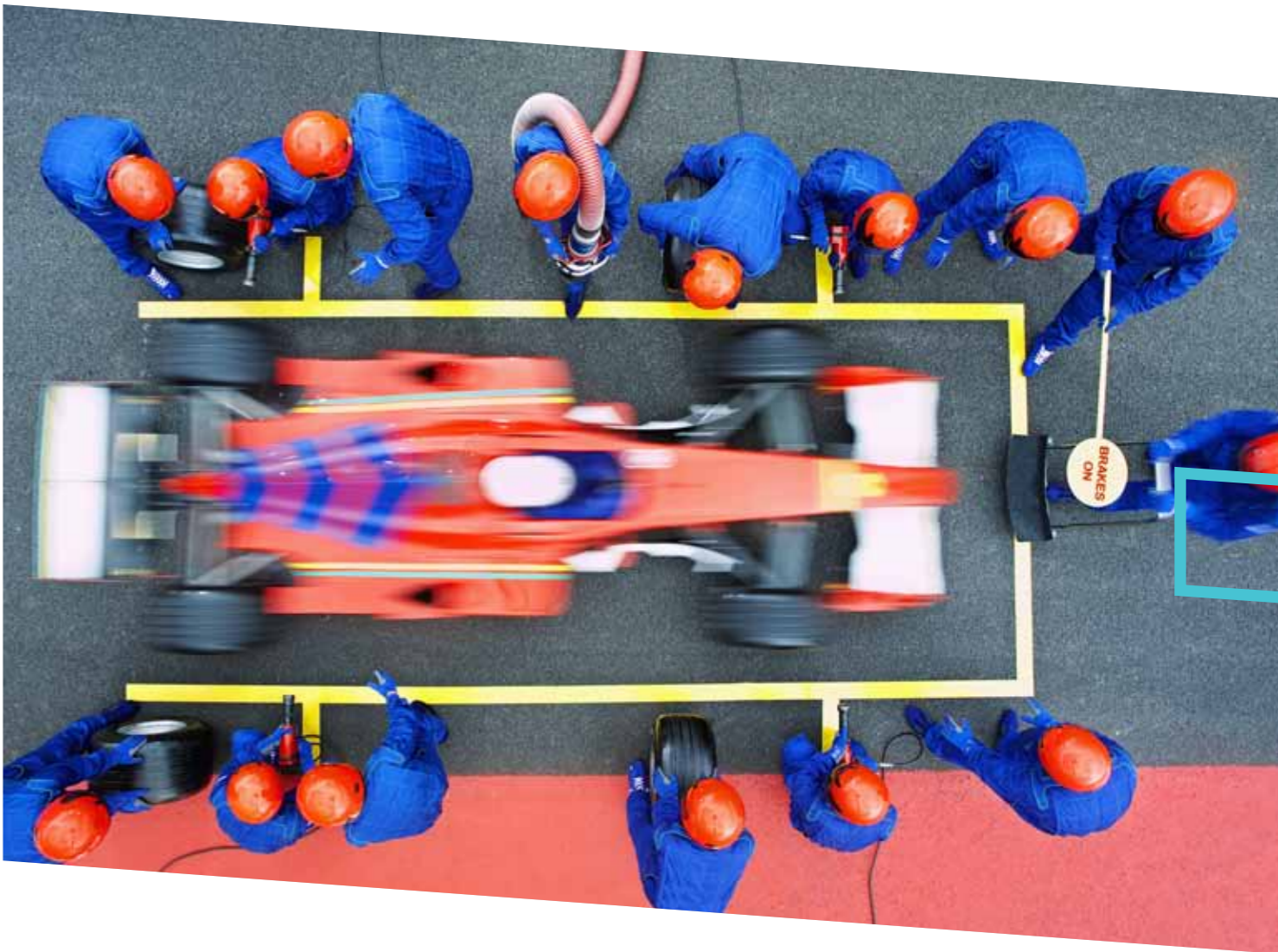
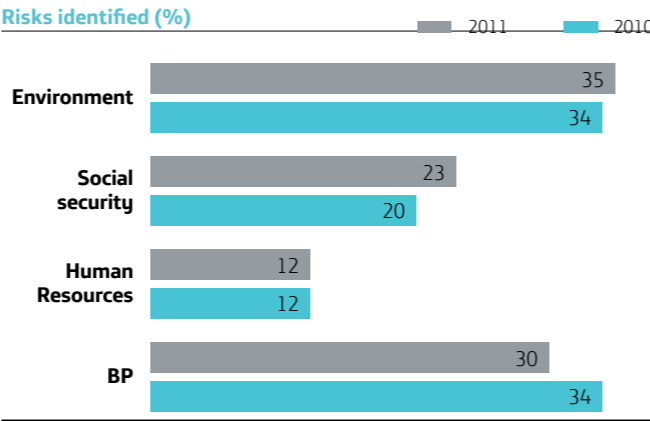
In 2011, we continued to progress in implementing the Comprehensive Ally Management Model:

- ↳ Ensuring compliance with labour regulations and contractual obligations
- ↳ Encouraging the development of collaborating companies.
- ↳ Becoming the sole platform for managing Allies.
- ↳ Promoting the Group's Business Principles.
- ↳ Developing a Regional Scorecard to make reporting and monitoring of the programme easier.

If in previous years we focused on monitoring compliance with labour regulations, in 2011 we concentrated on the sustainable development of suppliers. In this respect, we must highlight Argentina, where the conditions of a contract, which had already been awarded to a loop supplier, were varied so that in addition to ensuring the sustainability of the supplier, the development of its employees was also guaranteed.

Main indicators of the Allies programme:

- ↳ Administrative reviews: 13.171.
- ↳ On-site audits: 1.702.
- ↳ Corporate audit checklist: 59 - the attached graph shows the main risk areas.
- ↳ Suppliers with Non-Compliance gradings: 292.
- ↳ Improvement plans underway: 178.



Promoting efficiency

At Telefónica, we believe that all companies can influence, within the scope of their own supply chains, the search for more efficient and less costly processes, that lead to the sustainability of the communities where we act.

As regards energy efficiency, the Group's Climate Change Office works along three lines:

- ↳ a. Incorporating and requesting energy efficiency requirements in the TCO4 of network products.
- ↳ b. Homogenisation of criteria and prices in energy purchasing decisions
- ↳ c. Inclusion of energy efficiency criteria in the standardisation of network equipment.

More information is given in Environmental Dimension.

The Allies programme (Programa Aliados in Latin America) cemented its status as one of the best practices in supplier management. Over 243,000 allied workers provided customer care directly to our customers



Sustainability culture:

For Telefónica, sustainable progress is based on creating value and our suppliers are strategic allies in achieving this objective. Sharing a single vision and applying the same values and principles will allow us to work on a daily basis to maximise our contribution to society. For this reason, there are numerous initiatives in our business lines, which are aimed at:

- 1. **Training our teams.** Within the Allies programme, there are training schemes for contract managers. Particularly noteworthy in 2011 were:
 - a. **Chile and Colombia:** Diploma in Business Management for contract administrators.
 - b. **Ecuador:** training and certification for the company's contract administrators, with a total of 164 participants.
 - c. **Venezuela:** certification of the Complete Leader programme, with 13 training sessions given and 222 participants.
- 2. **Training our suppliers and other partners.**

In addition, within the Allies programme there are regular training courses and communication initiatives with suppliers, such as:

- d. **The iCampus platform:** This is an e-learning portal, where we make available to our allies training about our business principles, purchasing processes, products, services and

commercial offerings. This service is available for call centres and for companies who provide on-site services. At the current time, it has been rolled out in four countries and has over 11,018 active users.

- e. **Argentina:** All labour-intensive service contracts require a plan for training provided by the supplier, which is monitored by compliance controls. In many cases, these are systematised by the supplier, by following quality methods such as ISO, COPC, PNC and other methods. In 2011, an average of 385,000 hours of training were given.
- f. **Chile:** We must highlight the inclusion in the "Imagina" organisational culture workshops of the leaders of strategic allied companies. There was participation from contract managers and administrators that allowed strategic alignment with the Company, approximately 200 people.
- g. **Colombia:** Telefónica signed an agreement with SENA "Servicio Nacional de Aprendizaje" (an institution belonging to the government and responsible for training in the country) that helps to certify the professional skills of loop-service workers. At the current time, more than 1,000 technicians have been certified.

Building relationships with our stakeholders

- a. **Meeting our commitments:** we are working to improve invoice management, in order to meet the commitments undertaken.

According to the information in the financial report, the Telefónica Group's Spanish companies have adapted their internal processes and payment schedules to the provisions of Law 15/2010, which

establishes measures against late payments in commercial transactions. To this end contractual conditions with commercial suppliers in 2011 have included payment periods equal to or inferior to 85 days, as established in the regulation.

Millions of euros	2011	
	Amount	%
Payments made before deadline	8,361	95.2
Other	425	4.8
Total payments to trade creditors	8,786	100.0
Weighted Average Excess Period (days)	38	
Postponements which at the closing date had exceeded the timeframe (*)	27	

(*) With the object of adapting to the provisions of Law 15/2010, the Spanish companies of the Telefónica Group paid in the first few days of 2011 an amount of €82 million which corresponded to the outstanding balance awaiting alignment at the close of 2010.

- b. **Collaborating with other organisations to improve the impact of our supply chain:** we are collaborating with organisations such as Green Choice Alliance, OK International or Forum Empresa.

In the last case, we have fostered the study of sustainability and call centres, where quantitative and qualitative information is collected on how to combine outsourcing and subcontracting such that the end customer "lives" the company's CSR policy. (www.empresa.org/Estudios2011/sustentabilidad-callcenters-esp.pdf)

- c. As founding members of the Global e-Sustainability Initiative (GeSI), we encourage the use of E-TASC5 among our main suppliers. In 2011, we monitored the compliance level of our main suppliers by volume and activity risk in this tool.
- d. Establishing alliances to achieve a greater impact:
 - i. Globally: Public-Private Alliance for Responsible Minerals Trade
Telefónica is part of the Public-Private Alliance for Responsible Minerals Trade - a joint initiative by the U.S. Department of State and private-sector ICT companies and trade associations and civil society - and of the International Conference on the Great Lakes Region.

4. TCO: Total Cost of Ownership: this is a calculation method designed to help users and business managers to determine direct and indirect costs, as well as the benefits, related to the purchase of equipment.
5. E-TASC: Electronics - Tool for Accountable Supply Chains is a self-assessment tool that allows a homogenous assessment, unique for all subscribing customers, of the level of compliance with labour, ethical, environmental and health and safety standards.
6. Fenattel: Federação Nacional dos Trabalhadores em Empresas de Telecomunicações, an entity which represents the workers in the sector in Brazil
7. Febratel: Federação Brasileira de Telecomunicações, the entity which represents employers from the telecoms sector

For Telefónica, sustainable progress is based on creating value and our suppliers are strategic allies in achieving this objective

LESSONS LEARNED

Audits are not enough to ensure the sustainability of the supply chain
Collaboration between sector companies and other organisations is also necessary.
Promoting training arising from and among our suppliers

CHALLENGES 2012

Fostering collaboration among sector companies to improve the results and efficiencies of evaluations and audits of suppliers.
Moving forward in implementing the Rule of Extending the Business Principles among our at-risk suppliers and/or strategic suppliers

- It is thus consolidating earlier initiatives by different organisations which have enjoyed limited success, such as the iTSCi project, which Telefónica has been involved in for the past two years. For more information: <http://www.resdue.org/site-pqa>
- ii. Locally: Brazil: An agreement was entered into between Fentattel6 and Febratel 7 - headed by Carlos Antonio Valente, chairman of Telefónica Brazil - to guarantee best practices for action in the telecommunications industry at national level.

Triple Bottom Line
Environmental dimension



Green ICT at Telefónica



Telefónica's environmental and Green ICT strategy focuses on management of waste and energy efficiency opportunities, reduction of Greenhouse Gases (GHG) and optimisation of resources.



At Telefónica we view Green ICT as an additional set of processes and activities that allows us to generate value for the company by reducing costs and creating new revenues. It depends on the principles of eco-efficiency, internal carbon management and reduction of energy consumption. The company also offers its customers green ICT services that promote environmental sustainability and a low-carbon economy.

The ICT sector has the potential to dematerialise the economy. Aware of this, we must seize the opportunities that come with the need to manage energy, carbon and climate change. To do this, Telefónica's Climate Change and Energy Efficiency Office is directing the group's corporate energy and carbon strategy in five main areas: operations, employees, purchasing, customers, and positioning.

In 2011, Telefónica's Green ICT strategy was consolidated into a single model based on three main strategic themes: Green from ICT, Green by ICT and Global Green ICT.

Our **Green ICT 2011** strategy aimed at three mutually compatible targets. First, we wanted to improve energy efficiency within the company and reduce our CO₂ equivalent emissions, by optimising the use of global resources available and creating economies of scale. Second, we looked at developing competitive Green ICT solutions that would make our customers more eco-efficient based on a strategy of global service provision in the digital world. Thirdly, we sought to position Telefónica as the global, regional and local leader in Green ICT.

GLOBAL GREEN ICT Telefónica's Global Positioning

We are well aware of the ICT sector's transformative potential to create an eco-efficient⁽¹⁾ low-carbon economy. The challenges posed by the digital world and the scarcity of natural resources such as energy present us with an opportunity to re-invent our Green ICT business model at global and local scales. The model starts from the global energy, environmental and climate change agenda and looks to the solutions Telefónica can deliver to its stakeholders: the markets where it operates, its shareholders and investors, the ICT sector and its analysts and, most importantly, its customers.

To do this, we pursue an active policy of global positioning, based on four fundamental pillars.

- ⇒ Trust and transparency
- ⇒ Green ICT standards
- ⇒ Green ICT Innovation
- ⇒ Policy advocacy

Trust and transparency

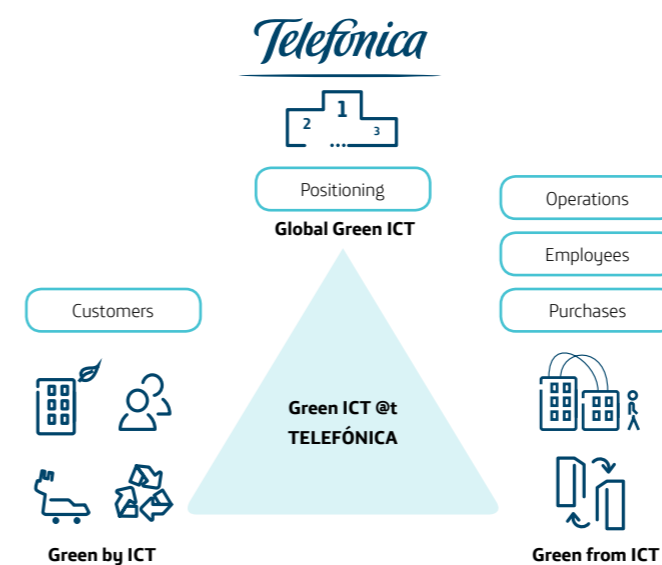
We consider that the best way to lead is to generate trust and be transparent about what has been achieved. Transparency on climate change goes hand in hand with a clear assessment of risks and opportunities, process-based management and an accurate allocation of responsibilities.

In 2011, we made progress on identifying the risks and opportunities that climate change offers Telefónica as part of the company's global risk model. These included regulatory, business, operational and reputational risks that could impact earnings unless they are properly managed. As it stands, management of energy and climate change in the companies is generally discretionary. However, one of the main risks identified is that the ICT sector may move toward a regulated process of emissions quantification, perhaps leading to compulsory reduction targets in the future.

Our first task if we are to manage the identified risks is to accurately measure the energy that we are using and quantify the carbon footprint of the company and its services. This has allowed us to take the right decisions and lay out our route map for 2015.

As a listed global company, we have seen how over the last few years investors and shareholders are attaching increasing importance to the environmental management of firms and particularly to energy and climate change issues. In Telefónica, for instance, we have over 1.4 million shareholders who expect us to provide transparent, accurate and positive information, not only on our financial liabilities but also on energy efficiency and green business as these too affect earnings. Telefónica provides shareholder value through a strategy of energy efficiency and action against climate change which is both clear and appropriate to the world where the company operates. One indication of our success is that in 2011, for the second consecutive year, the Carbon Disclosure Project (CDP) gave us the highest score in the telecommunications sector.

¹ Eco-efficiency: efficient management of environmental issues such as water, energy, waste and greenhouse gases, among others.



Telefónica ranked top by the Carbon Disclosure Project (CDP)

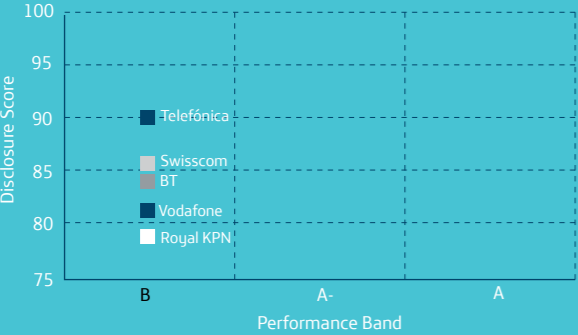
CARBON DISCLOSURE PROJECT

In 2011, for the second year running Telefónica received the highest CDP score in the telecommunications sector. The CDP is composed of two indexes which list 551 institutional investors with 71 billion dollars under management and rate companies' transparency and performance vis-à-vis climate change.

With a score of 90 points out of 100 - one point more than last year - Telefónica is the only Spanish company listed on the **Carbon Disclosure Leadership Index (CDLI)**, which measures the quantity and quality of the information that companies provide on climate change.

Energy management and CO2 emissions, green services and, in general, the utilisation of opportunities and the minimisation of risks associated with climate change were key to achievement of this position on the leading carbon investment index.

Top disclosure scores vs. top performance bands



In 2011, we worked to meet all milestones set by our Green ICT strategy, including producing the annual report for shareholders and other corporate reports. In 2011 also, we upgraded our web 2.0 global channels for information and debate on energy efficiency and Green services, particularly for our customers. In 2012, we will continue to communicate effectively on our global processes for managing energy, carbon and Green ICT.

Green ICT standards

If we are to realise the benefits of the ICT sector for a low-carbon economy, we need standards or methodologies that allow comparisons across companies and between Green ICT services. In 2011 we continued to contribute to the International Telecommunications Union's Standardisation Sector (ITU-T) study group 5 on the "Environment and Climate Change"⁽²⁾, charged with drafting methodologies to measure the environmental impact of ICT.

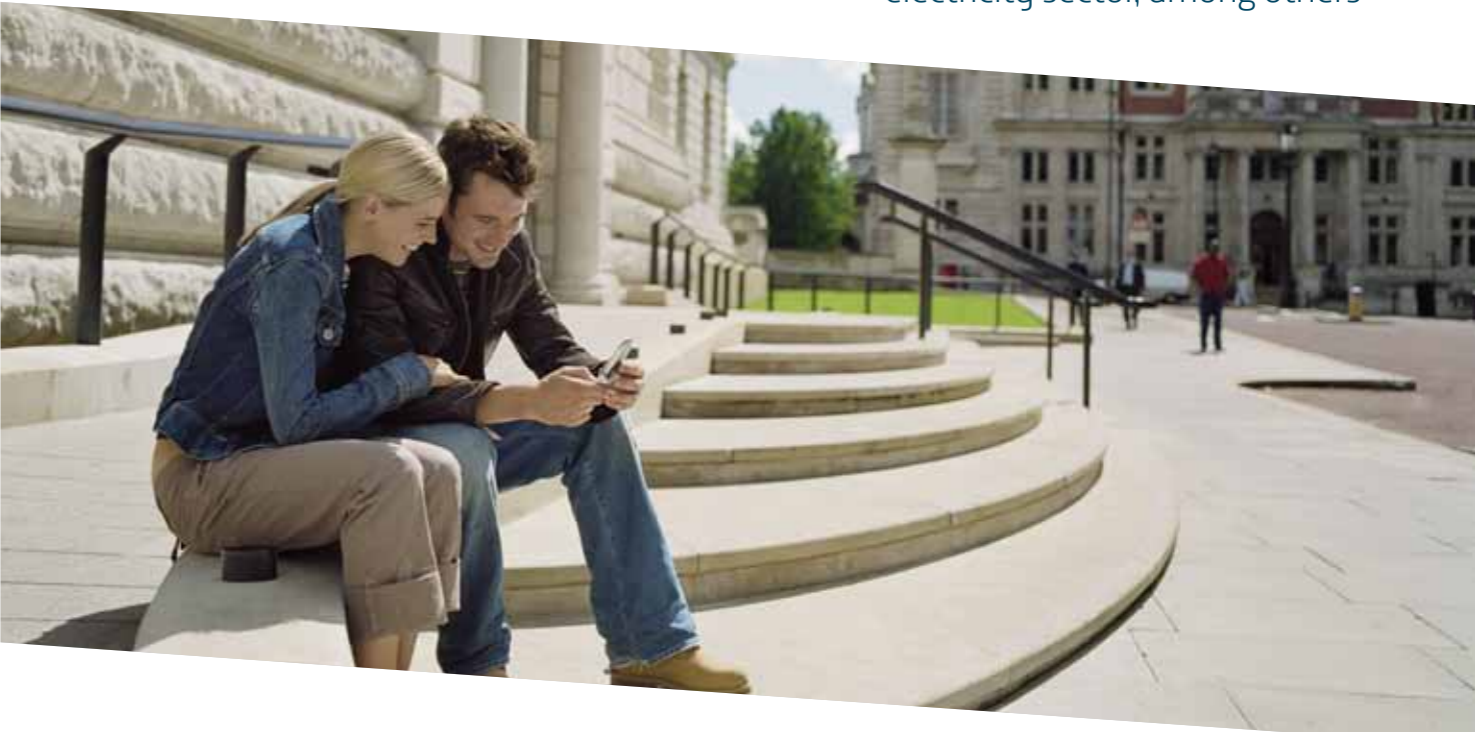
At Telefónica we recognise ITU as the standard-setting body mandated to organise, lead and promote standards and methodologies for Green ICT worldwide. 2011 marked a major milestone for methodology in Green ICT. Three recommendations were approved for the ICT sector which will directly impact telecommunications.

ITU recommendations for Green ICT – 2011

- ⇒ **(May 2011) ITU-T Recommendation L1000:** Standard for the universal charger and charging solution for mobiles and other ICT hand-held devices: This lays down general specifications for a single charger that will fit all mobile handsets, including: an "independent" micro usb cable which can be used with other equipment (mp3 players, cameras, GPS), a maximum load of 0.03 W for the adapter when the mobile is not connected, and a recommended charging current of between 750 and 1500mA.
- ⇒ **(Sept. 2011) ITU-T Recommendation L.1410:** Methodology for environmental impact assessment of information and communication technology goods, networks and services. This establishes a methodological framework for quantifying energy consumption and greenhouse gas emissions by ICT using life-cycle analysis (LCA).
- ⇒ **(Sept. 2011) ITU-T Recommendation L.1420:** Methodology for energy consumption and greenhouse gas emission impact assessment of information and communication technologies in organisations. This defines the methodology for ICT companies compiling an inventory of energy and greenhouse gas emissions.

2. ITU: International Telecommunications Union. UIT-T: the ITU's telecommunications standardisation sector. (N. de las T.)

Telefónica's challenge is to incorporate green and energy efficiency concerns into ICT services for buildings, transport and the electricity sector, among others



These standards mark the start of a methodological process that will make Green ICT part of the solution to issues of energy efficiency, greenhouse gas emissions and electrical and electronic waste.

In 2012, Telefónica will continue to work with the ITU on developing a second set of methodologies to quantify the environmental impact of using Green ICT worldwide, with a special focus on cities. In 2012, Telefónica will have to include the universal charger recommendation among its mobile standardisation and purchasing processes for our more than 306 million customers.

Green ICT innovation

Many think that the economic crisis has pushed Green agendas onto the back burner. The ICT sector in general and telecommunications in particular has proved an exception. We have instead emphasised the business opportunities offered by energy efficient services, which can help cut costs and make our customers more competitive. The development of Green technologies goes hand in hand with successful business models based around innovation and understanding the market. Telefónica's challenge is to incorporate green and energy efficiency concerns into ICT services for buildings, transport and the electricity sector, among others.

Telefónica's global innovation strategy aims to realise the possibilities of a new digital world and to be one of its leading players. In 2011 the Telefónica's R&D team alone invested €15 million in innovation processes for energy efficiency (transport, utilities, smart buildings), especially M2M-based services.

Green Quadrant: Sustainable Telecom Companies

Verdantix is one of the leading analyst firms in the industry for assessing green and sustainability issues in the ICT sector. Verdantix compared the solutions of 18 telecommunications operators and analysed their answers to more than 40 questions about their offerings for virtual meetings, virtual hosting, cloud computing, smart metering and M2M solutions. The survey included questions about the business strategy for energy efficiency, carbon management, innovation and sustainability and interviews with 15 buyers of telco services, representing revenues of more than €175 billion.

Telefónica's top scores according to Green Quadrant Sustainable Telecoms 2011" are: a) availability of energy efficient services, notably smart building services, smart metering and M2M, virtual hosting, and green mobile services with efficient devices, b) energy efficiency and climate change strategy integrated with the heart of business development and c) corporate governance model to manage energy and greenhouse gas emissions and support the achievement of global targets.

BeyWatch Project

The European BeyWatch Project (**Building an Energy Watcher**) came to a successful conclusion at year-end. This was a research project spearheaded by Telefónica's R+D unit, the purpose of which was to create and demonstrate new technological solutions paving the way towards a sustainable energy system. BeyWatch is a trail blazer for Smart Energy, the new electrical system paradigm which integrates renewable energy sources, distributed and intermittent generation and new consumer models (mobile chargers such as electrical vehicles and consumers that also produce energy). It also requires the Smart Grid, which incorporates the consumer into the system's operation through **Active Demand Management**.



Thanks to the implementation of these processes and the bringing to market of several Green ICT services, we were recognised in 2011 as Europe's leading telecommunications company for energy-efficient solutions promoting sustainable business, according to the "green quadrant" report by Verdantix. Telefónica was among five global companies operating in Europe found to best integrate energy efficiency and sustainability criteria into products and services.

As part of its Green Innovation outlook, Telefónica has set up service demos at its innovation centres in Madrid and Barcelona. These recreate innovative Green ICT services in connected cities, including M2M telemetering, energy efficient building management services, NFC-based solutions, electric vehicles, and others.

In 2012, all Telefónica's Green ICT services must be able to measure their benefits for energy and greenhouse gas emissions. This will naturally attract the market's attention and drive innovation, investment and the development of new Green ICT.

Policy advocacy

Green ICT is fundamental to stimulating global competitiveness in cities and strategic sectors of the economy. One way to do this is by developing energy efficient services, applications and devices, running across energy-efficient telecommunications networks. At Telefónica we recognise that we can contribute to global efforts to

mitigate and adapt to climate change and to the implementation of joint initiatives aimed at reducing greenhouse gas emissions.

To make this happen, we are involved in several cross-sector groups which seek to put green ICT on the climate change policy agenda and to foster environmental sustainability on a global scale. Success will depend, we believe, on working with the ICT sector to identify the best ways forward. In 2011, we took part in several cross-sector working groups that sought to position Telefónica and the ICT sector at the heart of the solution to climate change. In 2012 we will continue in this direction.

To take forward the Green ICT agenda at the top level of the global climate agency, particularly on issues of adapting to climate change, Telefónica is working through the Telefónica International Wholesale Services (TIWS) on the *Task Force to assess the potential of submarine cables in controlling the climate and oceans*, a project sponsored by ITU, the World Meteorological Organisation, and Unesco.

Green from ICT

We are working at global level with the operations, purchasing and human resources departments to promote internal energy efficiency and reduce greenhouse gas emissions from our processes.

The Company contributes to a number of intersector working groups to put Green ICT on the political agenda for climate change

As every year, we quantify our energy resources and our internal carbon footprint on the basis of a global model based on the GHG Protocol and ISO 14064. In 2011 our inventory was calculated on the basis of the recently approved ITU-T L. 1420 Recommendation: *"Methodology for energy consumption and greenhouse gas emissions impact assessment of information and communication technologies in organisations"* issued by the International Telecommunications Union (ITU). The baseline year for our greenhouse gas emissions is 2010, due to the quality of data available and first-time consolidation of Telefónica-Vivo (Telefónica Mobile's subsidiary in Brazil).

Telefónica: leadership and active participation in strategic forums and working groups.

ITU	Group Nº. 5 of the ITU-T on Environment and Climate Change (ITU SG5): developing Green ICT standards and methodologies.
GESI	Climate Change Group of the Global e-Sustainability Initiative (GeSI): thinking through the sector's global positioning.
ict4ee.eu	Group Nº. of the ICT4EE Forum: leading the energy efficient products and services group.
GSMA	Green Power for Mobile and the GSMA's Energy Efficiency initiative: developing energy efficiency and renewable energy projects.
Etno	Sustainability and energy groups for the European Telecommunications Operators Network (ETNO), positioning operations as ICT leaders on Green issues.
ERT	The European Round Table of Industrialists (ERT) Climate Change working group: working with other sectors of the economy on their climate change agendas.
E3	Founding members of "Companies for energy efficiency in Spain" to foster joint initiatives towards better energy efficiency for businesses and end customers.

Energy	Measurement unit	2010	2011
Fuel consumption by vehicle fleets (petrol and diesel)	Thousands of litres	24,843	22,882
Biofuel consumption by vehicle fleets (ethanol and biodiesel)	Thousands of litres	1,640	928
Fuel oil consumption: operations & offices	Thousands of litres	18,363	16,011
Natural gas consumption: operations & offices	Nm3	6,623,162	5,413,698
Electricity consumption: operations	MWh	5,099,303	5,269,807
Electricity consumption: offices	MWh	770,323	739,645
Renewable energy generated and purchased	MWh	677,904	743,585
GHG emissions			
Direct emissions (Scope 1)	tCO2eq	126,247	112,377
Indirect emissions (Scope 2)	tCO2eq	1,602,769	1,615,732
Other indirect emissions (Scope 3)	tCO2eq	49,300	52,207
Emissions saved	tCO2eq	244,626	272,033
Total emissions	tCO2eq	1,778,316	1,780,316



In 2011 the Group's GHG emissions totalled 1.8 million tonnes of CO₂, an increase of 0.4% on 2010, mainly due to an increase in our customer base worldwide. Nearly 85% of our greenhouse gas emissions were indirect emissions from energy consumption from networks that represent an annual cost of 600 million euros.

Operations: energy efficiency and savings

In 2007 we established an undertaking to reduce our energy consumption by 30% (measured in kWh/equivalent access) by 2015. At the end of 2011 we had already achieved 20% of our long-term objective.

We are sure that, to attain excellence in management of energy and carbon, and to achieve the objectives of the company, it is vital that third parties be able to verify the objectives. Absence of data in measurements of our emissions would entail non-compliance with corporate goals, and future non-compliance with possible standards in relation to the measurement of emissions or compulsory objectives to reduce levels of CO₂.

Each year Telefónica carries out an independent audit of energy use and emissions data based on global procedures for drawing up inventories of energy and CO₂. What cannot be measured cannot be managed or improved. Hence the importance of compiling a scorecard. A high-quality emissions inventory is key to measuring progress and meeting targets.

In 2011 we carried out more than 30 global energy efficiency projects on our networks, culminating in an energy expenditure reduction of €7.6 million, a reduction of 68 GWh and approximately 24 kTonCO₂eq. The energy efficiency projects in 2011 included a number of Free Cooling processes (using exterior air to control temperature at mobile base stations and fixed-line plants) in Uruguay, Nicaragua, Spain, Argentina and Brazil.

We have a well structured corporate governance model, with an energy manager in each country and an *energy efficiency*

good practices manual (101 practices). These projects and their savings in terms of energy and emissions of CO₂ are also verified on an external basis. The Telefónica Group's energy managers are drawn from local operational staff, and are responsible for energy usage in companies in other countries. They are supported by Telefónica's Global Operations Team, and work in tandem with the Corporate Centre.

Each year, we improve our forums for exchange of best practice. All information is shared across internal social networks and at the Global Workshop on Energy Efficiency and Climate Change. In 2011 this was held in Lima, Peru, with attendance by local energy teams, technology partners and special guests. For more on this event, see: www.eficienciaenergetica.telefonica.com

Our energy efficiency strategy also encompasses our data processing centres. Currently, our data centres worldwide use 6.7% of our total electricity consumption. Telefónica therefore remains committed to signing the European Code of Conduct on Data Centres Energy Efficiency, and is currently building the most energy-efficient data centre in Spain. We are also working in sector standardisation groups to set specific energy efficiency metrics for data centres.

In 2011, Telefónica used the GSMA energy efficiency service to help improve the energy efficiency of our operations by drawing comparisons between countries and with competitors. This identified major opportunities to make savings, particularly in the group's global mobile operations. In 2012, Telefónica will prioritise investments in energy efficiency based on the results of these projects.

With regard to fuel, in 2011 we consumed 16 million litres of fuel-oil, mainly providing back-up power supplies. To reduce our GHG emissions from this source we have drawn up a specific plan that includes extending our energy efficiency best practices and using renewable energies as an alternative power source.

At Telefónica, we see renewable energy as one of the best ways to cut our global carbon footprint.

We are currently buying renewable energy in the markets wherever this is possible: Germany, the UK, Ireland and Brazil. In 2011 we bought some 736 GWh of energy from renewable sources, thus preventing the emission of 26.5 Teq CO₂eq. into the atmosphere.

We generate our own renewable energy at our Spanish and UK plants, and some of our plants attained almost 4.6 MWh of green energy in 2011. Telefónica has renewable energy systems in its networks, and we worked with GMSA and its "Green Power for Mobile" system in 2011 to identify base stations with potential to generate renewable energy in Latin America.



The study was carried out in Argentina, Chile, Colombia, Mexico, Nicaragua and Venezuela. It covered 127 sites and was able to identify business cases in Mexico and Colombia particularly. The potential savings from implementing hybrid (solar/wind) systems could be as much as 2.7 million dollars a year.

Details of the study can be found at: <http://www.gsma.com/developmentfund/wp-content/uploads/2012/04/telefonicasouthamericafeasibilitystudies.pdf>

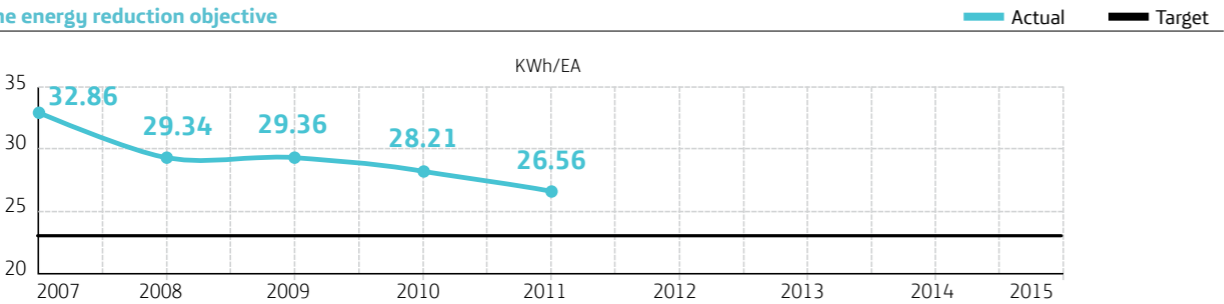
Purchases: energy efficiency in our supply chain

To make the company more energy efficient, we have instituted policies and procedures that will take account of the carbon content and energy efficiency of our product and service purchasing processes. In 2011 we stepped up our activities in three areas:

- **Incorporating and demanding energy efficiency requirements** in the TCO (total cost of ownership) of network products. Following analysis of these requirements we decided to incorporate an energy-efficiency factor into our measurement of TCO.
- **Standardisation of criteria and prices** in purchasing decisions on the energy market. For example, in 2011 Telefónica saved one million euros on purchases in Brazil's free market.
- **Energy efficiency criteria** in the standardisation of network equipment. One outstanding challenge is to have these criteria applied to customer devices.

We see our suppliers as natural allies of any company wanting to become more energy efficient. If we buy more efficient devices, infrastructure and services our bills will fall and our CO₂ emissions along with them. Extending the climate change culture to suppliers also helps create a more sustainable economy.

Trends in the energy reduction objective



Energy efficient purchasing is supported by the global sustainable purchasing project, which seeks to optimise relationships with our suppliers worldwide.

Employees: a culture of energy efficiency

In 2007, we set a target of cutting energy consumption per Telefónica employee by 10% in their day-to-day work by 2015. To move toward this target, operational teams guided by our global heads of energy are running energy-saving projects at various head offices.

The global and local human resources departments are working to promote energy-efficient policies in the office, sustainable mobility and reductions in business travel. We are also encouraging teleworking and the use of Green ICT tools for remote collaboration (video-conferencing, web conferencing and telepresence).

In 2011, the O2 UK team in its new British headquarters building carried out an exercise to measure the impact of remote working solutions for its employees.

Green by ICT

We have a global Green ICT services strategy focused on creating integrated solutions that could be used worldwide, in both developed and developing countries. This would make other sectors and our customers more efficient, and help them reduce their GHG emissions. The services also provide solutions for mitigation of and adaptation to climate change, and are clear examples of technology transfer worldwide.

In due consideration of its characteristics as an integrated world telecom operator (mobile and fixed), Telefónica has a large space for development of the Green ICT market. We are working hard to implement Green ICT solutions in our products and services catalogue for management of energy and environmental resources

in strategic economic sectors such as transport, building, industry and service companies or utilities, among others.

ICT is fundamental to improving global competitiveness, in cities and in strategic sectors of the economy. One way to do this is by developing energy efficient services, applications and devices, running across energy-efficient telecommunications networks.

In 2011, Telefónica set up two major in-house working groups to identify Green ICT services worldwide. The first was the Electric Vehicle Task Force, looking for business opportunities from electric vehicles for ICT companies like Telefónica. The second was the Smart Cities Task Force, to define a global business model for cities that would help promote global sustainability.

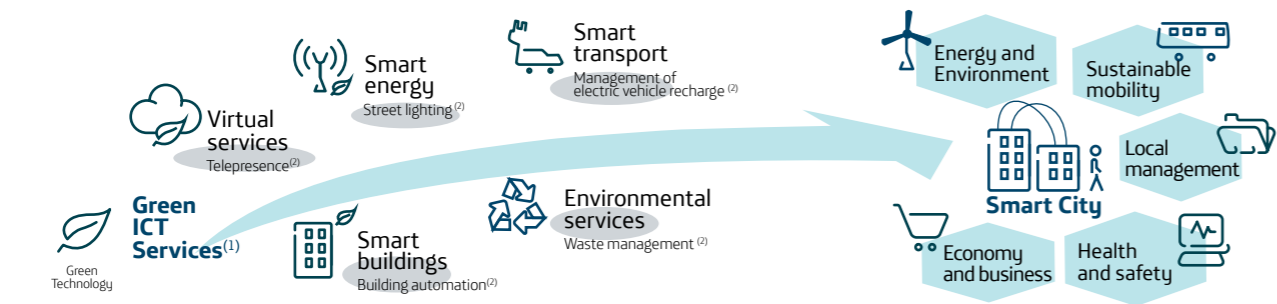
Our Green ICT services help to furnish an eco-efficient low-carbon economy, and above all assist with urban sustainability. As part of this effort, in 2011 Telefónica designed an integrated smart cities model for the whole Group.

Just over 50% of the world's population are now city-dwellers, and they are responsible for 75% of all global emissions. En masse migration to cities is expected to continue. All cities are likely to come together in adopting smart solutions, since they are the point of intersection for transport, industrial, supply network and housing solutions. Cities will inevitably become the front line of government when it comes to managing climate change issues. In the future, smart cities will define structures for energy efficiency and sustainability using ICT-based solutions.

Smart Cities at Telefónica

Telefónica's Smart Cities offer is based on an integrated vision of sustainability and Green ICT within an internal working group. Its aim is to develop a unified set of services that can be applied to smart cities worldwide, from Madrid to São Paulo.

Green with ICT (green innovation)



(1) ICT: Information and Communication Technologies (2) Green ICT Services in the market.

Examples of Green ICT services

Telefónica's Green ICT services are focused on optimising the use of resources such as energy and managing environmental issues such as water, waste, climate change etc.



Waste management in Spain

Telefónica, via Biouniversal, has taken a pioneering initiative to recycle used cooking oil, through smart containers equipped with Telefónica M2M services. This is a unique solution which enables the systematic collection of such waste for the first time anywhere in the world. The project has been launched with the first 250 containers in Cádiz and there are plans to expand it to all Spanish towns with more than 50,000 inhabitants within three years, and to other European countries thereafter.

Telefónica's intervention was essential to the project's viability. Telefónica provided the M2M services free to the containers, essential for optimal management of the system. These smart containers use an SIM card to send an SMS signal to the control centre with an identification code and data on the container, ensuring accurate information and monitoring; this means that there is no need for anyone to regularly check the status of the containers. Telefónica's M2M services provide information on how full the container is, and also trigger security alerts in the event of any unexpected event, such as a fault in the container, robbery, movement, etc.

Electric vehicle recharging point

Telefónica believes it can provide a number of ICT solutions to support penetration of electric vehicles in Europe and worldwide. In 2011, we reached an agreement to supply mobile communications technology to Chargemaster in the UK, the company entrusted with building a British charging network for electric vehicles. Chargemaster Plc. manufactures electrical solutions for vehicles. For the system to work every point needs to be able to communicate with the central database to authorise the recharge of a particular user. This is where Telefónica comes in. It will supply Chargemaster with the SIM cards for communication with the data centre. The Global M2M area expects to sign agreements with other suppliers in other European countries to encourage the uptake of electric vehicles worldwide.

Smart Bus in Brazil

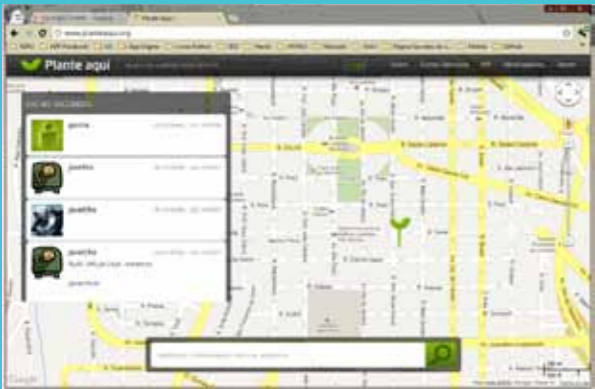
In 2011, Telefónica-Vivo and Ericsson developed a joint initiative to make the transport system in Brasileira de Curitiba, Brazil's seventh biggest city, more efficient using M2M technology for e-ticketing and managing the city's buses. The service meant traffic flows could be optimised, reducing fuel outlays by the local authorities. The project was acknowledged as a breakthrough in terms of mitigating climate change during the COP17 Climate Change Summit in Durban (South Africa) at the end of 2011. This type of solution to manage public transport is extremely popular among cities wishing to reduce their carbon footprint.

Green ICT Application Challenge

The "Smart Recycling" application won the ITU's first international competition, sponsored by Telefónica and Research in Motion (RIM), to identify innovative applications that boost energy efficiency and help counter climate change. The winner presented the application at the ITU Green Standards Week in Rome (Italy) in September 2011, and received a 10,000-dollar prize to develop this application.

The winning application at the second Appies Hackathon, held in Sao Paulo last December, was "Plante Aquí", a genuinely global green application. The competition was sponsored by ITU and Telefónica-Vivo.

The application can be used by any consumer on the planet to plant a tree or support its planting via the web or a mobile device, not necessarily a smart phone. The "Plante Aquí" application by Tadeu Gaudio is available at: <http://www.planteaqui.org>.



In 2011 the Telefónica Foundation presented the Smart Cities study: "an initial step towards the Internet of things" and developed by a team of Telefónica R+D experts, establishing that application of information and communication technologies (ICT) is a must for cities. This is because cities are genuine platforms where people live and work, where companies conduct their business and where many services are provided. The study can be downloaded at: http://www.fundacion.telefonica.com/es/que_hacemos/conocimiento/publicaciones/index/1

In 2010 we intend to bolster the Smart Cities Model, a goal close to Telefónica's heart. In this model, Green ICT services carry a considerable amount of weight, since local authorities urgently need to lower their costs and energy consumptions.

Telefónica's Green ICT services are focused on optimising the use of resources such as energy and managing environmental issues such as water, waste, climate change etc. Telefónica already offers a portfolio of Green ICT services, which continues to grow year by year. Green ICT services already commercially available include: green BMS, fleet management using M2M technology, virtual web hosting, and others. These services are already operational in group business around the globe.

Green Customer Experience

For the expanding residential mobile phone networks, in 2010 Telefónica designed the Green Customer Experience programme, which means customers can have a green experience from the moment they decide to buy a device through to the end of its useful life. It also includes green applications and functions to promote energy efficiency and the utilisation of non-contaminating materials in appliances.

In 2011 we strengthened the Telefónica view with respect to devices and applications as part of the GCEX model. Telefónica reinforced its strategy to develop Green applications via a joint initiative with the International Telecommunications Union (ITU), creating the first Green ICT Application Challenge, seeking to identify the most

Working alongside Biouniversal, Telefónica has deployed a pioneer initiative to recycle domestic cooking oil with containers using M2M services

ingenious creations to boost energy efficiency, protect the planet and stave off climate change. Working with the BlueVia expert community in Telefónica applications, we created a specific strategy to develop Green apps. We see Green apps as an excellent example of how technology and ICT use can be transferred worldwide.

In terms of green devices in 2011, we bolstered our strategy with specific environmental characteristics, particularly through the addition of the universal charger standard to new customer purchases. The Telefónica O2 UK team continued to implement the eco-rating model to make customers aware of environmental issues in relation to their purchases of mobiles. Telefónica O2 Germany implemented the eco-rating model in 2011. Telefónica is now spearheading a cooperation with other ICT companies to create a global standard for homogenous comparisons of the environmental sustainability of mobile devices placed on the market.

In 2011 Telefónica took its GCEX model to Peru in order to encourage efficient habits among its clients in Latin America. This programme will be extended to a number of Group companies in 2012.

Telefónica firmly believes that the ICT sector is part of the solution to climate change. We are committed to integrated services that offer added value, not just connectivity. Our business lines, particularly in M2M, cloud computing and apps, are working to design such services. We also believe we need to work with partners to achieve success in different markets.

Green Customer Experience in Peru

In 2011, Movistar Peru linked up with Nokia to launch their first offering. The joint venture was the first "sustainable" solution by any Latin American operator and manufacturer to combine mobile usage with energy saving, thereby helping environmentally-conscious customers to secure cutting-edge handsets while minimising their environmental impact.

Made from innovative eco-designed materials, Nokia's handsets are 100% recyclable, smaller and preloaded with green apps and content.

The mobiles also come with a highly efficient charger and an end-of-life recycling option. All of this in an attractive commercial package from Movistar that rewards the decision to buy this integrated service. Handsets available with the offer are the Nokia C7, N8 and C3.

Environmental Management at Telefónica

In 2011 the Company worked on the Eco-Efficiency Principle to minimise the environmental impact of its business, implementing best management practices and adopting environmental criteria in deployment of its network.

Telefónica, in line with its commitment to support the welfare of all, makes ICT available to society as a tool for economic and social development. We recognise the importance of efficient management of scarce resources such as energy or water to guarantee sustainable development worldwide. We therefore base our environmental risk management policy on operating eco-efficiency and, above all, compliance with environmental law.

At Telefónica we have a clear environmental policy, in which environmental awareness is not just a commitment but one of our business aims. This poses a challenge to internal management, as legal compliance, environmental management and control of resources must all ultimately result in better energy efficiency.

We worked hard in 2011 to minimise the environmental impact of our activities, promoting best management practice in all countries where we operate. We applied environmental criteria in rolling out our network and all employees were recruited to the effort to achieve these aims.

Telefónica Group Environmental Policy

The Telefónica Group's environmental policy lays down lines for environmental action, energy efficiency and climate change for all companies and all business units in the Company:

- 1. To guarantee compliance with environmental laws and all Telefónica's voluntary commitments on the environment in countries where the group operates, and, where environmental legislation is inadequate, to put in place stricter internal rules and guidelines than required by law based on the precautionary principle.
- 2. To put in place environmental systems to avoid and reduce the negative impacts of infrastructure activities on the environment, identifying and extending best practices throughout the Group.

- 3. To promote continuous improvement throughout the Company, by the systematic and regular assessment of environmental performance against a specified index, and the setting of environmental targets.
- 4. To make sustainable use of natural resources, encouraging procurement of products whose origin and manufacture are most environmentally friendly, minimising consumption of raw materials and the production of waste and encouraging recycling, recovery of materials and appropriate treatment of waste.

- 5. To communicate to the supply chain and service providers the environmental procedures and requirements for working with Telefónica and ensure compliance with these.

- 6. To put in place the necessary processes to ensure communication, awareness and training on environmental issues to Group employees.

- 7. To publish an annual report on the Company's environmental performance, including the most appropriate indicators and targets achieved.

- 8. To help combat climate change, by reducing internal greenhouse gas emissions and developing products and services that help other sectors reduce their emissions.

- 9. To promote the creation of telecommunications services that support the sustainable development of society.

- 10. To work with other organisations in seeking more sustainable models of development.



Electromagnetic fields

Telefónica is well aware of social concern with electromagnetic fields (EMF) from telecommunications equipment and is careful to communicate transparently on this matter. Whenever asked, the Company provides information to communities, public authorities, customers or any other interested party on the functioning of our base stations and mobile antennae. It also works to communicate the current state of knowledge on this issue.

In 2011, the Group made progress on consolidating global policy and the Electromagnetic Fields working group.

At Telefónica, we have always deployed our network in compliance with all international and local legal requirements. Even at the outset, when no law was in place, we signed up to voluntary best practice codes and in most countries where we operate we led a number of initiatives.

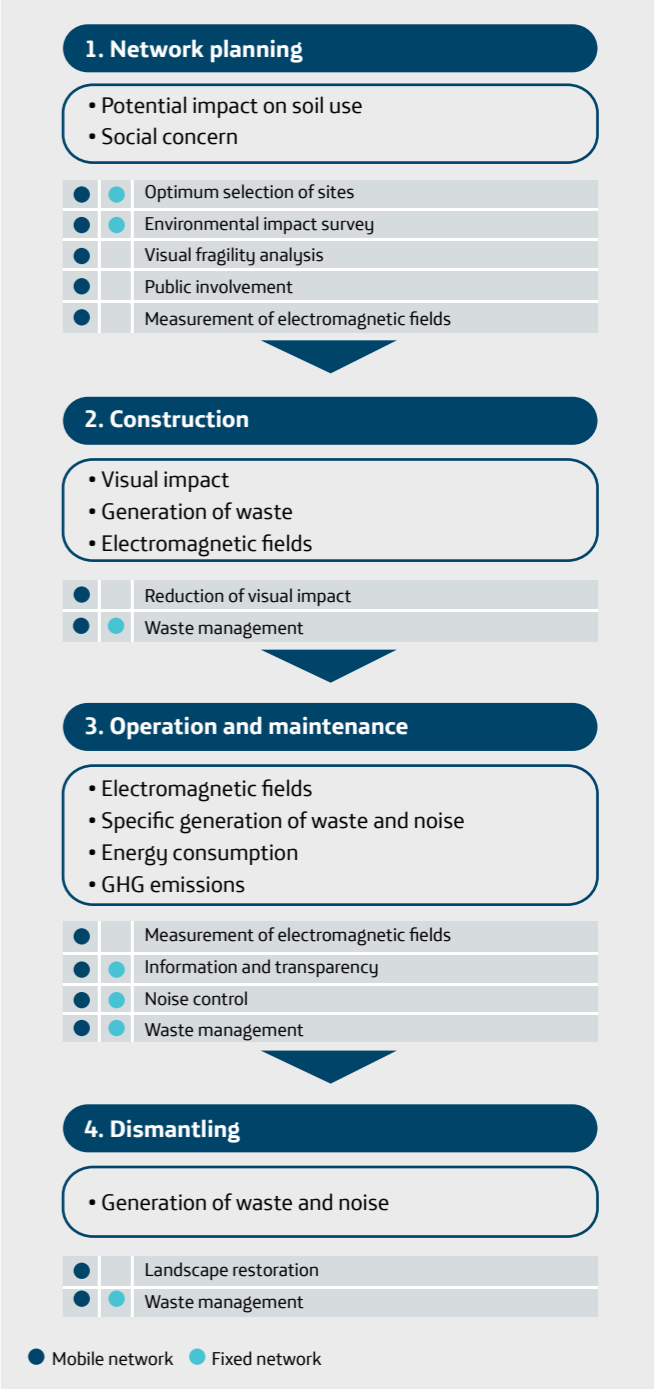
We not only adopted the limits on radio wave exposure established by ICNIRP and endorsed by the World Health Organisation, but also created international procedures pursuant to our ISO 14001 Environmental Management System, which enable us to track compliance with these standards.

To ensure compliance with these minimum limits, we share best practice and take coordinated action on electromagnetic fields. There is a global EMF project which coordinates all relevant aspects of this issue.

In 2011 we reached consensus on minimum commitments which were added to the EMF Global Policy. This sets minimum standards for all Telefónica's operations:

- ➔ To comply strictly with international regulations, standards and guidelines for all products and services.
- ➔ To promote legislation based on international guidelines (ICNIRP), especially where there is no local regulatory framework, which drives a standardisation of rules and eliminates barriers to deployment.
- ➔ To support and publish top-quality independent scientific research on mobile communications endorsed by the World Health Organisation.
- ➔ To be open and transparent in our communications with customers and the public at large.

Environmental issues in network deployment and Telefónica's response



Eco-efficiency at Telefónica

For Telefónica, eco-efficiency means *efficient management of environmental issues such as water, energy, waste and greenhouse gases, among others*, in our operations.

The main environmental issues associated with our businesses are in network deployment. During operations we must manage our waste output, energy consumption (electricity and fuel) and the visual impact of our facilities. Our business operations are not by nature particularly harmful to the environment, but we have a massive geographical deployment which makes it essential that environmental management is based on standardised procedures.

Telefónica applies a global Environmental Management System (EMS), as recommended by ISO 14001, which sets environmental management guidelines for all Group companies. Under this system, Telefónica seeks to improve its environmental performance by generalising best practices across all countries and adopting eco-efficient criteria, particularly in the deployment of its network.

In addition, in the process of providing services to the final customer, Telefónica's offices, stores and call centres inevitably generate waste, consume energy and water and generate GHG emissions. Also, on a global scale, countries are developing waste management and recycling plans for customer devices, particularly mobile handsets.

Telefónica has several KPIs for eco-efficiency in Group operations, which have environmental management systems either in place or in the process of implementation. Currently, 65% of Telefónica's operations have ISO 14001 environmental certification.

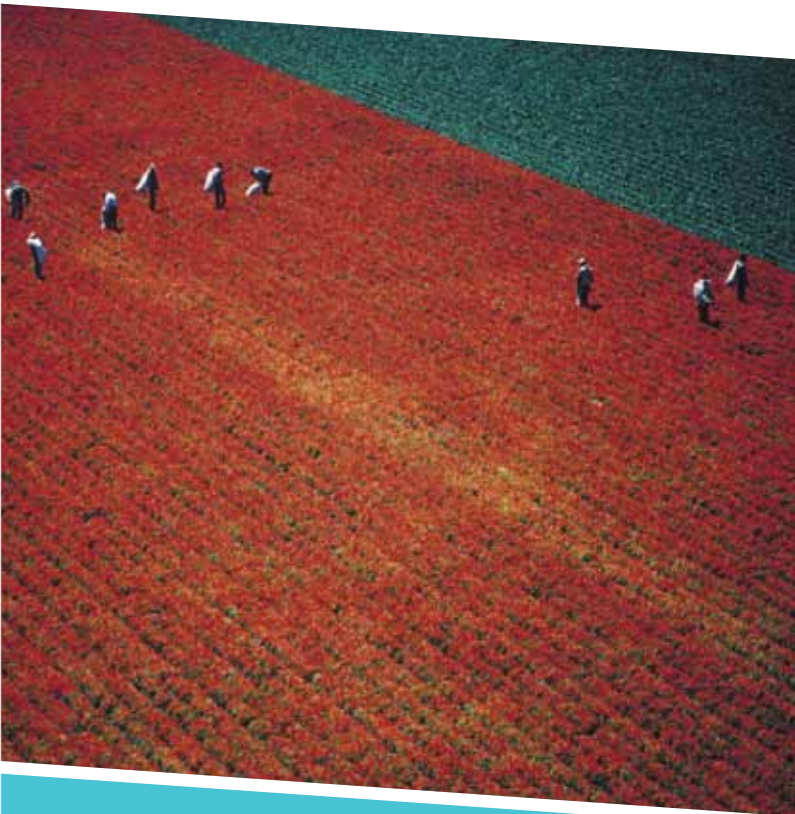
Environmental Management System			ISO-14001
Company	Fixed	Mobile	
Spain	☹️	😊	
Argentina	☹️	😊	
Brazil	☹️	☹️	
Chile	☹️	☹️	
Colombia	😊	😊	
Ecuador	N/A	😊	
El Salvador	N/A	☹️	
Guatemala	N/A	☹️	
Mexico	N/A	😊	
Nicaragua	N/A	☹️	
Panama	N/A	☹️	
Peru	☹️	😊	
Venezuela	N/A	☹️	
Uruguay	N/A	☹️	
Germany	😊	😊	
UK	N/A	😊	
Ireland	N/A	😊	
Czech Republic	N/A	😊	
Slovakia	N/A	😊	
N/A: N/A			

Global eco-efficiency indicators

Consumption of Resources		2009	2010	2011	% Chg.
Total consumption of plain paper (including bills)	Tonnes	16,941	14,720	13,171	-10.5
Total consumption of recycled paper	Tonnes	637	523	492	-5.9
Number of customers with e-billing	Thousands	12,597	10,338	29,618	186.5
Water consumption	Cubic metres	4,436,869	4,004,086	3,927,601	-1.9
Waste					
E-waste from devices (Operations)	Tonnes	1,571	2,048	2,180	6.5
E-waste from devices (Customers)	Tonnes	1,895	1,644	1,702	3.5
E-waste from devices sent for recycling	Tonnes	3,462	4,056	3,998	-1.4
Energy ⁽¹⁾					
Total fuel consumption ⁽²⁾	Thousands of litres	39,285	44,847	39,820	-11.2
Natural gas consumption: operations & offices	Nm3	6,637,096	6,623,162	5,413,698	-18.3
Total energy consumption ⁽³⁾	MWh	5,839,742	5,869,626	6,009,452	2.4
Renewable energy generated and purchased	MWh	497,095	677,904	743,585	9.7
GHG emissions ⁽¹⁾					
Direct emissions (Scope 1)	tCO2eq	114,580	126,247	112,377	-11.0
Indirect emissions (Scope 2)	tCO2eq	1,559,203	1,602,769	1,615,732	0.8

⁽¹⁾ Data on 2010 energy and emissions verified in 2011. Data on 2011 energy and emissions being verified.
⁽²⁾ Total consumption of petrol, diesel, ethanol and biodiesel from operations, offices and vehicle fleets.
⁽³⁾ Includes consumption from operations and offices.

Telefónica operates certain eco-efficiency indicators for all its operations. Currently, 65% of Telefónica's operations have ISO 14001 environmental certification



How Colombia manages its wireline waste

Telefónica Colombia ran a hugely successful first-time project to dismantle some of the Group's wireline towers, known as the "Plan de Chatarrización de Torres Bianaual II Inalámbrico", in conjunction with the Colombian IT Fund FONTIC. Some 951 towers were dismantled in 2011, producing approximately 204 tonnes of scrapped iron. 1.6 tonnes of telephone cable were retrieved, and sale of waste earned some €30,000.

- ➡ **1. Efficient use of water.** Water consumption at Telefónica is controlled at office level as it is not used in the networks. In 2011, there was a 1.9% reduction in global consumption, mainly thanks to water-saving projects and awareness campaigns among employees.
- ➡ **2. Efficient management of paper consumption.** In 2011, the company's offices used 1,125 tonnes of plain paper and 425 tonnes of recycled paper. At Telefónica, we are developing practices to reduce consumption and promote the use of recycled paper in offices. We also seek to sign up customers to paperless billing.
- ➡ **3. Efficient waste management.** Waste is one of the key environmental issues in our business. Different types of waste are generated, but all are managed separately on the basis of the hazard they pose, and are processed by approved waste managers. The greatest volume is e-waste from equipment used in the network and offices (2,556 tonnes), and hazardous waste, mainly batteries (2,371 tonnes). Of the total waste generated by Telefónica, we recycled more than 3,998 tonnes. In most of our operations, Telefónica also has collection points where customers can drop off their unwanted handsets for recycling.
- ➡ **4. Management of energy and CO2:** In 2011, we continued to manage our energy and GHG emmissions, based on the "Green from ICT" model defined by the Group's Energy Efficiency and Climate Change Office. GHG emissions grew by almost 0.4% year-on-year, mainly due to the growth of our network in Latin America.

Triple Bottom Line
Social dimension



Our professionals



Telefónica knows that the key to its leadership lies with its employees, which is why it designs its training, development and compensation programmes with a view to making the Company the best place to work.

Telefónica is currently at an important juncture of its history. We have become a leading player in the communications sector, thanks to the contribution of each and every one of the persons working here at Telefónica. Today, more than ever, we are aware that our success as a company depends on the commitment displayed by our professionals to tackling the challenges looming in the years ahead. To this end, we design our HR policies, our processes and initiatives at each of our companies to ensure that our employees receive the resources, career development opportunities, recognition and support they need to feel they are in the best place to work.

In 2010, the HR-sponsored corporate transformation initiatives focused on the “Live the Experience” programme and the eight related forms of conduct. In the last quarter of 2011, however, in conjunction with the launch of Bravo+, the new strategic plan enshrining Telefónica’s priorities to 2020, the thrust was shifted to focus the five new forms of conduct that will align the entire organisation with the Bravo+ targets and achieve the desired cultural and strategic transformation. These five forms of conduct sum up how each professional should behave and also how the organisation needs to respond so that things happen quicker and Telefónica delivers its targets.

In addition to the five Bravo+ forms of conduct, the HR teams continue to work on other projects and initiatives related to core issues such as career development, teamwork, recognition and clear communication lines.

Our professionals in numbers

The Telefónica Group, excluding the Atento Group, has more than 134,000 employees, 1,540 of which are executives. The Telefónica Group workforce, distributed across 25 countries, increased by 1% in 2011. Factoring in the Atento Group, the overall headcount is 291,027, growth of 2.1% with respect to year-end 2010. This growth is all the more noteworthy when viewed against the backdrop of the challenging economic environment and far-reaching overhaul in the telecommunications market.

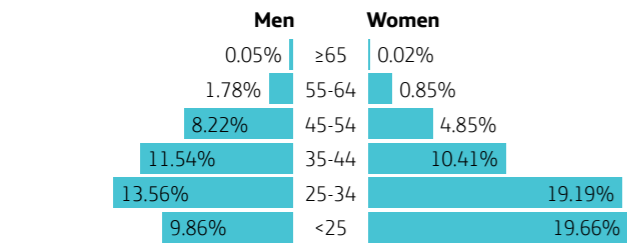
Due to the nature of Atento’s business (intermittent campaigns over the course of the year), its employee turnover metrics are not comparable to those of Telefónica’s core businesses (telecommunications services), and substantially distort the overall turnover rate (52.68%). Telefónica’s turnover rate excluding the Atento business was 22.39% in 2011.

An examination of employee breakdown by region reveals that Latin America continues to account for the bulk of the Telefónica Group’s headcount—71%. This region is followed by Spain (19%) and the rest of Europe (9%). The remaining 1% is distributed across a number of countries not included within the defined core regions.

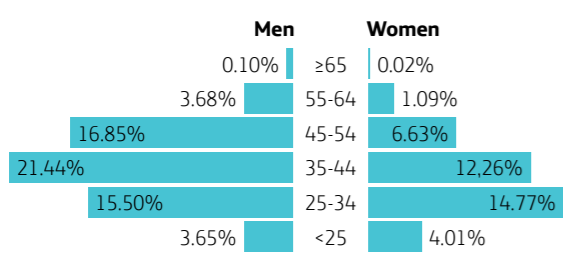
Ninety-six per cent of Telefónica’s workforce, excluding Atento, have permanent employment contracts. Including Atento, this figure falls to 81%.

Leaving aside Atento, at year-end 2011, 37% of Telefónica’s workforce was female; this figure rises to 54% factoring in Atento. In 2011, Telefónica increased the percentage of women in management positions to 19.1%.

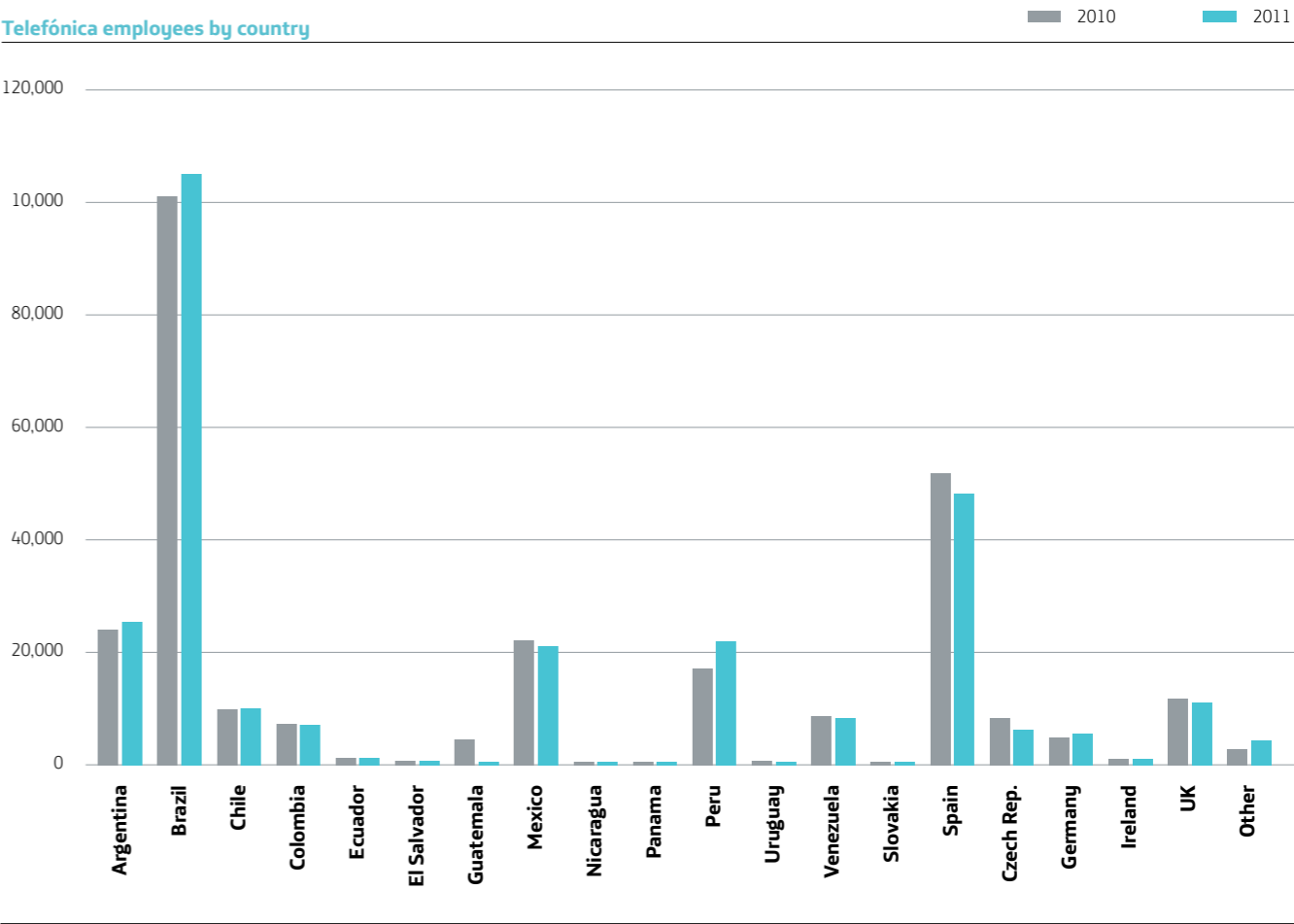
Telefónica



Telefónica without Atento



Telefónica employees by country



Training and talent management

Telefónica approaches its training and career development programmes as part of a cycle that starts with target-setting, continues with performance evaluation (what has been achieved and how was it achieved) and concludes with individual career development plans based on the opportunities Telefónica has to offer. Throughout this entire process, we seek to foster inspiring leadership that encourages a culture of feedback as a crucial element of personal and professional growth.

Career development opportunities at Telefónica are articulated around various tools: in-person (courses, seminars, workshops, conferences, etc.) and e-learning training initiatives; critical experiences (international assignments, project management, etc.); on-the-job career development opportunities; project sharing; mentoring and coaching programmes; performance reviews and self-assessments.

Training in figures

In 2011, Telefónica invested €66.4 million in training its professionals (including Atento), over 10% more than in 2010. In 2011, employees received over 17 million hours of training, which translates into an average of 60 hours per employee (including Atento). This marks a 34% increase over the number of hours of training provided in 2010,



	2010		2011	
	Year-end workforce	Turnover ¹	Year-end workforce	Turnover ¹
Telefónica without Atento	133,210	16.22	134,293	22.39
Atento	151,896	91.72	156,734	79.14
Total workforce	285,106	55.80	291,027	52.68

¹ Turnover is calculated using the average workforce during the period.



Universitas Telefónica ran 43 editions of 14 different programmes in 2011:

- 1. Leading & Managing Change
- 2. Leading Self
- 3. Leading High Performing Teams
- 4. Telefónica 2020 **New***
- 5. China **New***
- 6. Customer Focus
- 7. Effective Negotiations
- 8. Fundamentals of Business Management
- 9. Engaging Realities **New***
- 10. Innovation & Leadership **New***
- 11. ComunicAction
- 12. Postgraduate in Business Telecom
- 13. Powerful Leadership Conversations
- 14. English Week

significantly outstripping the growth in investment, largely due to the ongoing boost to e-learning initiatives in 2011, which enabled Telefónica to manage the resources it devotes to training efforts in an increasingly effective manner.

Universitas Telefónica

Universitas Telefónica plays a key role in the employee training effort. In 2011, the Universitas team defined its new vision: “To create a place destined to become a meeting point for Telefónica, an incubator of ideas, a place for reflection, a laboratory for experimenting, trial and error, learning and sharing, so that Telefónica can become a true learning organisation”.

Universitas Telefónica modified its strategic approach with a view to achieving academic and learning environment excellence, becoming more important to Telefónica (by performing specific research about Telefónica, through programmes sponsored and jointly run by Telefónica and via the commitment of the Academic Committee), maximising networking opportunities, championing diversity and cross-fertilising culture.

Changes were also made to **Campus Universitas** Telefónica in 2011 with a view to making it a place that invites its guests to relax, network, learn, share best practices and grow as people and professionals. The construction of a tennis court and other changes to the decor have helped make the indoors and outdoors more welcoming.

As part of the Synergies and Cooperation Programme underway with China Unicom, and with a view to stimulating mutual trust and facilitating closer ties among the executives from the two firms, Universitas organised part two of the **China Unicom Programme** which took place in Peking. The programme was focused on improving the cultural handling of the participants' strategic leadership.

As for course participation, Campus Universitas hosted **2,674 participants** in 2011, broken down as follows:

		Total 2011 (est)
Universitas Programmes EXECUTIVE		695
Universitas Programmes PRE-EXECUTIVE		684
Regional Programmes (Telefónica Europe)		41
Internal events		737
Foreign language courses		90
Telecom Postgraduate		83
Train the Trainer Programmes		27
External events		317
Total		2,674

The **overall average score given by participants to their Universitas Telefónica experience was 9.0 out of 10** (one-tenth higher than in 2010). The highest-rated programme, with a score of 9.6, was the Leading Self Programme, followed by Leading & Managing Change, at 9.3.

Corporate e-Learning (a+)

Universitas Telefónica encompasses management of Telefónica's Corporate e-Learning initiative. The main achievements on the e-learning front in 2011 were:

- The rollout of a new **version of the global e-learning platform**. The biggest changes related to the addition of a battery of web 2.0 tools in order to foster a '**social learning**' culture in-house.
- The implementation of the:
 - **English language school** with close to 7,000 enrolled students; the facility is getting terrific feedback.
 - **School of finance** (over 2,000 students) including master classes from top executives from the corporate finance department.
 - **ICT School**, with over 6,400 students.
- Pilot Pilot Chinese language course (mix of online and in-person learning).
- Design and rollout of **global content** of strategic value to the company ("Get to Know Telefónica", "Social network usage guidelines for Telefónica employees", "Business Intelligence Fundamentals").
- Creation of **local e-learning management communities** in all of Telefónica's local operating markets.



Company ranking

Latin America		Atento	
Company ranking	Companies	Company ranking	Companies
1	Nicaragua	1 (companies with over 1,000 employees)	Atento España
1	Uruguay	2 (companies with over 5,000 employees)	Mexico
1	Venezuela	2	El Salvador
2	Ecuador	3	Uruguay
3	TM Argentina	3	Puerto Rico
4	El Salvador	4	Guatemala
4	Chile	6	Argentina
5	Colombia	9	Peru
5	Panama	39	Mexico
11	Guatemala		
12	TASA		
13	Mexico		
15	Peru		
22	Vivo		
78	Telesp		
5	Mexico		
8	Vivo		
40	Telesp		
		Europe	
		Company ranking	Companies
		6 (companies with over 250 employees)	Ireland
		Among the best places to work in Germany	Germany
		Among the 50 best places to work in the UK	UK

Ecuador

Seventy-two per cent of the total training hours provided was taken by men and 28% by women. This gender gap reflects the relatively high weighting of training hours devoted to operations and technology (38% of the total), an area of the company where most of the employees are male. The gender split is closer to 50% in the courses devoted to administration, sales and marketing and finance.

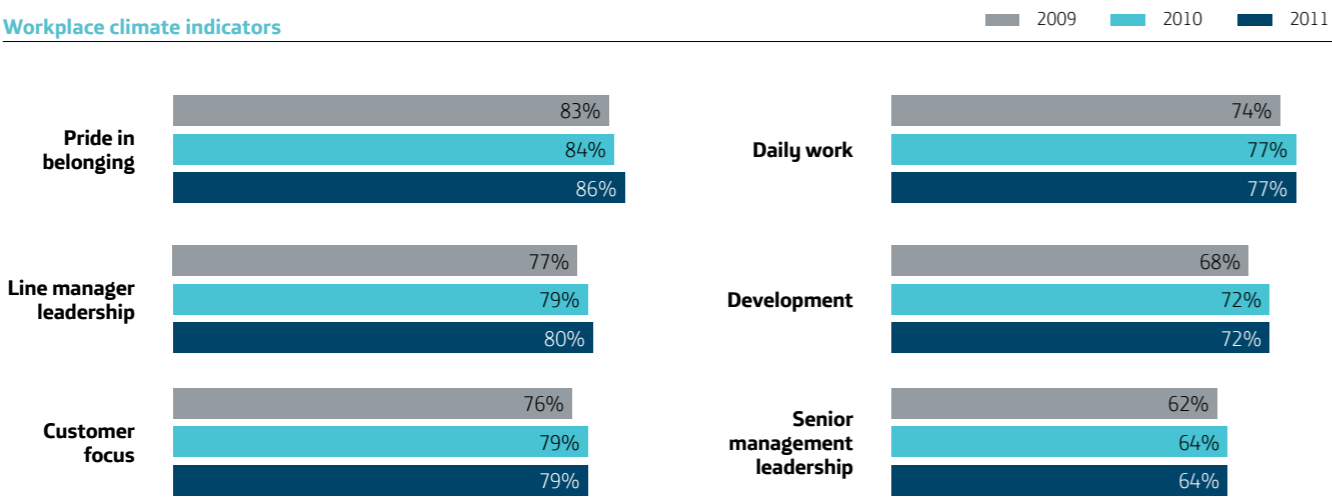
Note with respect to the gender breakdown of participation in Universitas Telefónica courses (68% male; 32% female).

Working environment and commitment

In 2011, over 108,000 employees in 24 countries filled out the global workplace climate and commitment survey towards the end of the year.

The survey yielded a score of 76% in 2011, two points above the result of the 2010 survey and two points better than the target set for 2011, which was to maintain the 74% achieved in 2010.

Workplace climate indicators



Performance by region	2009	2010	2011
Spain	60%	63%	65%
LATAM	83%	84%	83%
Europe	76%	75%	76%
TSA and Subsidiaries:	67%	66%	71%
Overall Telefónica	73%	74%	76%

Note:
1. Employees taking part in the work climate survey at December 2011. The survey does not include call centre personnel.

Participation increased by 0.5 points to 75% of those asked to fill out the survey.

Some of the aspects where Telefónica made the greatest progress include the sense of pride in belonging and line manager leadership.

For the first time in 2011, we added questions to the employee survey intended to help us delve further into employee commitment and the conditions they need to work more effectively. This approach is termed 'Effective workplace climate' (commitment + working conditions) and it helps us to manage employee commitment better.

After conducting these surveys – the first step in the chain – the results were distributed to the organisation's leaders around the world. The feedback fed the design of specific plans for improving

employee sentiment with a view to achieving our goal of positioning the company among the best places to work anywhere in the world.

Great Place to Work Awards

In 2011, the Great Place to Work Institute named Telefónica one of the 25 best companies to work in the world.

This was the first time this prestigious Institute, known globally for its local and regional rankings, compiled a global ranking.

Specifically, Telefónica ranked #17 among 350 shortlisted companies from 45 countries. The candidates are all multinationals with at least 5,000 employees, at least 40% of whom must work outside of the company's country of origin. To prepare this global ranking, Great Places to Work also assessed the local results of employee satisfaction surveys and of audits analysing the companies' HR policies and practices.

Telefónica also ranked among the Great Places to Work in 13 countries.

In recent years Telefónica has been voted the best company to work for in Germany, Ecuador, Uruguay and Venezuela. In 2010, it ranked second in Latin America as a whole and made it into the top 25 in Europe.

Atento, a Telefónica subsidiary, has also ranked among the top 25 best places to work, coming in 24th. At year-end 2011, this BPO and CRM services provider boasted a global headcount of some 152,000.

Telefónica is the only telecommunications operator appearing on the list, while Telefónica and Atento are the only Spanish companies in the global ranking.



Work-life balance policies and practices at Telefónica

One of the company's priorities is to facilitate work-life balance for our employees. To this end, Telefónica has implemented various programmes and initiatives.

What follows is a summary of some of the most important initiatives:

“Tiempo para Vos” (Time Out for You)

This initiative was launched in Argentina in order to generate a flexible work culture that gives employees the freedom to strengthen their bonds outside the workplace.

The benefits of this initiative include shorter work days, fewer working hours during their children's first year, two personal days a year, teleworking arrangements, Friday afternoons off, study leave, etc.

Teleworking at Telefónica Spain

As a result of resounding success of its teleworking initiative, launched in 2006, Telefónica has since renewed this commitment, which is enshrined in the 2011-2013 collective bargaining agreement. The idea behind this initiative is to provide a tool to support the transformation effort. It is based on a climate of trust and is voluntary. Employees opting for this regime must present certain traits (self-discipline, adaptability,

independence, flexibility, ability to work unsupervised, etc.). The job must also lend itself to a teleworking arrangement. Once within the programme, teleworkers can work from home between two and four days a week (or equivalent working hours) and are guaranteed the same union rights and employment terms and conditions, including pay-related.

As at June 2011, Telefónica España has 2,277 teleworkers, 1,609 of which belonging to the fixed telephony business and 668 to the mobile business. The teleworker gender mix is roughly equal. The following chart shows the trend in teleworkers since the initiative was first introduced in 2006.

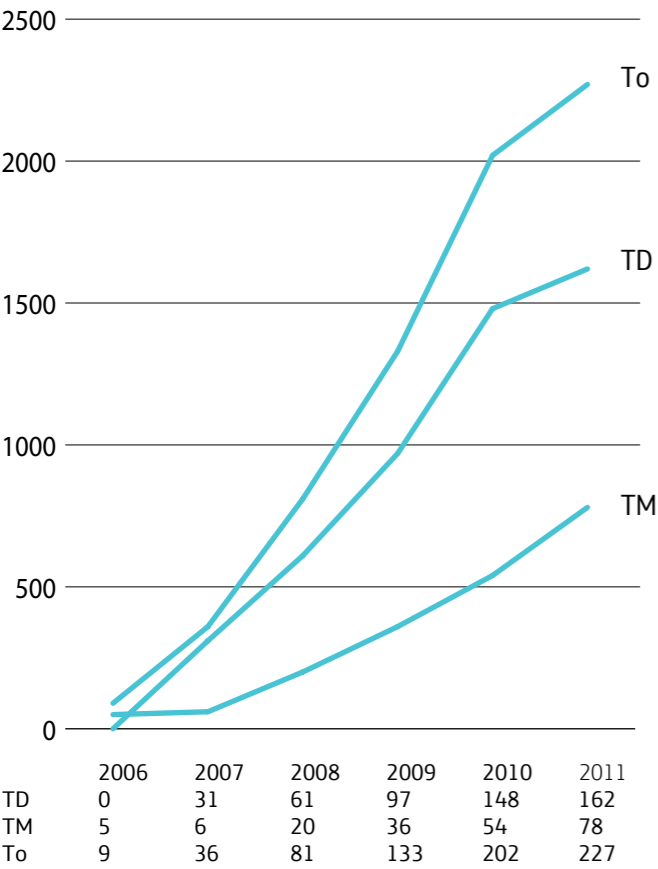
Some telling feedback from different areas of the firm participating in this initiative:

- “10% increase in productivity” (Accounting/Treasury)
- “Improvement in personal customer care” (Large Companies)
- “More productive working from home than from the office” (Commercial Services)

“Joined Up People” Programme at Telefónica UK

In the UK, Telefónica launched an initiative dubbed “Joined Up People” to promote flexible working arrangements which has wrought a change in corporate culture and in the way people work together.

Trend in number of teleworkers



Staff from the Sales, Technology, Finance and HR divisions participate in this programme. Productivity has risen while absenteeism has trended lower. Moreover, the results of the employee survey have improved in respect of work-life balance issues. According to Telefónica's UK HR professionals, the programme also constitutes a powerful recruitment tool when it comes to attracting and retaining talent.

Elsewhere, the initiative entails significant cost savings. For example, just by reducing the number of desks needed (and all the related work station equipment) by 500, the company has saved over £3.8 million. Management also expects spending on paper to fall by 30% at the Slough head office, with obvious environmental ramifications. Another source of savings relates to business travel, where the firm expects to save around £600,000 a year.

In short, this project promotes work-life balance by providing flexible working conditions which contribute to creating a culture in which "what counts is what gets done and not where it gets done".

UNO Programme at Telefónica Chile

UNO, a Quality of Life programme rolled out in Telefónica Chile and viewed as a benchmark practice for all of LATAM, was created with the goal of getting employees emotionally committed by offering them à la carte benefits. The programme was designed around employee feedback compiled from the workplace climate surveys and discussion groups where they were asked "What does quality of life mean to you?" What should a quality of life plan take into consideration?"

UNO was built on the basis of the answers to these questions. Under this scheme, every employee chooses among a pool of non-monetary benefits (emotional salary), choosing those that best suit and motivate them, thereby erecting a flexible and tailored work-life balance programme.

The main features of the programme are:

- ↳ 21 benefits created for approximately 6,000 employees but conceived of for each and every one of them.
- ↳ Each employee is given 1,000 credits with which to create his or her own flexible quality of life plan.
- ↳ Plan choices can be modified three times a year (April, July and November).
- ↳ Management can approve additional changes with their staff as warranted.
- ↳ The term of the quality of living plan is one year (April to March). The credits are not cumulative.
- ↳ Most of the benefits centre around the following issues:
 - ↳ Family.
 - ↳ Healthcare.
 - ↳ Bonuses, scholarships and loans.
 - ↳ Special offers and entertainment.
 - ↳ Products and services.



Attracting and retaining talent

On the talent front, one of the major milestones of 2011 was the design of a new **Global Performance and Talent Management Model** which will be rolled out in all Telefónica companies in the course of 2012. The key aspects of this new model are summarised below:



Postgraduate programmes

Telefónica places great importance on attracting and managing our professionals' talent from the beginning of their careers. To this end, there are a number of local programmes in place targeted at new university graduates and designed to accelerate their career development within the organisation.

At present around 300 graduates are participating in local programmes underway in Argentina, Brazil, Ecuador, Mexico, Peru and Telefónica Europe. Participants are put through an exhaustive selection process. Those selected to join the programmes receive comprehensive career development programmes encompassing ad hoc training courses at business schools, corporate induction programmes, allocation of a mentor and/or coach and opportunities to take up international placements across Telefónica's markets.

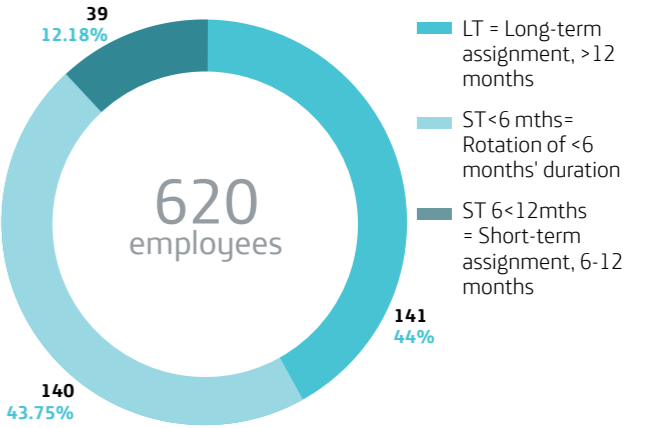
The benefits of these post-graduate programmes include enhanced job performance by most participants and higher talent pool retention rates.

Talent mobility

Telefónica prioritises talent mobility based on its view that it represents a key factor in personal and organisational development by fostering the exchange of know-how and best practices among

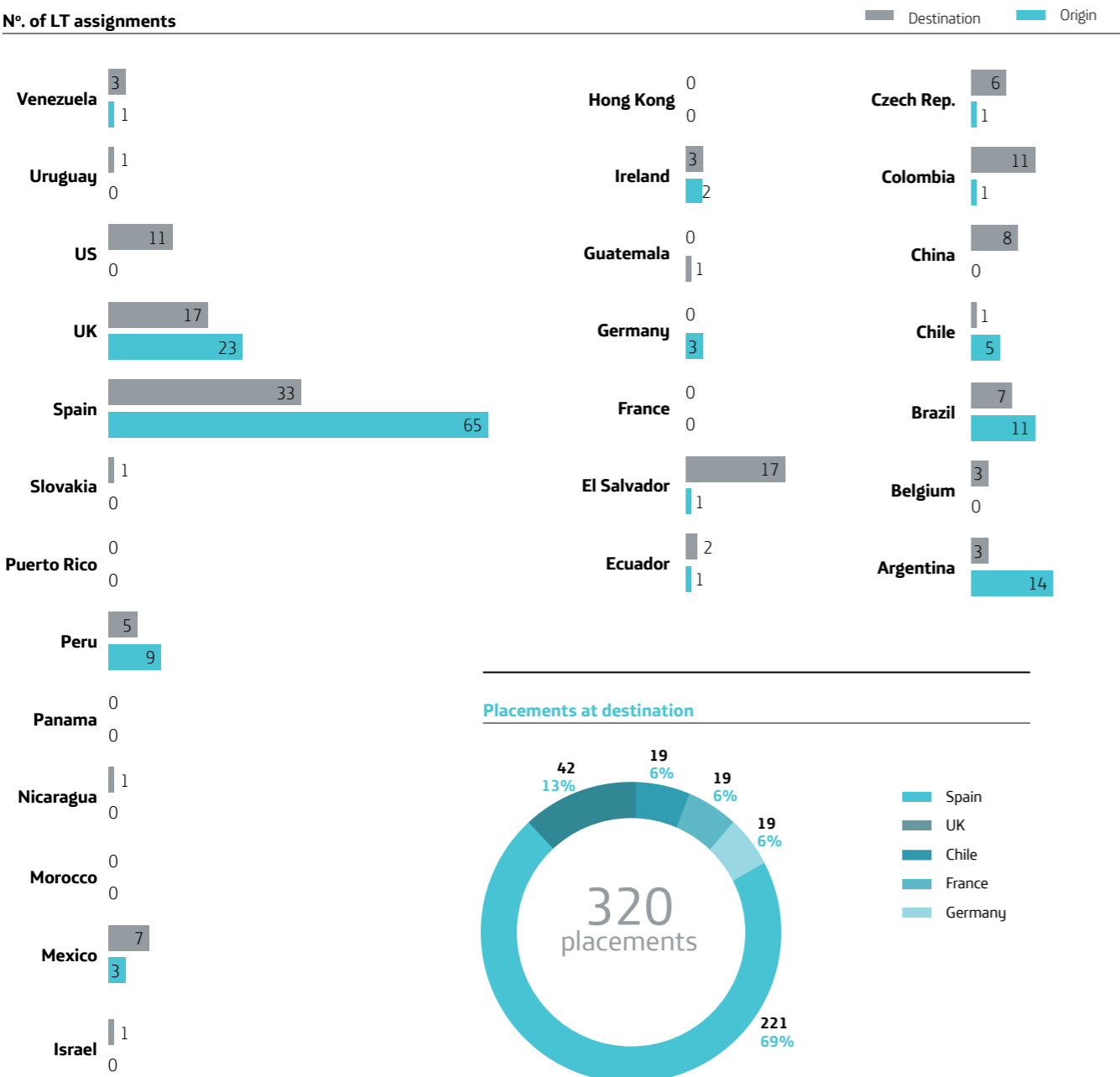
the various companies. This was the reason for the launch in 2008 of the **Global International Placement Management Model**. In 2011, a total of 320 international job placements were ongoing under this model. Of these, 48.75% were new placements (156), marking a slight slowdown on the growth in 2010 (52%) and 2009 (54%).

Number of employees by type of assignment, 2011



To maintain a fair compensation regime and recognise its professionals' performance, Telefónica regularly conducts market salary surveys to ensure it remains competitive

Nº. of LT assignments



Fair pay and performance recognition

The overriding goal of Telefónica's compensation policy is to design compensation packages capable of attracting, retaining and motivating the finest professionals so that the company can deliver its strategic targets against the backdrop of an increasingly competitive and global business, while managing to keep costs in check.

To this end, Telefónica regularly conducts market salary surveys to ensure it remains competitive, working with consultancies that take a global approach whose work methodology and tools are designed to cater to regional needs and ensure consistent application of methodology and results analysis.

The fixed compensation paid by Telefónica is above local minimum wage levels in all instances, albeit by varying degrees. For example, the ratios of basic pay to local minimum wages at the biggest employer companies are: 2.73x at Telefónica Spain, 1.22x at Telefónica Brazil, 1.56x at Telefónica Mexico and 1.35x at Telefónica Argentina.

As for the ratio of basic salary of women to men, in the home market (Spain, the biggest market), this ratio is 95.2% for all female staff and 94.6% in the female management category.

In most cases, in addition to fixed basic pay, our professionals' compensation packages include an annual bonus tied in part to attainment of specific business targets that are readily quantifiable and aligned with the corporate value creation imperative and in part to individual job performance. These targets are fine-tuned every year to ensure optimal fit with the strategic business priorities.

Telefónica share payment schemes:

Global Employee Share Plan

This Plan continued its natural course in 2011. Employee enrolment in this plan began in May 2010 and is totally voluntary. Currently more than 38,000 employees around the world are company shareholders, holding over 2,400,000 shares between them. The minimum stipulated period for holding



these shares expires in September 2012, which is when active plan participants will be given their additional shares.

Long-term share-based incentive scheme at Telefónica, S.A.: Performance and Investment Plan.

At Telefónica, S.A.'s General Meeting on 18 May 2011, the company's shareholders approved a long-term share-based incentive scheme called the Performance and Investment Plan which is targeted at high-potential and high-performing Group executives and is designed to stimulate and compensate them for individual and organisational performance and increase their investment in the company's earnings performance in their capacity as dual stakeholders: employees and shareholders.

The scheme will run for five years in total and is divided into three independent three-year cycles (i.e., delivery of the shares corresponding to each cycle three years from inception). The first cycle began on 1 July 2011 (so that the corresponding shares will be delivered starting on 1 July 2014) and the third cycle will begin on 1 July 2013 (so that the corresponding shares will be delivered starting on 1 July 2016). The number of shares ultimately delivered under the scheme will range from 30% of theoretical shares (in the event that Telefónica, S.A.'s total shareholder return (TSR) is at least in line with median TSR for the defined peer group) and 100% in the event that the TSR is at least 75% of that of the peer group; the number of shares delivered if the TSR falls between the median and 75% will be calculated using linear interpolation.

The first allocation of shares under this scheme – a total of 5,344,463 – was made on 1 July 2011.

Telefónica, S.A. share plan: "Performance Share Plan" (PSP)

This is a long-term incentive scheme targeted at Telefónica executives intended to align their efforts with the company's desired performance and to create a shareholder spirit among its professionals. This plan comprises five annual share allocation periods, each carrying a vesting period of three years. Upon maturity of the plan in July 2011, a total of 2,898,948 shares (corresponding to a total of 4,126,082 gross shares less a withholding at source of 1,227,134 shares) were delivered to the beneficiaries (Telefónica Group executives) of the second cycle.



"Restricted Share Plan" (RSP)

At Telefónica, S.A.'s General Meeting on 18 May 2011, the company's shareholders approved a new long-term share-based incentive scheme called the Restricted Share Plan (RSP). This is a flexible share-based payment scheme for use in external recruitment. It is useful in retaining key management personnel in the wake of new acquisitions by offering them a stake in the company's equity in the form of rights convertible into shares. This scheme has a total term of five years. Share deliveries are ad hoc and independent of each other and may take place at any time between 2011 and 2015.

Performance recognition

Under the umbrella of its global business strategy, in 2010 Telefónica launched the Bravo! Awards covering all employees. This was the first time that the firm undertook a global initiative to reward its professionals for their commitment, efforts and good work. In 2011, Telefónica employees put forward a total of 1,700 candidates. These nominations were sourced the various prizes previously awarded to Telefónica's best-performing individuals and teams at the local and regional level. Nominations in Spain totalled 700, compared to 550 in Latin America and 430 in Europe. Bravo! Awards were ultimately given to close to 300 people. They represent the firm's highest mark of distinction for outstanding performances under the Telefónica Group's various local and regional recognition initiatives.

Dialogue and transparency with employees

The Internal Communication Model established by the Internal Communications Corporate Committee and promoted by the Chairman's Office and HR Department continues to set the global communication strategy and editorial line of all corporate communication channels.

Telefónica has continued to make new internal communication tools available to its employees. These notably include the global SOMOS corporate magazine, electronic and audiovisual media such as the Telefónica Daily, the corporate intranet, the Distrito C portal, the Telefónica España intranet, the executive portal, the global knowledge platform eKISS 2.0 and the bravo!+ programme.

In 2011 a number of microsites were developed to cover topics of interest to employees, such as the Best Sales and Marketing Practices Day and the Unified Global E-Mail microsites. The first urged employees to go online to watch the event broadcast live, while also engaging staff by informing them of the company's new work dynamic, the most novel ideas and the best practices selected across all the business units. The purpose of the Unified Global E-Mail project was to ensure familiarity with Telefónica's new standardised global e-mail system and its benefits.



Freedom of association and social dialogue

Telefónica's position on freedom of association is guided by its Business Principles and the Social Protocol on International Agreements in force with Union Network International (UNI).

Telefónica respects its professionals' privacy rights in respect of their union membership choices, to which end it does not compile membership data. A total of 77,736 employees voted in Telefónica's last union elections (over 27% of the total workforce), underlining

In its labour relations in Latin America, Telefónica emphasises employee proximity, communication and respect for applicable labour law. This has helped to make it the second highest-ranked place to work on the continent

the dynamism of union activity at the Company. These elections are held freely and related rights are fully protected.

The labour relation policies in place in all our Latin American businesses emphasise employee proximity, dialogue, communication and respect for applicable labour law. To this end, Telefónica systematically promotes initiatives that get employees involved, search for ways to do things better and more innovatively, with a focus on issues related to change management and technology development that affect its employees and their surroundings. All this has underpinned Telefónica's selection as second best employer on the continent, measures on which it stands out in comparison to its peers.

The union relations at our Latin American companies are based on respect for legitimate worker representatives and compliance with international labour regulations and guidelines. We guarantee an open communication channel by building relationships based on trust. In some markets, our efforts to enhance dialogue between the organisation and its employees have been externally recognised. Dealings with the unions were absolutely normal in 2011. There were hardly any conflicts despite the fact that the company undertook restructuring work to merge the fixed and mobile telephony operations.

Last year the company also made progress on fine-tuning and coding the rules and policies governing relations with contractors: this issue is complex and raises certain employee concerns.

Lastly, we are working on negotiated formulae designed to reduce labour litigation at two or three businesses which have resorted to this avenue frequently on account of historic labour relations.

Collective bargaining

In 2011, 71% of Telefónica's workforce was covered by collective bargaining agreements.

Specifically at Telefónica Spain, thanks to the pattern of dialogue between the organisation and its employees established in recent years, this company successfully culminated the negotiation of its collective bargaining agreement covering 2011-2013 and a restructuring plan (ERE for its acronym in Spanish) which contemplates up to 6,500 redundancies. This marked the culmination of two significant collective bargaining arrangements that will enable the company to forge ahead with its strategic transformation initiative designed to defend its competitive position

in the current market, responding optimally to customers' evolving needs.

The new collective agreement factors in important issues solicited by the workers' representatives with a view to ensuring employment stability throughout its term of effectiveness and modifying the job classification scheme, moving towards a classification defined around professional categories. It includes some very novel developments, such as the protocol defining what to do in the event of alleged instances of sexual and gender harassment in the workplace. On the salary front, the agreement guarantees equilibrium by way of a pioneering scheme in Spain which ties salary increases to the company's earnings performance, decoupling wage increases from the traditional inflation indices. The result is a very reasonable compromise that balances the interests of the organisation and its employees.

Also against this backdrop of negotiated agreement, the firm reached an important restructuring agreement with the workers' representatives covering 2011 to 2013 under which employees can voluntarily sign up for the redundancy packages contemplated therein. Importantly, the agreement's voluntary, universal and non-discriminatory nature is guaranteed.

Union elections also took place at Telefónica Spain to choose worker representatives. Workforce participation in the March 2011 elections to appoint the members of this company's provincial worker committees was 81.64%. No incidents were recorded and all rights were duly guaranteed.

With regard to other Group companies, it is worth noting the collective bargaining agreement signed by Telefónica Soluciones in force in 2011.

Joint management-worker health and safety committees

The occupational health and safety model in place in Telefónica's various markets ensures high worker involvement in health and safety matters through their representation on the corresponding joint management-worker health and safety committees, which number 222 across all of Telefónica's markets.

It is worth noting that the work performed by the respective health and safety committees in countries such as Mexico, Chile and Venezuela in 2011 reinforced the occupational health and safety programs in place and their scope of engagement.

The health and safety committees in place in all of Telefónica's markets constitute the channel enabling the deployment of



Diversity and Inclusion

We are all different. At Telefónica, we view differentiation as a competitive advantage. In the marriage of differing backgrounds, experiences and perspectives lies the key to success. Because through the uniqueness of each and every individual, we all grow. We are responsible for creating a culture in which we all feel respected and included. That is true Progress. Progress by means of inclusion.

Diversity management at Telefónica

At Telefónica we view our diverse workforce as a genuine value driver. The differing origins, experiences and viewpoints of our human capital constitute a competitive advantage and one of the cornerstones of our success.

Our Business Principles, which govern employee conduct, specifically state: 'we promote equal opportunities and treat all people fairly and impartially, without discriminating on account of race, skin colour, citizenship, ethnic origin, creed, gender, sexual orientation, age, disability or family responsibilities'.

Indicators

A cierre de 2011, el número de mujeres en Telefónica era de 156.897, el 54% de la plantilla total (3,5 puntos porcentuales más que en 2010). and 19.1% of executives were women (compared to 16.8% at year-end 2010).

The number of employees living with a certified disability totalled 1,568 in 2011.

Lines of initiative pursued in 2010

The work initiated in 2010 under the umbrella of the global diversity programme (unveiled in 4Q10 by the Business Principles Office) continued in 2011. The project, designed to integrate diversity protocols and sensitivity into all areas of the company, entailed a pilot test at Telefónica Europe last year, the results of which were so satisfactory that the initiative will be rolled out to the other regions in 2012.

Diversity at Telefónica Europe

In 2011, the organisation conducted in-house and external studies to determine what the company needs to do to optimally manage diversity at Telefónica. Keenly aware of the breadth of the diversity term, both studies focused on gender diversity, enabling a more accurate diagnosis of the situation in respect of an issue of great significance.

Internal research:

The in-house analysis consisted of holding 'discussion groups' with various groups of employees (non-management women, female managers, male managers, women coming back to work after maternity leave) as well as in-depth interviews with managers in all the countries making up the European business unit in 2011.

The result is a commitment to create taskforces to tackle three lines of initiative:

- **1. Leadership**
A commitment to enhance our leaders' understanding of the benefits of managing with diversity in mind so as not to miss out on the opportunities afforded by correct diversity management.
- **2. Customers**
The performance of in-depth studies investigating customer groups that present a high sales potential but are not being sufficiently addressed as part of our customer base.
- **3. Talent**
Improvement of the hiring and talent management processes with a view to attracting and retaining the best female candidates.

Telefónica Europe plans to implement several programmes to help it fulfil the following commitments:

- 1) Talent pipeline.
- 2) Female leadership programme.
- 3) Candidate profiling programme.
- 4) Graduate profiling programme.
- 5) Hiring committees.

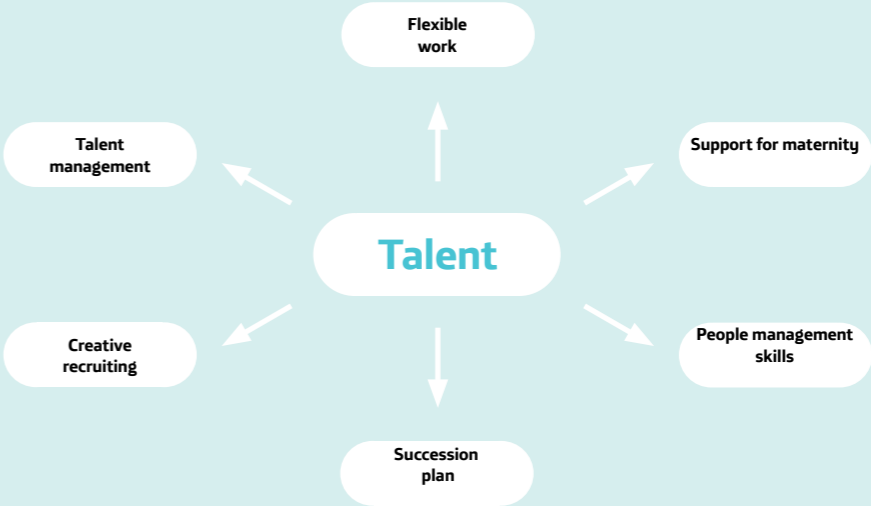
Towards the end of 2011, each of the countries classified within the European region was asked to designate one of its board members as Diversity Champion. A European Champion was also appointed: in 2011, the CEO of Telefónica Germany will act as European Champion and will take responsibility for championing initiatives designed to achieve the above-listed commitments.

Some of the initiatives already underway by year-end 2011 included:

Telefónica Spain

- Introduction of a protocol defining what to do in the event of alleged instances of sexual and gender harassment in the workplace into the collective bargaining agreement for 2011-2013.
- Plans for the execution of the discussion groups needed to conduct the in-house research already performed in Europe.

Areas of interest flagged in the in-house diversity research conducted





Telefónica Czech Republic:

- ↳ Onsite day care facility.
- ↳ Support programme for employees on maternity/paternity leave.
- ↳ Online portal to enable new mothers to remain in contact with the firm during maternity leave.

Telefónica Germany

- ↳ This company's CEO signed an industry initiative to promote female participation in management positions.
- ↳ Telefónica Germany is also an active participant in an industry programme to increase female representation.

Telefónica Ireland

- ↳ Enhanced flexi-work scheme.

Telefónica UK

- ↳ Mental health awareness campaign.
- ↳ Enhanced flexi-work scheme.
- ↳ Introduction of diversity into sales strategy: new customer segments to consider; enhanced store design; service and language fine-tuning to address underserved customer segments by factoring in their preferences and needs.
- ↳ Launch of 'mumsnet', new sales packages targeted at families.

Some of these initiatives are very local in conception and cannot be readily exported to other countries. Others however deal with issues common to all countries. By way of example, returning to work following parental leave entails a tough adaptation period in all markets. Telefónica is aware of the risk of losing talent if we fail to cater to these needs. The programme for supporting parents on leave seeks to help professionals experiencing these adaptation difficulties without regard for gender.

External research:

Together with LinkedIn, in a research capacity, Telefónica conducted research during the second half of 2011 to understand what makes female professionals satisfied with their jobs and employers. The idea underlying this effort was to try to pinpoint potential shortcomings and barriers as well as positive attributes with a view to moving towards an equal gender mix at the Telefónica Group by placing particular emphasis on ways to help women to get ahead at companies such as ours.

The research methodology is summarised below:

- ↳ **LinkedInResearch Network** selected a representative sample of telecommunications and technology professionals from Spain, Brazil, Ireland, Germany, the Czech Republic and the UK.
- ↳ Those candidates that were members of LinkedIn were asked to participate by means of an e-mail sent by LinkedIn.
- ↳ LinkedIn surveyed **826 members for this research in September 2011**.
- ↳ LinkedIn's **Recruitment Index** was calculated based on responses to a selection of core recruitment questions and is based on 5,000+ responses in recent benchmarking studies.
- ↳ A number of the 826 LinkedIn members surveyed from the various countries and professional categories were also interviewed.
- ↳ The geographic breakdown of the members surveyed: Spain (16%), UK (21%), Ireland (16%), Germany (16%), Czech Republic (15%) and Brazil (16%)
- ↳ The members participating in the survey can be categorised as follows: female salaried employees without children (25%), female managers without children (25%), working mothers (17%) and male senior managers (27%)
- ↳ In the UK, Germany, Ireland and the Czech Republic, the questions were asked about O2 as Telefónica's subsidiary.

The conclusions drawn were of tremendous interest to the firm and have been factored in to the overall diversity management project and to how we manage our human capital in general, reinforcing some the ideas that have always inspired diversity at Telefónica:

- ↳ 360° Diversity. Diversity is a transversal issue and one which must be built in to all areas of the organisation.
- ↳ In terms of the gender diversity issues explored, women rated their career development prospects above all other attributes

It is also worth noting the consistency between the findings of the two studies performed, in-house and with the assistance of LinkedIn, so that they doubly underpin the lines of strategic initiative being taken by Telefónica on the diversity front.

Attracting, recruiting and hiring diverse talent:

For years now Telefónica has been working to try and become the employer of choice for candidates of varying backgrounds, race, gender, age, etc.

The idea is to build diversity considerations into recruitment to fuel a balanced hiring process so that the new hires in turn become diversity advocates, helping the firm achieve a diverse workforce capable of understanding and responding to the needs of customers of differing backgrounds, race, gender, age, etc..

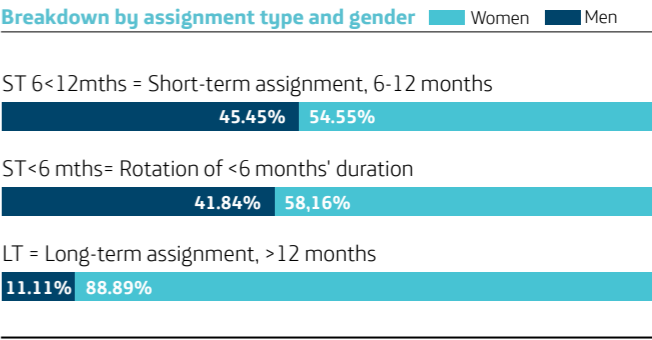
In 2011, the Great Place to Work Institute named Telefónica one of the 25 best companies to work in the world.

Talent mobility as a means to promoting diversity

Telefónica prioritises talent mobility based on its view that it represents a key factor in managing the diversity at its disposal and enables personal and organisational development by fostering the exchange of know-how and best practices across Group companies. This was the reason for the launch in 2008 of the **Global International Placement Management Model**.

Of the new assignments arranged in 2011, 35.26% were taken up by women and 64.74% by men. This marked a decline with respect to participation in 2010 (41% women; 59% men) and was more in line with the 2009 figures (35%/65%).

Looking at the gender breakdown by length of placements, the mix is broadly similar for shorter-term assignments. However, 88.89% of new assignments of 12 months or longer were taken up by men compared to just 11.11% by women. The reason for this discrepancy lies with the fact that in the vast majority of the societies where we do business, the men are the main breadwinners, which is why the women find it harder to take on challenges that entail uprooting the family, no matter how attractive the expatriate package terms.



Occupational health and safety

At Telefónica, occupational health, safety and well-being is governed by the same principles of 'solidity and prestige' that inspire and dictate the Company's Business Principles.

Our objective is to tap the synergies afforded by a global corporate model with a view to implementing common policies, procedures and initiatives that enable us to foster continual improvement with a direct impact on the well-being of employees and a corresponding reduction in workplace accidents.

Mission

The overriding objective is to implement a Global Occupational Health and Safety Management Model across Telefónica's operators in its various markets that allows us to pinpoint and share best practices and monitor the platform as outlined below:

Europe: to continue to extract synergies through implementation of the common global platform coupled with progress on prevention as required.

Spain: to move forward with the continual fine-tuning of the platform.

Latin America: to further consolidate the management platform by enhancing its implementation and reaching for excellence. Medium term the goal is to deploy the global platform in all the companies comprising the Group.

Management body

The Joint Occupational Health and Safety Department (which reports to the HR and Talent Management Department of Telefónica Spain), is the unit designated by the Telefónica Group as its Centre of Excellence for this issue and is tasked with coordinating its global health and safety initiatives.

Through its advisory service, this unit continued to promote health, safety and well-being issues at the operators located in Telefónica's various markets throughout 2011, fostering implementation of the preventative approach across all Group companies and setting the foundations for a global health and safety management system by readying the implementation of the Human Capital 2.0 project.

In 2011, the organisation conducted two studies, one in-house and one external, to determine what is required to optimally manage diversity

GRI indicators, 2011. Global boundary

	IR	ODR	LDR	AR
TOTAL 2011	0.83	0.36	25.62	4,436.23
TOTAL 2010	0.91	0.32	27.78	5,562.11

IR (Injury rate). ODR (Occupational disease rate). IDR (Lost day rate). AR (Absentee rate)

Injury rate (IR): The frequency of injuries relative to the total time worked by the total workforce in the reporting period.

IR= (Total # of injuries / Total hours worked) x 200,000

Occupational disease rate (ODR):The frequency of occupational diseases relative to the total time worked by the total workforce in the reporting period.

ODR= (Total # of occupational disease cases / Total hours worked) x 200,000

Lost day rate (LDR): The impact of occupational accidents and diseases as reflected in time off work by the affected workers. It is expressed by comparing the total lost days to the total number of hours scheduled to be worked by the workforce in the reporting period.

LDR = (Total # of lost days / Total hours worked) x 200,000

Absentee rate (AR): Refers to a measure of actual absentee days lost as defined above, expressed as a percentage of total days scheduled to be worked by the workforce for the same period.

AR= (Total # of missed (absentee) days over the period / Total # of workforce days worked for same period) x 200,000

*Note: The factor 200,000 is derived from 50 working weeks @ 40 hours per 100 employees. By using this factor, the resulting rate is related to the number of employees, not the number of hours.

To facilitate transparency and a meaningful comparison with other sector players, only Telefónica's core businesses have been included in these ratios: fixed and mobile telecommunications operations in all countries in which we do business plus all activities performed in Spain as this is the company's corporate centre. Employees engaged in businesses other than these core businesses (mainly Atento and Terra in Latin America) have been excluded from these calculations. The ATAM companies which hire people according to certain community criteria such as disability considerations were also excluded because this would make a comparison between Telefónica and other telecommunications operators less meaningful as the main purpose of these companies is to integrate people with disability into the workforce.

		CONSEQUENCES			
		SLIGHTLY HARMFUL	HARMFUL	VERY HARMFUL	EXTREMELY HARMFUL
PROBABILITY	VERY LOW	Trivial	Tolerable	Moderate	Moderate
	LOW	Trivial	Tolerable	Significant	Significant
	MEDIUM	Tolerable	Moderate	Very important	Very important
	HIGH	Moderate	Significant	Very important	Very important
	VERY HIGH	Significant	Very significant	Very important	Very significant

Lines of initiative followed in 2011

The following milestones stand out among the initiatives pursued in 2011:

Initiatives pursued by the Health, Safety and Well-being Centre of Excellence

In 2011 this unit continued to work on standardising all health, safety and well-being procedures and guidelines, promoting and disseminating best practices across the Telefónica Group's various operators.

The Centre of Excellence made considerable progress on diagnosing the status of implementation of the health, safety and well-being platform in the various companies by using the 'self-assessment questionnaire' (structured into four levels: beginner, intermediate, advanced and excellent), enabling it to define common occupational health and safety related targets.

Against this backdrop, healthy progress was made in all regions, as shown below:

Europe

In Germany, Ireland, the UK and the Czech Republic, the health and safety management platforms once again obtained the top rating. The Slovakian operator continued to make very noteworthy progress, moving up to 'advanced'. This was achieved by implementing an incident monitoring application into its management platform to enable effective risk monitoring and mitigation.

Spain

At the Spanish business, as part of the overall health monitoring system, the entire workforce is offered a medical check-up every year.

Note that the new collective bargaining agreement signed in Spain provides access to the psychotherapy service as a way to improve the already excellent healthcare services on offer. This further consolidates Telefónica's commitment under the "Good work, good

health" initiative promoted by the European Telecommunications Network Operators (ETNO) involving several regional sector players with a view to sharing best practices in the sector in respect of workplace mental health and well-being management.

Latin America

The Latin American operations made significant progress on their health, safety and well-being management systems. Specifically, the self-diagnosis procedure followed in Argentina, Brazil, Chile, El Salvador, Guatemala, Peru and Venezuela categorised these operators' respective performances as 'advanced'.

"Workshop 2.0 – Global SAP Project"

In 2011 the officers responsible for HR and health and safety all around the world met in Madrid to establish the global process model for the prevention of occupational health and safety hazards and compliance with internal and external health and safety standards for addition to the SAP Human Capital Management tool. Specifically, the corporate "General Assessment of Risk Factors at Telefónica" risk matrix was agreed upon, applying five levels of probability and various degrees of consequence severity to enable estimation of the risks associated with the work performed by the Group's employees.

Lastly, the various risk factors were classified into the following categories: safety, hygiene, ergonomics and psychosociology.

The global risk assessment tool will enable the Group to define a common set of work safety guidelines and procedures and set targets for ongoing improvement across all of Telefónica's regional operators.

Audit of the Health, Safety and Well-being Management System

Having obtained initial OHSAS (Occupational Health and Safety Assessment Series) certification for the occupational health and safety management system at the Group's head office at Distrito Telefónica, in 2011, as part of the verification process stipulated under the above standard, the OHSAS certification was renewed.

The officers responsible for HR and health and safety across the entire Group met to establish the global process model for the prevention of occupational health and safety hazards

The OHSAS model implies continual improvement designed to ensure maintenance of high employee health and safety protection standards as well as the implementation of a management system coordinated and consistent with the organisation's objectives and strategies and designed to reduce incident rates.

Participation by the Joint Occupational Health and Safety Department in the GSM Association's international forum

The GSMA represents the interests of mobile telephony operators worldwide. Over 800 operators, including Telefónica, from more than 220 countries are members.

The GSMA has a myriad of taskforces for the exchange of shared synergies and lines of initiative under the umbrella of the GSMA's overall strategy.

One of these taskforces, the HSSE, is devoted to health and safety specifically in relation to mobile operators and is made up of several operators.

Telefónica's corporate health and safety department participated on the HSSE taskforce by preparing the document titled "Guideline for the prevention of occupational risk related to the protection and prevention of occupational hazards as they relate to infrastructure sharing".

This protocol is designed to provide a series of guidelines on health and safety issues in relation to customary infrastructure sharing arrangements. Already implemented in Spain, the goal was to use the HSSE platform to export it to other countries.

By exchanging information and establishing rules for inter-operator coordination and communication, the parties can establish effective preventative measures that ensure worker safety, regardless of which operator is working at a given site.

Further enhancing preventative action across the Telefónica Group's business regions

In Europe the work put in by Telefónica Slovakia last year is worth special mention: this operator completed risk assessment and risk factor classification work for all its offices.

In addition, the injury rate fell a considerable 15% with respect to 2010, evidencing the improvement associated with the effective implementation of a workplace health and safety management system.

In Latin America it is worth highlighting the work performed in 2011 to boost the continual improvement of the local operators' health and safety programmes. For example, Brazil Vivo ran a course for the prevention of falls from heights with 300 participants.

Chile implemented some 40 emergency plans, to which end the operator had to first inspect the various workplaces, install signs, designate emergency response teams and provide safety talks to all building occupants, etc.

Peru defined safety protocols for work at posts, in underground chambers and for safe driving.

Having appointed 80 health and safety officers, the Venezuelan operation set up a total of 68 health and safety committees.

The Colombian operator achieved the local equivalent of OHSAS 18001 certification (RUC), obtaining a mark of 96%.

To this end it established a health and safety management system structured around four main areas: management leadership and commitment, management system development and execution, risk management and risk assessment and monitoring (audits, corrective and preventative actions, inspections, regulatory compliance monitoring, etc.).



Injury rates

The Telefónica Group Workplace Accident Analysis Tool in place in all the Group's operating regions enables comparable study of accident incident rates across all companies and the definition of measures designed to continually improve the Group's record in this area (further information in the table at the bottom of the page).

The indicators compiled in the various regions in 2011 are as follows:

- Incident rate
- Severity rate
- Average duration rate

Workforce representation in formal joint management-worker health and safety committees

The occupational health and safety model in place in Telefónica's various markets ensures high worker involvement in health and safety matters through their representation on the corresponding joint management-worker health and safety committees, which number 233 across all of Telefónica's markets.

It is worth noting that the work performed by the respective health and safety committees in countries such as Mexico, Chile and Venezuela in 2011 reinforced the occupational health and safety programs in place and their scope of engagement.

The health and safety committees in place in all of Telefónica's markets constitute the channel enabling the deployment of initiatives designed to facilitate delivery of health and safety targets by providing ongoing monitoring and advice on programmed prevention activities.

Accident incidence indicators

Spain	2011	2010	2009
Incident rate	7.78	7.78	7.69
Severity rate	260.13	199.43	208.75
Average duration rate	33.82	25.60	23.02

Europe	2011	2010	2009	Latam	2011	2010	2009
Incident rate	3.52	4.09	5.21	Incident rate	10.79	12.23	8.16
Severity rate	98.73	79.63	89.39	Severity rate	323.27	420.02	137.75
Average duration rate	28.08	19.43	17.12	Average duration rate	29.96	34.33	16.87

Digital inclusion



The elimination of barriers to accessing information and communication technology by leveraging Telefónica's ability to eliminate geographic, social and economic barriers is to promote social inclusion.

Telefónica is committed to developing the economic, social and cultural development of the communities where it does business. This commitment extends to ensuring that all of society can enjoy the benefits of information and communication technologies. Our goal is to eliminate the barriers impeding access to ICTs, whether they be economic, geographic, educational or disability-related.

For several years already, Telefónica's challenge consists of moving from what we term 'social inclusion', which consists of donating money or technology to community and digital inclusion projects, towards a new concept that leverages Telefónica's hallmark business strengths, which derive from its corporate track record as well as its geographic reach and technological prowess. Social innovation at Telefónica is aligned with the company's business strategy so as to maximise the impact of the initiatives by creating value for the business.

Telefónica understands social innovation as new ideas (products, services and models) that fill gaps in society at the same time they create new business opportunities. In short, application of saleable solutions to social challenges in a wide spectrum of areas including healthcare, safety, education, agriculture and access to internet in rural areas.

(for more information, go to www.rcysostenibilidad.telefonica.com/es/innovacion)

Access to remote areas

The geographic divide is a barrier that can impede access to telecommunications service in remote rural areas due to the high cost of bringing the required infrastructure to these areas; this investment is hard to recoup due to the high proportion of fixed costs associated with the services business model. With a view to breaking down this geographic divide, Telefónica earmarks resources to researching new technology and services. Some of the most powerful examples of the work performed in this arena in 2011 were:

ConectaRSE

Last year, Telefónica launched "Connect for growth: Telecommunications-driven rural development prize", intended to pinpoint the best telecommunications-based initiatives developed in rural areas in Spain that had a social and economic impact on their citizens and communities.

The overriding goal of this award is to identify the top transformation practices and best use of ICTs with a view to learning how to manage the business rurally and promote innovation and entrepreneurialism in the process. The ultimate aim is to single out the local towns that are participating in the opportunities thrown up by ICTs, as their experiences could search as an example for many other individual initiatives, collective undertakings, alliances with NGOs and public-private partnerships with an economic/productive impact based on the use of internet, mobile telephony, public telephony and pay-TV technology.

The prizes were awarded to three winners which will receive equipment, training and end-to-end consultancy services for the development and reinforcement of their respective initiatives (\$30,000 for the first prize; \$20,000 for the second prize and \$0,000 for the third prize). Telefónica also awarded five Special Life Testimony Prizes for the most moving stories of change wrought by the use of new technologies.

The first prize went to ASTURS (association of charitable rural tourism) in Capachica (Puno). The winning initiative consists of boosting family skills and abilities, implementing and enhancing tourist services and developing charitable tourism activities targeted at entrepreneurial families living from rural tourism in the less visited towns in Lake Titicaca. ASTURS has enhanced the living conditions of 75 families and nine communities thanks to microloans, skill-building using ICTs and the development of charitable tourist visits. The association is supported by France's DEPARTS and Culture Contact associations.

ConectaRSE aims to pinpoint the best ICT-based initiatives developed in rural areas of the country





Fono Ya Programme in Peru

Movistar created the “Fono Ya” programme in Peru at the end of 2009. It consists of a wireless fixed telephony service supported by cellular technology which has enabled penetration of remote areas without other options for connecting their homes up to the communication networks. By the end of 2011, over 560,000 households boasted communication services thanks to Fono Ya. Under the programme, Movistar is increasing the number people in Peru that can enjoy its telecommunications services.

It is a 'high-speed, user-friendly and affordable' package. Customers simply buy the package and bring it home for set-up to begin talking from the comfort of their own homes. The benefits afforded by this service for the less privileged segments of society include the opportunity to access additional services at no extra costs (e.g. SMS messaging).

Notably, the company had launched its 'virtual Fono Ya top-ups' service in 2010, enabling users to top up their fixed-wireless phone credit virtually in any of 60,000 points of sale around the country, locking in line activity for 30 days at all times.

Conexão Amazônica in Brazil

The Brazilian Amazon is better connection to the world thanks to Telefónica technology, specifically an antenna that will bring broadband internet access and 3G mobile technology to almost 20,000 people living in remote communities in the state of Pará, in the north of Brazil. The antenna, which began to operate in 2009,

was installed in the small town of Belterra, where its almost 13,000 inhabitants had formerly lived in total isolation in the heart of the Amazon without any link to the outside world.

The initiative was developed by Telefónica local mobile operator, Vivo, and Sweden's Ericsson, as part of a major social innovation project spearheaded by NGP Saude e Alegria. For over 22 years this NGO has been working to combat isolation in the region, among other issues.

The advent of our technology had a positive knock-on effect on the lives of these riverside communities by contributing decisively to the region's development. According to research conducted by Facultades Integradas do Tapajós, almost 90% of those polled believe that mobile telephony changed their day-to-day lives for the better; 53% believe it made a decisive contribution to creating companies and jobs; over 40% of students now use internet in their studies; and 20% of these are enrolled for distance learning programmes.

Economic inclusion

Two-thirds of the world's population earns less than \$2,000 a year. In economic, these people form part of what is known as the 'base of the pyramid'. In Latin America alone, close to half of the population of close to 700 million falls into this category, with 25% of the total below the poverty line (implying daily expenditure of just \$2).

However, poverty is not just a Latin American issue. According to a report titled 'Social exclusion and development, 2012' prepared

ICTs are an ideal tool for forging social and economic inclusion in low-income communities

by Fundación FOESSA and Cáritas, the Catholic Church's NGO, the percentage of Spanish households living below the poverty line is almost 22%, with another 25% classified as 'at-risk'.

ICTs are an ideal tool for forging social and economic inclusion in low-income communities. Services such as mobile banking present a very real opportunity for promoting financial inclusion across low-income communities, while speeding up delivery of the UN Millennium Development Goals.

The most noteworthy initiatives sponsored in this field in 2011 were:

Porta a Porta programme in Brazil

In Brazil, Vivo set up a salesforce at the end of 2009 to market the installation of fixed communication services in the low-income segments of the Piratininga neighbourhood in the outskirts of São Paulo. What started out as a pilot test is currently being rollout out in other low-income communities in Brazil. This initiative, dubbed “Porta a Porta” (door-to-door), currently provides jobs directly to some 1,000 people.

The sales people are hired from the communities the service is targeted at; as a result, in addition to generating economic wealth, the initiative has a social impact by the creation of direct employment. And because the salepeople are locals, they inspire greater trust among the potential customers targeted.

Today, Vivo has more than two dozen different initiatives tailored for low-income customers. They are primarily based on a pre-paid pay-as-you-go model. Customers do not pay monthly rental fees and credit can be used for any either fixed or mobile connectivity.

Helping SMEs in Colombia

The “Empresarios Pymedia” program for SME entrepreneurs was set up in Colombia in 2009. The application of ICTs in small and medium sized companies is crucial to increasing the productivity and competitiveness in a global economy. To this end, and taking advantage of technology installed by Telefónica under the Compartel initiative, Telefónica, in collaboration with several Colombian universities, helps local SMEs to adopt ICTs as a means to boosting business competitiveness.

The purpose of the programme is to bring students and graduates of communication and advertising degree courses together to counsel SMEs on implementation strategies and the creation of online advertising campaigns in order to increase their chances to tapping new customers. In short, to create the ideal ecosystem for students and business owners.

The fourth edition of this programme took place in the first half of 2011 and was structured around the “E-volution Ideas” concept. Fifteen universities from seven cities took part, as did 447 companies. The winning company was Guianza Express and the winning university students were two students from Jorge Tadeo Lozano University in Cartagena. The idea for the next editions of this initiative is to entrench the programme at participating universities in order to reach more students; this will also enable Telefónica to increase its SME customer base. Another aim is to create a virtual community of SME businesses owners and to bring in new strategic partners with a view to ensuring the project's sustainability.

Wanda, Financial Inclusion in Latin America

Telefónica and MasterCard have joined forces to set up a joint venture with the aim of spearheading development of mobile-based financial solutions in Latin America.

The agreement encompasses the 12 countries in the region in which Telefónica operates under the Movistar trademark. This is the first time that two leading companies from payments and telecommunications industries join forces to create a new company devoted to integrating the user-friendly and accessibility attributes of mobile telephony with a tool designed to provide financial solutions associated with existing electronic payment systems.

The use of electronic payments platforms is set to extend to new segments which traditionally only accepted cash payments (e.g., taxis and street merchants). The spectrum of opportunities opened up by this initiative spans from the financial inclusion of still unbanked segments of the population to transformation of traditional payment methods by implementing the facilities provided by new technologies, mobile telephony in this instance.

In 2012, Wanda will offer mobile payment solutions to over 87 million Movistar customers in its twelve business markets in the

The Brazilian Amazon is better connected to the world thanks to Telefónica technology that brings internet to remote communities in northern Brazil



region. These mobile payment services will be associated with an m-wallet or prepaid account from which users will be able to transfer money, top up credit, pay bills and do e-shopping, among other things. The m-wallet will be available 24-7, no matter where users are located.

Movistar Remesas

Movistar launched 'Movistar Wire Remittances' in 2010 by which customers can send money quickly and safely to families and friends using more than 200,000 points of sale located across over 190 countries. According to recent research conducted by the World Bank, Latin America receives more than €38.3 billion in money transfers every year, equivalent to 70% of private investment in the region.

This service is the result of a business alliance between Telefónica and MoneyGram International designed to make it easier for Movistar customers to send money from any Movistar Remesas location to the international network of MoneyGram, which has offices all over the world.

Vicente del Bosque, coach for the Spanish football side, inaugurated the new money transfer network by making the first two transfers; the first to a Madrid-based NGO that helps people with Down's syndrome and the second an international wire to Telefónica's Proniño programme in Latin America. The two donations totalled €20,000.

M-Inclusion:

The Mobile Inclusion Platform for Europe and Latin America (M-Inclusion) is a support action co-funded by the European Commission under the FP7. The general objective is to create an online platform to foster cooperative framework between European and Latin American mobile solution developers and entities to encourage the use and growth of innovative, user-oriented, and affordable mobile solutions in order to promote social integration among people at risk of exclusion. The partners in this initiative include three universities: Universitat Politècnica de Valencia (Spain), Universidad Peruana Cayetano Heredia (Peru) and Universidad Federal de Minas Gerais (Brazil).

The project was launched in 2011 and will run for two years. The objective of the project include:

- ↳ To develop an exhaustive inventory action aimed at mapping organizations, actual needs of the target groups and existing mobile solutions and trends for social inclusion in Europe and Latin America.
- ↳ To establish workgroups that identify main needs, analyse technological solutions and trends and define an overall M-INCLUSION road map.
- ↳ To support the identification and promotion of new ideas for future R&D projects.
- ↳ To create awareness on M-INCLUSION action through a wide dissemination of project results.
- ↳ To generate market opportunities within the mobile technologies sector.

This year for the first time, Telefónica, as a member of the European RSE+D disability network sponsored by Fundación ONCE, is publishing most of the indicators recommended by this network to enable the evaluation of the integration of persons with disability at Spanish companies.

Disability indicators	
Indicator	Figure for 2011
Compliance with Spain's Social Integration of the Disabled Act	3.18%
Amount purchased from suppliers that employ PWD* (€) (Spain)	8,979,000
Level of accessibility to web content ** (W3C)	AA
Dialogue with associations representing PWD* (Spain)	Agreements with ONCE, CERMI, CNSE, FIAPAS, FEAPS, ASPAYM Granada and CENTAC
Products / services designed using universal accessibility and 'design for all' principles	Avatar LSE, Braille bill, Special calling plans, ATAM (LAVECO, MONDECO, SERVITELCO, DO2 SOSTENIBLE)
Investment in social innovation and disability (€) ***	9,877,734
Telefónica volunteers that participate in initiatives whose beneficiaries are PWD*	920
PWD* benefitting from corporate volunteering work	11,300

Figures for the Telefónica Group at year-end 2011
(*) PWD: persons with disability
(**) Movistar.es website
(***) LBG figure. Includes sponsorship and initiatives undertaken by Telefónica Europe that benefit PWD and ATAM associations.

'Fishing with Nets' in Brazil

The 'Fishing with 3G nets' programme is designed to foster economic development in Brazil and to increase public safety. To this end, it seeks the digital and social inclusion of isolated people that work in the fishing and fish-farming industries.

Fishing is one of the main way of life in the Bahía region in Brazil and many families depend on it to survive. However, in recent times, the industry has suffered from overfishing, lack of investment and deficient infrastructure. As a result, income has fallen in the fishing-dependent communities, triggering missed opportunities and prompting family members to migrate in search of work.

The 'Fishing with 3G nets' programme offers financing and technical assistance to the IABS (acronym in Portuguese for the Brazilian Environmental Sustainability Institute in Brazil, which is active in sustainable development work.

Under the programme, fishermen and women were provided with handsets with credit for accessing Vivo's 3G HSUPA wireless network. These devices enable them to contact consumers and partners onshore while offshore using voice and data services. Tailored software was also developed for this target audience to build in navigation, climate, marketing, direct sales, data gathering and technical support tools. Lastly, a skills training centre was set up in the town of Santa Cruz Cabralia and on a ship capable to reaching and training the more remote fishing communities.



People with disabilities

Investment in sponsorship and other social innovation and disability related community programmes were close to €10 million in 2011, most of which through the ATAM platform.

The Company runs its Accessible Telefónica programme following the Convention on the Rights of Persons with Disabilities hand in hand with national and international associations for the disabled. Under the umbrella of this programme, the Company made the following progress in Latin America and Europe in 2011:

Europe:

In Spain:
The initiatives undertaken by Telefónica Spain last year and which it will continue to promote in 2012, can be summarised as follows:

- Development of a series of studies to better understand persons with disabilities and their needs

- Development of new products and services such as the Avatar LSE, based on voice recognition software. It also presents the content transcribed by voice in subtitled form in real time.
- Hiring from Special Employment Centres. Hiring from these centres amounted to over €8.5 million in 2011.
- Sponsored hiring of persons with disability. In Spain Telefónica's compliance with the Social Integration of the Disabled Act was 3.18%.
- Creation of accessibility solutions, such as the "Goo Taxi" application which enables users to get a special-needs taxi using mobile phone without having to place a call.
- Provision of accessible handsets targeted a various kinds of disability.
- Adaptation of the various customer care and communication channels to provide customer service adapted by class of disability, e.g. bills in braille and large sized font and the sign language teleintepretation platform.

In the UK:
Telefónica O2 UK offers a wide range of services for persons with disability, including bills in Braille, accessible customer care and dedication corners of the corporate website ("Access for all") containing information of interest. One of O2 UK's new projects was a pilot test intended to form a group of experts in its stores known as 'Gurus' on accessibility issues so that they can advise customers with disabilities on how to get the most from their smartphones and show them how to use the latest accessible mobile applications targeted at the disabled.

In the Czech Republic:
Telefónica O2 in the Czech Republic offers a broad range of discounts for persons with disability as well as special-needs handsets in its stores. One of its new product launches is a special customer service lined for the deaf. This subsidiary also launched an awareness campaign to promote the use of technology by the elderly called "Let's talk about age".

In Ireland:
Telefónica O2 in Ireland has a number of ways of providing customer service to customers with disability including text2speech, email, Twitter, web chats and Facebook. One of the new initiatives in 2011 entailed the provision of sign languages courses to store sales staff to improve the standard of customer care for deaf people throughout O2's Irish stores.

In Germany:
In Germany, Telefónica O2 offers a broad spectrum of services for persons with disability such as accessible customer care services and special offers for deaf people. As a new initiative in 2011, it set up an online store providing access to videos translated into sign language containing information on O2 Germany products and services.

Latin America

Most of the operating markets in Latin America focused on establishing direct contact with various entities and foundations working with persons with disability in 2011 in order to understand what they need from the sector and what opportunities there are for Telefónica.

Access to education

The world of information and communication technology opens up a host of ways for educators and students to broaden and enhance their work, helping in this way to facilitate access to education and raising education standards, crucial to personal development and community welfare. Against this backdrop, Telefónica invests in upgrading the technology skills of groups at risk of exclusion.



The inclusion of persons with disability into the value value chain, whether as employees, customers and/or suppliers, is of paramount importance at Telefónica

Universal Service is a pledge of telecommunication services of a minimum standard and at affordable prices to the entire population



Aula 365

Aula 365 is a free schooling aid leveraging multimedia content first launched in Argentina and later rolled out in Spain and Colombia. Through this educational portal, Telefónica provides its broadband subscribers with advanced Web 2.0 tools to help their children's learning: multimedia educational films, blogs, wikis, infographics, biographies, photo galleries, master classes, etc. This service helps raise school performance among students of all ages thanks to the virtual teacher who resolves doubts and questions.

In 2011 a total of 467 virtual classrooms were up and running, with 220,771 educators registered in the related virtual communities.

For more information, please go to the chapter on Fundación Telefónica.

Technology in childhood

Together with Foro Generaciones Interactivas and Pantallas Amigas, Telefónica launched a new online educational platform last year, Infancia y Tecnología, targeted at boys and girls aged between 6 and 11 and their parents and teachers. By means of three cartoons, the platform tackles issues related to the safe and healthy use of internet, videogames and mobile phones.

The purpose of the website is to provide children with criteria for using all this technology wisely and safely while they have fun and to give adults a close-up and positive view of what this technology can do. The cartoons are intended to teach kids in an entertaining environment while the educational guides are targeted at parents and teachers. Users can also download the cartoons onto mobile handsets.

One of the new developments pursued last year in terms of specifically protecting children and fostering the safe use of internet related to the negotiations concluded in Colombia for the development and launch (during the first half of 2012) of the first hotline in Latin America following the Inhope guidelines.

Interactive Generations Forum

In 2008, Telefónica joined forces with Navarra University and the Inter-American Organization for Higher Education to create the Interactive Generations Forum to learn more about how children and adolescents use new technology in order to draw up educational programmes for encouraging safe use of ICTs.

In 2011, the platform interviewed 127,154 school children in 2,900 schools across 10 countries: Spain, Mexico, Ecuador, Brazil, Argentina, Chile, Colombia, Peru, Venezuela and Uruguay.

Another milestone last year was the presentation of “La Generación Interactiva en Iberoamérica 2010. Niños y adolescentes ante las pantallas” (The Interactive Generation in Ibero-America in 2010. Children and Teens in front of the Screen) by Xavier Bringué, Charo Sádaba and Jorge Tolsá This second report - in which over 78,000 children aged between 6 and 18 took part -, focused on the reality in Ibero-America, highlighting the myriad educational and social challenges posed by intensive use of new technologies and the importance of teaching young people how to use them properly. The book was presented in five countries (Colombia, Guatemala, Mexico, Chile and Argentina) in November and December of last year.

This study was also carried out and published for Madrid, Andalusia and Ecuador. The Forum also published new editions under its “Children and the Social Networks” series”.

Following a period of investigation, the Forum has developed a series of educational initiatives: courses for teachers and educators, parent workshops, hands-on activities for children, etc. Since 2008, some 50,000 people have received training on the proper use of new technologies in Spain and Latin America.

In 2011, the Interactive Generations Forum’s volunteer team gave a total of 32 training sessions in schools and institutions.

	Local currency	Millions
Argentina	84,763,437	14,760,027
Brazil	239,154,248	102,880,570
Peru	46,293,295	12,903,151
Colombia	137,921,372,485	53,693,756
Venezuela	121,485,330	20,317,085
Ecuador	4,348,032	3,126,791
Czech Republic (1)	141,000,000	5,733,906
Spain ⁽¹⁾	44,480,000	44,480,000

(1) Data as of 2010

The health divide

Information and communication technology also provide proven solutions for enhancing healthcare. Very significant developments are taking place on this front which have the scope to improve citizens' quality of living and make healthcare more affordable and democratic.

Some of the e-Health initiatives launched in 2011 with a view to surmounting the health divide among at-risk citizens included:

Universal Service

Universal Service is a pledge of telecommunication services of a minimum standard and at affordable prices to the entire population. These services and the terms on which they are provided, including which operators bear this responsibility, are regulated by the telecoms watchdogs in each market as they see fit.

The purpose of these universal service funds is to ensure funding mechanisms for financing the investments needs to bring telecommunication services to the entire population to the stipulated quality standards and at the required prices.

Telefónica provides universal coverage services in Argentina, Brazil, Colombia, Spain, Peru, the Czech Republic and Venezuela.

Responsiveness to emergency situations



Good management of the telecommunications networks and services is crucial to enabling emergency response teams to act rapidly and effectively in natural disasters and other catastrophes.



Telecommunications services play a crucial role in the management of healthcare emergencies, natural disasters and other humanitarian catastrophes as they enable massive alert deployment, taskforce coordination, the provision of support for charity drives and more effective search operations.

Here at Telefónica we are aware of the positive role that competent management of our networks can play in preventing and mitigating these kinds of emergency situations. To this end we establish Business Continuity Plans with a view to putting ourselves in a position to continue to offer normal communications services in emergency situations in all of our operating markets. All these plans comply with international standards and factor in the risk factors specific to each region. Execution of these plans typically triggers the use of contingent communications platforms to support operations and speed up recovery in the event of system failure. The fact that the Company has a presence in so many countries enables local operators to help each other if necessary.

In 2011 Telefónica's involvement in the following dramatic national and regional emergency situations stands out.

Earthquake in Lorca (Spain)

The dramatic situation engulfing the citizens of Lorca drove a 15-fold surge in phone calls in the hours immediately following the earthquakes that devastated this town. At one point, Telefónica had to handle over 500,000 simultaneous calls. In response, Telefónica set up a toll-free customer care number and deployed mobile units to provide enhanced coverage at the heart of the affected area.

The Company also set up lines for closed user groups for the emergency military and state security forces, which also sustained notable peaks in caller traffic. Telefónica did not charge for national calls or text messages placed from mobile phones located in Lorca on the day of the quake or the following two days. It also established the so-called "Free calling plan for Lorca" for a maximum term of one year for fixed telephony lines and ADSL and pay-TV services for earthquake victims who lost their homes.

Floods in Central America

Over one million people in El Salvador, Guatemala, Costa Rica, Nicaragua and Honduras were affected by the heavy torrential rains afflicting the region last November, which claimed the lives of over 100 people. The victims included some of the boys and girls in the Proniño programme and their families, many of which were forced to evacuate their homes. Fundación Telefónica called upon all of Telefónica's staff and volunteers to donate generously to a fund to buy essentials such



as food, medicine and clothing and to help locate accommodation for the thousands of people left homeless by the ravaging floods. This charity was channelled through the NGOs and other entities collaborating with the Proniño programme in the affected countries.

Puyehue-Cordón Caulle volcano eruption (Argentina)

To mark its sympathy for the inhabitants of the Patagonia towns affected by the volcanic and ash eruption, Telefónica offered all its local customers one month of free calls and discounts of up to 50%. We also released access to all educational content on our Aula365 Speedy social network to facilitate interaction so that isolated teachers and students could keep up their schooling from home.

Floods in Rio de Janeiro (Brazil)

In addition to making an extraordinary donation of one million dollars for the flood victims, Telefónica gave 100 professionals a half day so they could volunteer with the Red Cross, helping to sort and distribute donations. We opened an account for donations to the Brazilian branch of the Red Cross and set up boxes for collecting donations at the Campus Party ongoing at that time in Sao Paulo. Telefónica also ran a charitable SMS campaign. In addition, Vivo gave 30 devices and voice and data plans to the Brazilian civil defence force for communicating with the refugees located in the flooded areas. This campaign entails sending text messages to customers urging them to donate.

Social projects



Telefónica is committed to promoting the economic, social and cultural development of the communities where it does business. This commitment extends to ensuring that all of society can enjoy the benefits of information and communication technologies.

In 2011, Telefónica set aside €143.26 million for community investment, an 8.6% increase on the previous year. Importantly, 97.4 % of this was in cash and the criteria used to pick our investments followed the standard methodology of the London Benchmarking Group and was externally audited by LBG. The aim was to give a full and complete picture of the reach and value of our

investment in the community, to measure the impact of our actions, to help manage our relationships with the community and charitable sector and to make projects easier to insure.

Also, the large size of the "Other" line (3.3% of the total) reflects a one-off grant by Fundación Telefónica to Colombia following floods that had a particularly severe impact in Manaté, the very area where Fundación Telefónica Colombia was holding its 1st National Youth Conference.

Fundación Telefónica

Fundación Telefónica's mission is to invest in communities and culture in a way that is both effective and transformative, focusing on broadening access to knowledge through an innovative and global approach. To do this, it works through its own social innovation programmes, which make use of new technologies and cooperative networks to help children and young people in particular.

The Fundación works in all the main countries where Telefónica is active and its principal social aims are: the eradication of child labour in Latin America, improving the quality of education and knowledge through ICTs and sharing knowledge through all sections of society.

It also manages the Group's multicultural network of volunteers, supporting the development of charity work by employees in partnership with other institutions.

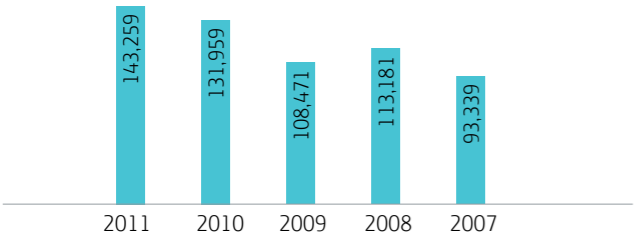
When picking projects to support, Fundación Telefónica's strategy is to focus on those that promote broader access to education and knowledge and the use of information and communication technologies (ICTs). In this way it seeks to foster equal opportunities in the societies where it works, boosting access to education and knowledge as a route to improving people's well-being.

Childhood

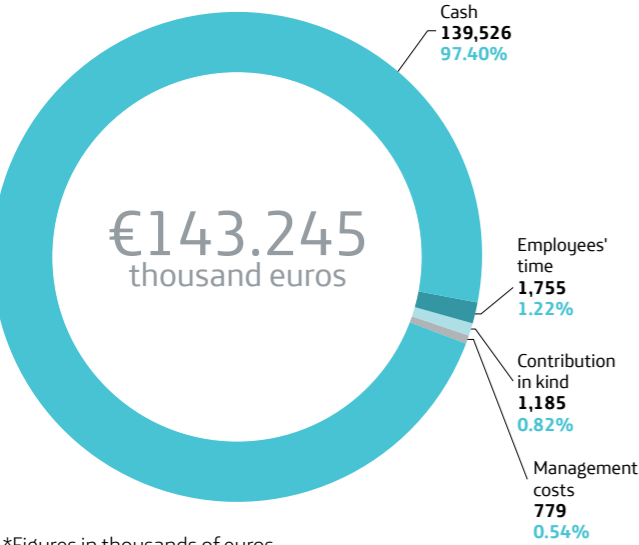
One of Fundación Telefónica's most important projects is Proniño, which combats child labour by promoting school attendance and caring for children and teenagers in Latin America. It is the biggest initiative of its kind by any private company.

In 2011, 279,511 girls, boys and teenagers were helped by the Proniño programme to continue attending 6,496 schools and 889 educational support centres in 13 countries.

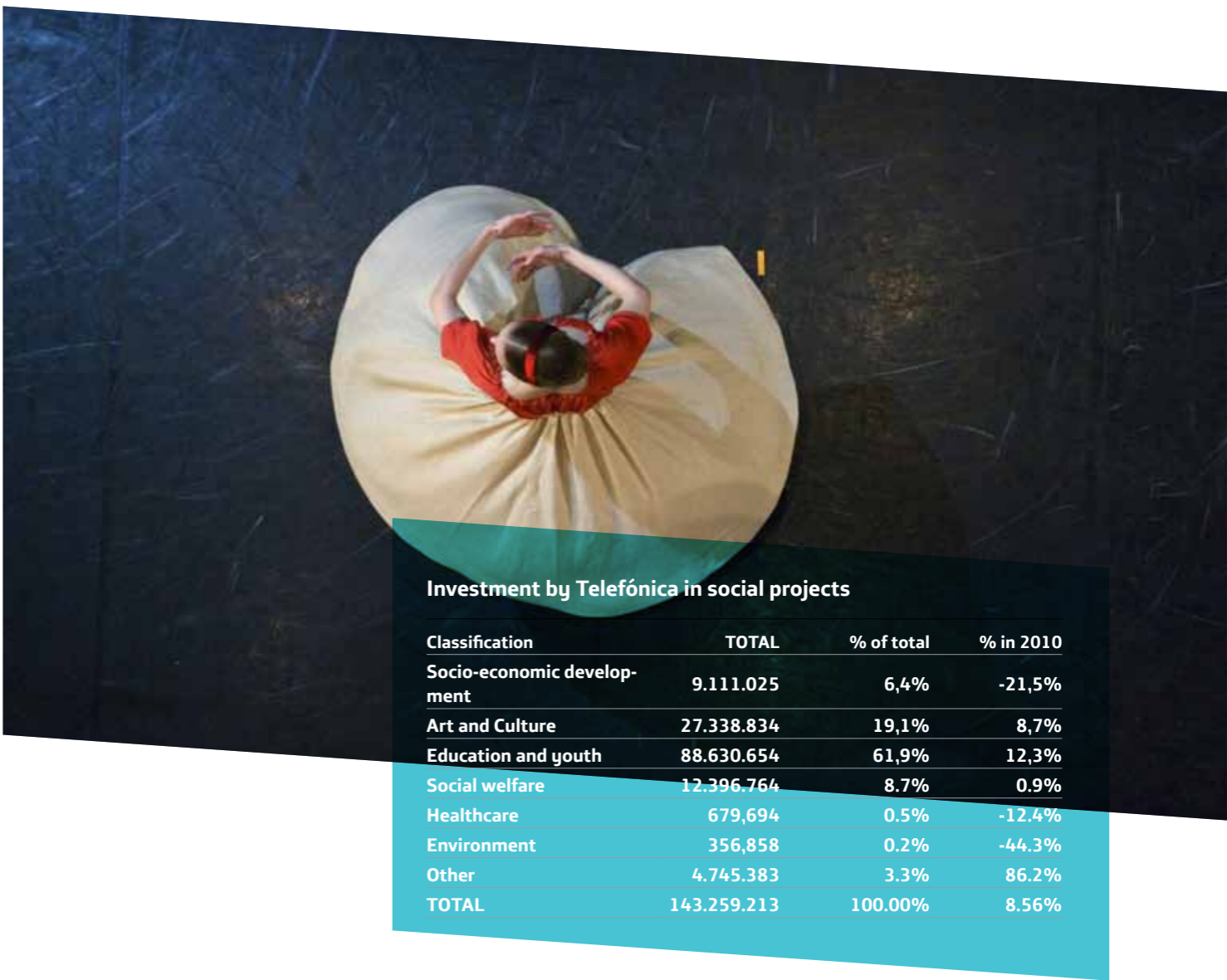
Trend in community investment*



Form of contribution: 2011*



*Figures in thousands of euros



Youth

The Fundación's projects to promote education and knowledge among young people have two strands. The first is targeted at young people coming out of Proniño Secondary schools in Latin America and aims to keep them in education. The second is the "What really matters" programme in Spain, conferences where young students and would-be students are given the opportunity to share personal success stories with speakers who use them to encourage positive attitudes and reflections on what really matters in life.

On 31 December 2011, 2,704 young people were registered in the entrepreneurship and continuing education project and over the year 477 continuing education grants were awarded.

People with disabilities

Telefónica's activities, particularly those of Fundación Telefónica, in the area of disabilities include a substantial R&D effort aimed at making it easier for people with disabilities to access information, communication, training and employment, improving healthcare and support for those who are old, sick, incapacitated or vulnerable, and helping with health education and preventative approaches to dealing with various illnesses and disabilities.

Community development

In 2011, Fundación Telefónica ran a number of trials in local development, such as Conexión Amazónica (Amazon Connection) in the Brazilian Amazon, and projects in Santo Antonio Park, São Paulo and Santa Cruz de Cabralia, Bahía. The aim of all these projects is to improve the quality of life for local people in a sustainable manner through access to technology.

Aulas Fundación Telefónica

Aulas Fundación Telefónica is a digital inclusion venture that promotes the use of new technologies as an essential tool for raising educational standards in Latin America.

Fundación Telefónica has developed a teaching model for training and ongoing support for teachers, which seeks to establish a virtual educational community (the Educator's Network). The aim is to create a learning space where teachers can exchange and share experiences with teachers from other Aulas Fundación Telefónica projects across Latin America, guided by a group of project leaders who are experts in orientation and training. The Aulas Fundación Telefónica network is part of the drive to meet the OEI's 2021 Educational Targets, not only by strengthening the educational

infrastructure but also by creating networks, opening up access to knowledge and narrowing the digital divide for underprivileged populations in the public schools that we partner.

The great strength of this project is that teachers follow an educational path that walks them through the different ways technology can be used, including collaborative environments, content production and methods for using ICT in the classroom.

In 2011, 467 Aulas Fundación Telefónica projects were in operation.

Escuelas Amigas (Friend Schools)

Escuelas Amigas is a project for cultural connection and exchange over the internet between schoolchildren in Spain and Latin America. The Latin American students come from schools where some are direct or indirect beneficiaries of the Proniño project.

The project has three participants: the students, the teachers and the Telefónica volunteers, who act as enablers for the activities. The starting point for Escuelas Amigas is the use of ICTs in the learning process as a means of breaking down geographical and cultural barriers.

EducaRed

The EducaRed website is home to an online cross-cultural learning community and is an international benchmark for the analysis of educational innovation. It promotes interaction between teachers, students, parents and teaching centres to share educational values across cultures. In 2011, we had 220,711 teachers registered in virtual communities and ran 34,747 online training sessions.

Fundación Telefónica sponsors the EducaRed International Awards for teachers from across the globe who have helped to improve education via ICTs. In 2011, the 6th International EducaRed Meeting took place, with 13,050 people signing up to its online phase and more than 1,300 attending the event in Madrid.

Teaching art

Fundación Telefónica has developed a series of educational programmes for school-age children, families and adults and other groups, tailored to the needs and interests of each audience. These programmes aim to create a space for dialogue, exchange,

observation, analysis and critical reflection that enriches and opens the eyes of our visitors.

The Fundación also carries out research, stages conferences and seminars with respected international artists and promotes contemporary artistic creation where it overlaps with technology via international competitions and an ambitious exhibition programme.

During the year, 42,678 people took part in 2,508 educational projects in Spain and Latin America associated with the various exhibitions.

Volunteers at Telefónica

Fundación Telefónica runs a multicultural network of volunteers from Telefónica Group, which supports social and collaborative projects by employees. The volunteers undertake charity work either as part of Fundación Telefónica's own programmes or in partnership with other foundations.

Volunteering is designed to channel the Telefónica Group's employees' charitable spirit by offering them ways to contribute their time, knowledge and/or money to help the neediest. Through this initiative, Fundación Telefónica helps to promote good citizenship in the societies where it operates.

The programme runs in all 19 countries where Telefónica Group is active, and in 2011 some 26,000 volunteers took an active part in the 1,459 volunteering initiatives on offer.

Social impact indicators in 2011

- Approximately 26,000 active volunteers at 31 December 2011.
- 1,459 volunteering initiatives carried out.
- 268,660 direct beneficiaries.
- 112,943 hours of volunteering.

ATAM runs the online course "Volunteering in disability-related projects" as part of Proyecto Pro with the Antena 3 foundation. This is a training programme in the theory and practice of helping people with disabilities. The training programme is aimed at volunteers working with people with disabilities or those who are interested in or unsure about this sort of volunteering. Five courses were run in 2011 for a total of 143 participants.



Integration of disabled people: ATAM

ATAM is a Telefónica-sponsored not-for-profit body recognised as a public service entity for its nearly 40 years' work aimed at preventing disability and supporting the social integration of people with disabilities.

In 2011 this involved more than 56,000 employee partners, either working, retired or having taken early retirement in the 30 Telefónica companies that currently have collaboration agreements with ATAM. Together they raised more than €14 million over the year. Thanks to this funding and the efforts of the association's nearly 100 full-time employees and co-workers more than 13,000 people were able to take advantage of ATAM's different programmes and services.

ATAM works in three main areas: family support, direct support centres and employment support.

Family support

ATAM provides personalised solutions for any need arising from situations of disability and dependency in the family environment through a network of support points throughout Spain. By deploying appropriate support, drawing on public and private

services and ATAM's own resources the network is able to provide help that focuses on the individual. In 2011, 3 family support points were set up: one in Seville for western Andalusia, another in Barcelona for Catalonia and the third in Bilbao for Cantabria and the Basque Country.

ATAM also has a system of **individual** financial support. In 2011, it invested more than €6.5 million to ease the costs of living with disability borne by people and their families. These grants cover any type of disability, physical, mental or sensory, and are delivered through two programmes aimed at people under and over the age of 60. During the year, 4,800 people with disabilities received 3,484 support payments, a 7.5% increase on 2010.

As for the **prevention of and recovery from disability** work continued through ATAM's clinical team of healthcare and psychological professionals. The team held 2,087 consultations in various specialisms in 2011 (ophthalmology, psychiatry, neurology, psychology, rehabilitation).

The year also saw the start of two innovative projects as part of the family support programme. **T, Resuelve** is a toll-free line that offers guidance to families throughout Spain on social or psychological concerns and doubts. In 2011 it dealt with 594

enquiries. **Aprende** is ATAM's online social training space which deals with a range of social issues. In 2011, it held its first course for 273 trainees looking at the preparation of non-professional carers for older people.

Direct support

ATAM backs up the public system with direct support centres providing education, care and residential assistance to people with severe disabilities. These services helped 140 people with disabilities in 2011.

Employment support

ATAM promotes the employment of people with disabilities in the spirit of equal opportunities. This work is done by personal advisors from the Social Support Network in partnership with the central unit. These advisors, who work throughout Spain, have an intimate knowledge of local circumstances. In 2011, ATAM responded to 762 jobseekers and processed 251 job offers. As a result of their efforts, 281 people with disabilities broke into the labour market. 2011 was especially challenging in this area of cooperation with companies given the problems facing the Spanish jobs market. ATAM also continued its advisory work with Telefónica Group companies.

Despite the protracted, severe and widespread economic crisis, ATAM endeavoured to consolidate the growth of its business activities and, as a result, its companies Laveco, Mondeco, Servitelco and Do2 Sostenible, which operate as Special Employment Centres, employed 527 workers at the end of the year, 92% with disabilities. These people form high-quality teams who overcome the difficulties that may come with disability through technology and training.

The companies work in a range of sectors including industrial laundry services, electrical and electronic component mounting and assembly, integrated environmental management solutions, cleaning, call centres, etc., operating to the same quality and efficiency standards as any rival in the marketplace. Sevitelco is a telemarketing services company, Laveco specialises in industrial laundry, Mondeco mainly assembles industrial components and Do2 Sostenible specialises in environmental care and management. 2011 was an especially momentous year for Servitelco, which increased its workforce by over 70% to 393 from 231 employees in 2010. This followed successful bids in tenders held by Telefónica and public sector bodies, including the one-stop shop service for Telefónica Employees, the Citizen Support Service provided by Madrid City Council's mobility unit and ongoing provision of the call centre service for Telefónica's General Directorate of Transport.

In addition, ATAM continued to work with Fundación Telefónica through the **Mercadis** website, which handles job offers and applications. This year 2,328 new users signed up, along with 46 companies, and 555 job offers were processed.

When a particular individual cannot be placed in an ordinary company or special employment centre because of their characteristics, the organisation looks to provide activities to prepare them for work. The occupational centres develop professional, personal and social skills through a programme of activities. ATAM has 4 resource centres working in partnership with the public sector, serving 247 users and managed in a range of ways.

Awareness campaigns

In December, ATAM took part in a TV programme *"The world moves with you"* on the state broadcaster TVE's channel 2. This is a show about disabilities which seeks to break down barriers faced by people with different physical and sensory disabilities. The report showed the central role work can play in facilitating the social integration of people with disabilities. A number of the association's employees were called on to explain how integration can be achieved and to demonstrate the professionalism and quality of the services

ATAM made great efforts to consolidate its growth and at 31 December 2011 its companies employed 527 people, 92% of whom had a disability.

offered by the special employment centres, which compete in the ordinary market with other companies in their respective sectors.

As usual, ATAM celebrated the International Day of People with Disability by arranging a visit by a group of T-Gestiona employees to the Servitelco and Laveco sites. During the visit, 15 workers from this Telefónica company were able to see the workings of a special employment centre, a model for economic sustainability in the workplace.

Research and healthcare days

In 2011, ATAM's clinical team took part in several medical conferences. In March, it attended the *IV Myasthenia Gravis and Congenital Myasthenia Conference*, which highlighted the importance of providing the right medical treatment for myasthenia gravis. In May, the team took part in the first International Conference at the National Centre for Rare Diseases in Burgos, where it made a presentation on hereditary spastic paraparesis, a rare neuromuscular illness. As part of this work, in October ATAM took part in the *4th National Rare Diseases Conference* organised by D'genes in Murcia and FEDER (the Spanish Rare Disease Federation). The event attracted over 300 people. More than 80 rare illnesses were discussed during the conference, which provided an opportunity for professionals, those affected by rare diseases and their family members to mingle. ATAM's team gave presentations on treatment paths, resource quality assessment and medical acupuncture for patients with rare diseases.



Media coverage of the first edition of the Telefónica Ability Awards (TAA) reached over 57 million people



Coinciding with International Alzheimer's year, Telefónica's Association for the Elderly arranged a day of seminars in association with ATAM called "Alzheimer is spelt with an A for Aid". The ATAM clinical team also took part, contributing its know-how on prevention, detection, diagnosis and treatment of Alzheimer's and on psychological and emotional help for the patient and their family and carers. More than 150 people attended, underlining the high level of interest in the subject and the presentations, which stimulated many contributions from the floor.

Dependent elderly

One of ATAM's lines of work is providing support for the dependent elderly to complement traditional disability-based interventions. In 2011, an agreement was signed with the AGMT to build up channels for communication and relationships, with a view to better identifying and resolving the specific needs of the dependent elderly. Using the system, elderly people can work with ATAM to identify and follow up the needs that arise from disability and dependency among older people and define appropriate responses to this group's problems. An "Ask ATAM" column was also started in Al Habla magazine to answer readers' questions in this area.

Telefónica Ability Awards

Telefónica's Ability Awards honour companies and institutions that develop sustainable business models which incorporate people with disability into the value creation chain as employees, suppliers and/or customers. The companies honoured have incorporated people with disability through their whole production cycle, adding value in a sustainable way.

The awards are given in six broad categories: Commitment of Senior Management and Leadership of Employees; Recruiting and Selection; Accessibility; Customer Counselling; Professional Progress and Training; Prevention and Retention; and in three overall categories: Best large private company, Best small or medium-sized private company and Best public sector organisation.

The first awards were given in 2010, attracting media interest from over 57 million persons. 2011 was the second year and the awards will be presented in 2012.

For the second edition in 2011, more than 410 candidacies were put forward, representing over 230 companies and organisations. This second year stands out for the high quality of the candidates. More than 80% of the organisations submitted met all the requirements to go on to the second stage. The 75 entities that will go before the Jury in 2012 are currently being selected.

The trustees for the awards include institutions, charities and public sector bodies involved with disability, whose staff are members of Club Ability.

Club Ability is a network whose members consistently strive to share and improve on the best practice identified at the Telefónica Ability Awards in the different categories. It currently comprises the 48 Ability Companies and Organisations that were finalists in the first round of awards.

The network has shone a spotlight on pioneering initiatives by Spanish companies and organisations that are worth sharing and publicising. The Club thus becomes a space for collaboration and exchange of best practice, helping all these organisations to meet new challenges and continue to improve. At the same time, Club Ability is raising awareness and changing opinions, helping other companies and organisations to include disability in their business processes.

In 2011, two workshops on the topics of leadership and universal access were held under the auspices of Club Ability. The third is scheduled for 2012 and its theme will be job creation. The workshops discussed the current obstacles to the integration of people with disabilities in the workplace, from the standpoint of leadership and universal access, and what actions or initiatives can be deployed to overcome them.



The year also saw the first Ability breakfast, where the accessibility of social networks was discussed by guests including bloggers with experience in the field of disability and representatives from CERMI, ONCE and the ONCE Foundation.

The first Telefónica Ability Awards ceremony, held on 17 January 2011, was also an opportunity to talk about the next phase: the rollout of the awards in four other countries where Telefónica operates.

<http://www.telefonicaabilityawards.com/>

Think Big

The Think Big programme was launched in Europe during 2010 to support young people in their transition to an independent and responsible adult life. Think Big was set up with backing from Fundación Telefónica. Its aim is to provide financial support and training so that young people can demonstrate their talent to the wider community, make a positive impact and drive forward their role as agents of social change, inspiring and celebrating

their successes as they take the lead in their own projects. The programme is committed to a positive view of youth and was launched in the UK under the slogan "We believe in young people".

The website collects proposals for projects ranging from the struggle against youth crime to improving community spaces or teaching music to other young people. Think Big is now up and running in the UK, Germany, Ireland, the Czech Republic and Slovakia, and supported more than 500 projects and trained nearly 1,600 young people in 2011.

Activities are programmed in cooperation with various leading NGOs (such as, in the UK, the National Youth Agency and UK Youth). The young participants receive appropriate project funding, training, the chance to call on a mentor chosen by themselves from among the Telefónica Volunteers network and support from the company to give their projects national visibility. The programme also includes activities aimed at persuading customers to take an active part in the projects being pitched and developed by the youngsters.



Impact of telecommunications services



Telefónica knows that the key to its leadership lies with its employees, which is why it designs its training, development and compensation programmes with a view to making the Company the best place to work.



External research on the impacts of telecommunications services

At Telefónica we work actively to enhance understanding and generate informed debate on ICTs and their impact on society. We publish research papers, organise specialist workshops and initiate debates on current issues and social impacts.

Publications

Since it was set up in 2006 the Fundación Telefónica/Ariel Collection has published more than 58 titles – books, notebooks and reports – covering research results, specialist workshops and the debates on current issues and social impacts promoted by Fundación Telefónica. Mostly, these address issues of new technologies and their economic, social and cultural

impact on the Information Society. During this time, besides the now classic annual reports on the state of the Information Society in Spain (ISS), which it has been commissioning for 10 years, the Fundación also publishes monographs on specific sectors: ICT and health, ICT and local government and a report on ICT and the Justice system. In 2011, 19 new titles came out in Spanish, Portuguese and English:

http://www.fundacion.telefonica.com/media/que_hacemos/pdf/Catalogo_2011.pdf

Among those with the biggest impact were: Mobile Communications and Economic and Social Development (Manuel Castells, Mireia Fernández-Ardébol and Hernán Galperin), Technological Nomadism (Giselle Beiguelman and Jorge La Ferla) and the 11th Information Society in Spain Report .



Telefónica chair	Thematic line	Telefónica chair	Thematic line
New Generation Internet UPM – Madrid Polytechnic University	Safety	Telemedicine La Laguna University	Healthcare
Sustainability in Mobile Communications UPM – Madrid Polytechnic University	Sustainability	Accessible technologies Las Palmas de Gran Canaria University	Social innovation
Social Applications for Decision Support UC3M – Madrid Carlos III University	Horizontal	Information and Communications Technologies and the Environment University of Oviedo	Energy efficiency
Internet of the Future for Productivity UC3M – Madrid Carlos III University	Productivity	Applied Technology for Energy Efficiency University of Extremadura	Energy Efficiency
The Economics of Telecommunications UC3M – Madrid Carlos III University	Productivity	Smart Networks University of Seville	Technology
Analysis of Evolution and Future Trends in the Information Society UPC – Polytechnic University of Catalonia	Energy efficiency	Scientific Culture and Digital Communications University of Gerona	Education
Social Media Pompeu Fabra University	Horizontal	Corporate Responsibility and Sustainability UNED	Corporate responsibility
New Technologies for the Environment and digital inclusion Polytechnic University of Valencia	Energy efficiency Social innovation	End-to-end Security University of Salamanca	Safety
New Technologies for Education Deusto University	Education	Corporate Social Responsibility University of Alcalá de Henares	Corporate responsibility
Security and Productivity in the Information Society, University of Zaragoza	Productivity Safety	CAPTA – Enhancing Personal Independence University of Alcalá de Henares	Social innovation
Technologies for Data Processing, Storage and Communications in Healthcare applications, University of Navarra	Healthcare	Sustainability and Inclusion University of Valencia	Energy Efficiency
		ICT and the Ageing Society University of León	Social Innovation
		Mobility and Education Chair University of Valladolid	Education

Fundación Telefónica also publishes the magazine TELOS, Innovation and Communication Notebooks, which has become an academic benchmark for communications research and the social impact of ICTs. Four new issues came out in 2011: number 86 (crisis in the public domain), number 87 (new professional profiles for digital communication), number 88 (culture in the digital age) and number 89 (the future of democracy).

Telefónica Professorships

The network of Telefónica Professorships promotes and encourages collaboration between Telefónica and universities to help develop our understanding of the impact ICTs are having in the Information Society.



The Professorships Network fosters a multi-disciplinary approach to this project with specialisation in each field. Research focuses chiefly on education, social innovation, energy efficiency, personal and corporate productivity, corporate social responsibility and sustainability, health, security, social media and technology.

For further information on the research papers, publications and debates generated by Telefónica professorships go to:

<http://www.rcysostenibilidad.telefonica.com/blogs/catedrastelefonica/>

You can also search for "**Telefónica Professorships**" on Twitter, Facebook and Youtube.



Internal research on the impacts of telecommunications services

Telefónica has been running a voluntary teleworking program in Spain since 2006 which has proved very successful and was renewed in the Collective Agreement 2011-2013. The program relies on a climate of trust. Teleworkers can work from home between two and four days a week (or equivalent working hours) and are guaranteed the same union rights and employment terms and conditions, including pay-related.

At December 2011, Telefónica España had 2,407 teleworkers, 1,626 of whom were employed by the fixed telephony business and 781 by the mobile business. The teleworker gender mix is roughly equal. The following chart shows the trend in teleworkers since the initiative was first introduced in 2006.



The scheme is generally highly rated by its users with a few areas for improvement. Some of the main points cited in surveys (of managers and employees) are:

- Some technical glitches with applications and tools: requires faster response times from the workstation
- Social isolation of teleworkers and longer working days.

Other feedback comments from some of those involved were:

- "10% increase in productivity" (Accounting/Treasury)
- "Improvement in personal customer care" (Large Companies)
- "More productive working from home than from the office" (Commercial Services).

Telefónica also gives its employees the same mobile technology as its customers so that they are free to work from outside the office without a specific teleworking contract (laptops, blackberries, iPads, 3G internet, Secure Client, single point remote access (ARU), etc.) The company also subsidises home broadband installation and monthly instalments.

Another big success has been the e-learning online training platform for Telefónica employees. A range of generation 2.0 tools were added in 2011 which will help develop a new internal culture of "**social learning**". Among the most successful programs in 2011 were the **English language school** (over 7,000 students), the **Finance school** (over 2,000 students) and the **ICT school** (over 6,400 students).

Recommendations for responsible use of telecommunications by customers

At Telefónica we help our customers to make responsible use of our products and services, especially when it comes to protecting children, combating spam and promoting energy saving. Our recommendations can be found on the Telefónica website for all mobile, internet and pay TV services.

Telefónica also has collection points in most countries where customers can drop off their unwanted handsets for recycling. In 2010, more than 1,600 tonnes of electrical and electronic equipment materials was recycled from customers' old mobiles. We now offer the option to recycle old phones in all our European markets and in Argentina, Brazil, Chile, Colombia, Ecuador, Mexico, Panama and Peru in Latin America.

At the Telefónica Climate Change and Energy Efficiency Office we have created the Green Customer Experience programme, which means customers can have a green experience from the moment they decide to buy a device through to the end of its useful life. Soon, users of this program will be able to visit green corners in Telefónica's main stores to find out about the offers available under the scheme. These solutions will be branded with the Green Technology icon.

Stakeholder Engagement



Day-to-day management of a company like Telefónica, with a history going back 85 years, demands constant engagement with all our stakeholders, particularly on issues that matter to us all (material issues).



Telefónica's ongoing interaction with its *stakeholders* enables the Company to identify and manage risks and opportunities related to the potential economic, social and environmental impacts of our business. It is also the way to create long-term relationships and trust.

Engaging stakeholders

The new *social media* have created a host of new ways to inform, listen, learn, talk, share and influence and we made increasing use of these media to engage with stakeholders in 2011. In combination with traditional face-to-face meetings, new media not only allowed us to make the best use of both the *online and offline* worlds but also brought added value: discussions with greater breadth, greater participation and greater intensity that develop over time, and better ways to follow up conclusions.

At Telefónica we are also aware that there are many topics we cannot address on our own. These matters demand sector-wide consultation, engage a range of different *stakeholders* (government bodies, NGOs, consumers, academics, scientists...) or straddle the public and private spheres

Issues for engagement

Using its **assessment of materiality**, Telefónica focuses on the issues that really matter to our *stakeholders* and which influence the Company's strategy. We also have a responsibility to engage wherever ICT **overlaps with issues on the public agenda**, i.e. issues that concern society as a whole such as education, health, productivity *e-government*, energy efficiency and climate change and to seek solutions that benefit us all.

Why we engage. At Telefónica we take the view that engagement should help strengthen relationships with stakeholders and **pursue**

concrete results, good for the company and good for the groups involved, and, wherever possible, that **it should link into specific projects**. This could mean tweaking the traditional consultation panels or finding new methods to foster **co-creation** in order to develop specific initiatives, projects and services with *stakeholders*.

In 2011, we continued to **engage on projects that help us manage risks and opportunities** in two main areas:

- 1. Initiatives where we were in some sense reinventing face-to-face engagement, tweaking our approach to change the way we do things.
- 2. Dialogue 2.0 to extract the maximum benefit from social media in relating with our stakeholders.

New initiatives for face-to-face engagement

In Spain and Ireland there were various examples of how greater engagement means better **co-creation** and a different way of doing things, with far greater stakeholder participation. Specifically, it makes it easier to **design services with customers**.

To make sure the voice of customers is heard when bringing new services to market and to get a first hand idea of their needs, in 2011 Movistar **España** rolled out Service Design and Design Thinking methodologies.

Service Design puts users at the heart of the creation process in all its phases (inspiration, ideation and prototyping) through engagement and close observation of their day-to-day usage. This approach helped us design a new voice and broadband access, based on 3G technology, to provide communication services in rural or remote areas which could not be reached through fixed-line technology. The aim is to reach 200,000 people who are currently without broadband, taking us a step closer to universal provision across Spain.



Engagement with service users is most important when dealing with **groups with different needs or capabilities**. In Spain, for instance, we linked up with the Autonomous University of Madrid (UAM) and the CNSE (the Spanish deaf association) to create a 3D avatar that communicates in sign language so that people with hearing difficulties can take part in a videoconference or watch television.

Similarly, after a series of meetings with the Irish Deaf Society, Telefónica **Ireland** launched a special price package for members of this association.

Before we act, we listen

Understanding what the different stakeholders are looking for is key to the success of any new initiative, whether business or philanthropic. Engagement is the best way to bring their real needs to light.

Before launching our social and environmental action programme in the UK, **Think Big Blueprint**, we engaged closely with sustainability experts, employees, customers, suppliers and environmental organisations. The process included studies, interviews, *focus groups* with customers, employee workshops and debates and presentations to customers, charities and NGOs. The contributions garnered fed into the work of the *Sustainability Taskforce* headed by the CEO of Telefónica **UK**, Ronan Dunne



Telefónica had 240 active online social channels in 2011 to engage with different audiences, most of which were on Twitter and Facebook

More inclusive engagement

One of Telefónica's aims is to engage with all parts of the Company and to take account of global as well as local stakeholder groups.

In 2011, for instance, we held mono-stakeholder meetings in different **provinces of Peru**, with employees, customers, media, government representatives, etc. The meetings, known as "Decentralised committees", allowed the **top management team** (general manager and directors) to hear and respond to the concerns of these *stakeholders*.

In these meetings, the "sponsor" is a key figure. The Director of each of Telefónica's ten biggest districts in Peru was charged with maintaining closer relationships with their city, addressing its needs, concerns, development plans, sales targets, etc. and acting as a voice for the area with the Telefónica Peru Management Committee.

A step ahead

Technological progress has brought new forms of communicating, relating, entertaining, expressing opinions, accessing information, working and participating in society. Telefónica is one of the companies at the cutting edge of this digital revolution and we set great store on staying a step ahead by consulting with *stakeholders* on the trends, opportunities and challenges of this new environment.

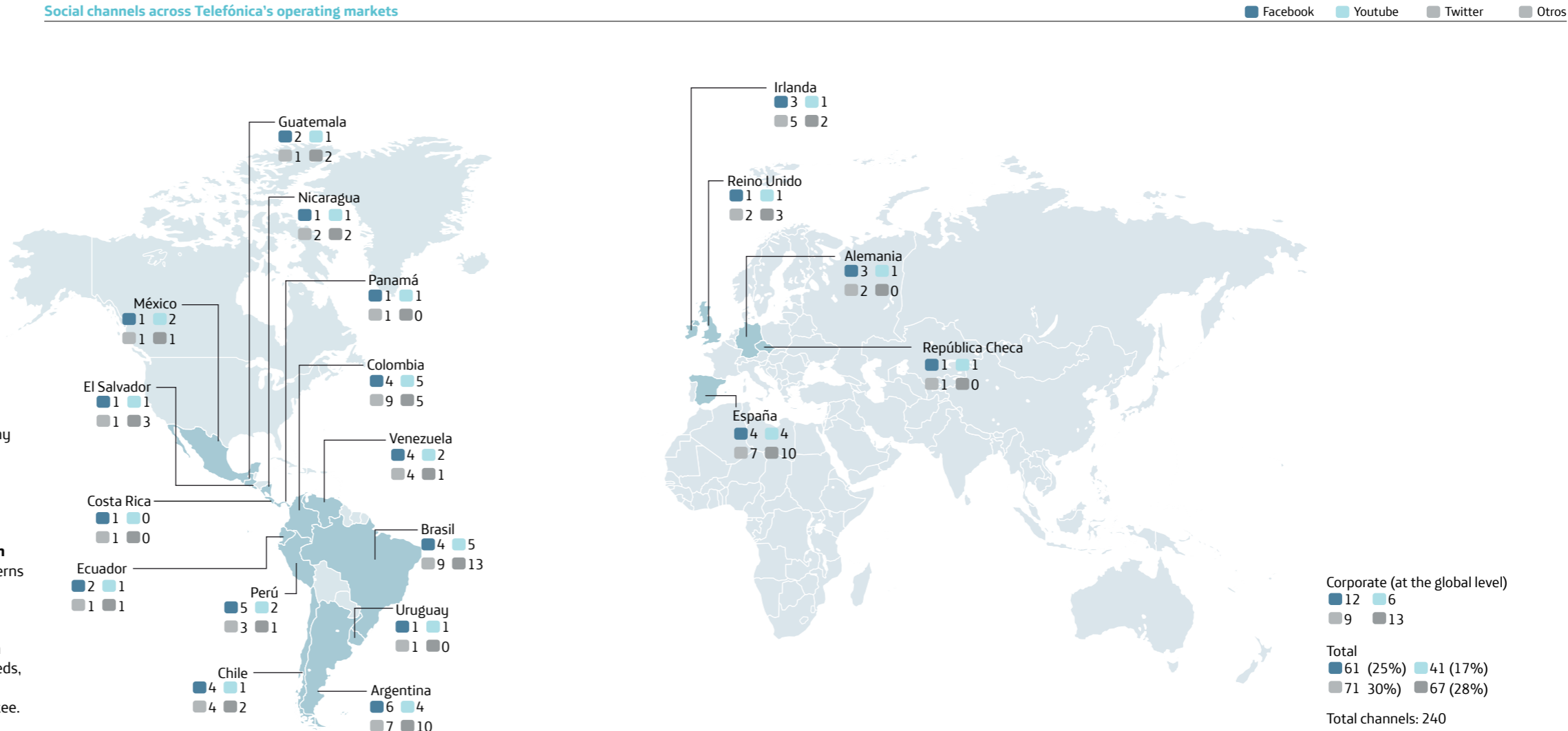
This led Telefónica Colombia to launch its **Digital Culture** initiative, which in 2011 ran eleven digital culture workshops for groups such as teachers, psychologists, employees and the wider digital community (tweeters, bloggers and experts). The meetings yielded proposals such as the use of "digital intelligence" to understand and reflect on social trends around the use of ICT, helping to develop good consumer habits. Other aims were to understand the digital environment in the everyday social world and include the internet in public policy.

Dialogue 2.0.

At Telefónica we had 240 *on line* channels in 2011 (215 in 2010), branded as Telefónica, Movistar, O2 or Vivo, to engage with different audiences. Our strongest web 2.0 footprints are currently in Brazil, Argentina, Spain and Colombia.

Of these channels, 30% use Twitter, 25% Facebook, 17% YouTube and the rest other popular platforms such as Tuenti in Spain (28%).

Social channels across Telefónica's operating markets



Follower numbers for these channels are constantly increasing and Telefónica's digital and *social media* strategy was recognised in 2011 by the **Spanish Internal Communication and Corporate Identity Observatory**.

The stakeholders to whom we gave most attention in these *online* engagement programmes were customers, employees, academics and university teachers, and anyone connected with social networks generally. The dominant issues to emerge were: new products and services, quality, customer service and supply, children and new technologies, digital inclusion, *green* ICTs, the CSR report and social actions.

Our aims in engaging with stakeholders via web 2.0 channels in 2011 were chiefly to learn more about their opinions and expectations, to provide a flexible and efficient channel for customer service and resolving incidents as an alternative to our call centres and stores, to provide more personalised information, to establish an emotional connection and to improve our image among stakeholders in a way that support our operations in our different markets.

Colombia: A growing customer service channel
Telefónica Colombia, through its Movistar and Telefónica Telecom arms, first moved into social networks in mid-2010 to create a space where it could engage with customers. But it was only in 2011 that this initiative started to bear fruit.

The initial step for each operation was to draw up a management strategy and, at the corporate level, March saw the creation of the **Digital Management Committee**, a working group bringing together Customer Service, Marketing, Communication and Institutional Relations.

Work done in the individual companies was coordinated to create a benchmark for social networks in Colombia with more than 150,000 Twitter followers and Facebook fans.

Operationally, for instance, the **@MovistarCo** tag went from handling 1,700 customer cases in September 2011 to 5,500 in December, growth of 223% making it the fastest expanding service channel in the company.

Spain: Different customers, different conversations
In 2011, Movistar España realised it needed to create new 2.0 channels for segments with specific needs and expectations. So it set up various profiles in Twitter, YouTube, Slideshare, Flickr and LinkedIn, Facebook, Google+ and blogs aimed at major customers such as multinationals (www.aunclicdelastic.com), SMEs (www.contunegocio.es) and entrepreneurs and independent traders (www.masquenegocio.com), all with the aim of generating brand loyalty through differentiated content targeting the specific interests of each audience.

At the same time, the Movistar mass market 2.0 channels created in 2010 also went from strength to strength over the year:

- **Tuenti:** 718,010 followers (442,941 a year ago)
- **Facebook:** 120,000 fans (45,207)
- **Twitter:** 55,000 followers (21,427)
- **Forums:** 42,000 registered users (11,000 in 2010), 350,000 unique visitors and 20,000 monthly posts.



Internally, the Company is using web 2.0 channels to deliver information to its employees, encourage dialogue and channel talent

Ireland: New customer care forum and costs under control
In March 2011, Telefónica Ireland joined the country's most popular web 2.0 community, *boards.ie* with the primary aim of improving its customer care.

The idea was to create a forum that would reduce calls from customers by acting as an alternative customer care channel and promoting *peer to peer* (P2P) problem solving without involving company agents. In this way, customers can resolve doubts and incidents quickly on a platform that is relatively cheap to run. Since its creation it has had 9,266 posts.

United Kingdom: Engaging with users for better products

In 2011, Telefónica UK launched **1st Edition**, a platform where customers work together to mould new digital applications before their launch. In this way, the company engages with customers to help improve products and the user experience on the go.

This model was used to develop *O2 Connect*: a new mobile service which allows *smartphone* users to make calls through WiFi networks using their regular mobile numbers.

The initiative also acts as a lever for innovation and cooperation, helping reduce time-to-market in an ever more competitive environment.

Plans are in place to roll out 1st Edition in other Telefónica Europe markets over the coming months.

Venezuela: Trust and proximity in changing times
@MovistarVe has undergone an overhaul since it was first launched and ended 2011 as the leading social network account in Venezuela's service sector. Telefónica Venezuela is the only telecoms firm with an official space for listening to, engaging with and giving specific responses to the most important needs of its users.

On balance, the change in the year was for the good: the account held up well and follower numbers kept growing, to 257,497 at the time of writing.

Web 2.0 tools for our people

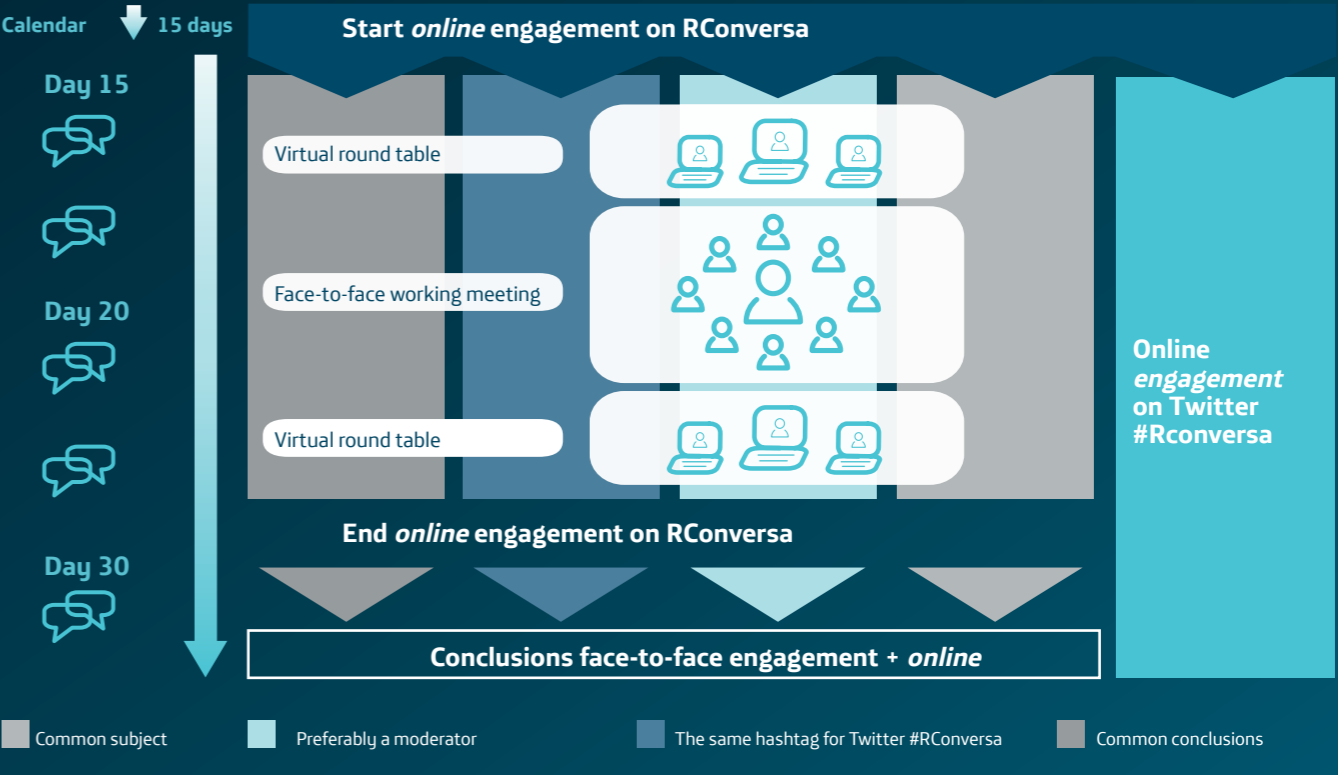
Telefónica is using web 2.0 channels to deliver information to employees, engage with them, channel talent, encourage cooperation, align day-to-day work with the Company's business aims and foster a feeling of belonging.

Yammer

Yammer has become firmly established in the company and had more than 20,000 users at the end of 2011: around 14,000 in Europe and some 7,000 in Latin America.



Example of how the dialogue methodology works



New ways to talk about Sustainability

In 2011, Telefónica developed a methodology for combining 2.0 channels with traditional face-to-face meetings with stakeholders.

For instance, based on *offline* events dealing with key issues facing the Company and its stakeholders, we *hold online debates via RConversa*, a platform created by Telefónica in mid-2011.

Debate on the *website* can be enriched by adding surveys, documents and links of interest, and it also links into the big social networks to broaden the reach of the conversation and increase participation (debates can move to Twitter using the #RConversa hashtag).

There is continuous feedback between *offline* and *online* worlds throughout the process as online contributions are brought into the physical debate and vice-versa. The moderator, a key figure in the methodology developed by the Company, acts as the transmitter, animating the conversation and pulling together the best ideas in the conclusions.

Throughout the conversation, we pay special attention to contributions from stakeholders to identify risks and opportunities for Telefónica arising from economic, environmental and social development and to build a closer relationship with the *stakeholders*.

Themes addressed at the time of writing include the commitment to universal access, the *green* consumer and the impact of new technologies on personal independence, development in rural areas and the growth of SMEs.

2.0 Channels: the Sustainability ecosystem

In 2011, Telefónica continued to strengthen its Responsibility *social media* ecosystem. This includes a website, a blog, a Twitter account, a YouTube and Flickr presence and the new RConversa platform.

Using these channels the Group can address issues such as energy efficiency and *green* ICT, social innovation, disability, children and new technologies, etc. The concept and the value of sustainability and *stakeholder engagement* generally were also topics frequently discussed with stakeholders.

The blog www.rcysostenibilidad.telefonica.com/blogs includes posts by Telefónica professionals and other experts on the subject. Content mainly serves as a starting point for wider conversations, most of which take place on Twitter. Effectively, the blog acts as a platform where we can post news, trend analyses, educational materials, practical advice, etc.. In 2011 we launched local versions in countries including Colombia and Mexico.

On Twitter the @RCySost (Sustainability) account is established as a benchmark in its field, attracting more than 23.5 million impacts by the end of 2011 (up from 1 million in 2010). In other words, @RCySost *tweets* appeared more than 23.5 million times in the *timelines*. The @RCySost concept has also been rolled out by Telefónica's local operations in Argentina, Colombia and El Salvador.

In addition, paper.li (an online journal that recycles selected Twitter content) was a way for us to discuss strategic issues in greater depth:



The network is proving very useful for sharing information, plans, concerns and customer or business issues. It has also become a good way for employees to feed ideas into ongoing projects which may even come to them outside office hours and be shared on Yammer via *smartphones*. For instance, *microblogging* on this channel in 2011 facilitated decision-making in areas like human resources and internal communications as well as at top management level.

Some of the most active Yammer communities have been formed by the *online* channel heads in Latin America and the communities on Telefónica's knowledge-sharing platform eKISS. Training is also moving into this new medium: each school (English School, ICT School, etc.) on our *e-learning* platform has or will soon have a Yammer extension.

eKISS is an internal global platform for engagement and knowledge-sharing that currently hosts over 200,000 documents and which had more than 250,000 visits and 32.5 million accesses in 2011. The eKISS team also arranges face-to-face conferences for all employees with online access, either in real-time or recorded, attended by more than 15,000 people

Internal wiki
The **Comunica 2.0** project, launched in November 2009, aims to compile and share the existing knowledge in our Company. In this way, employees can access and publish information on products and services, projects, departments and employee profiles. At the end of 2011, it had more than 5,500 registered users, 52% more than in 2010, and more than 3,200 new entries, a 17% increase. In 2011, we are working on extending the Wiki to Telefónica Europe, starting with Spain. The tool was launched in the Department for Audiovisual Content Development and the Corporates unit.

Phase two will see the start of a microblogging ecosystem using Yammer. Communities were set up in 2011 by Latin America Internal Communications, the mobile business's Online Channel and the Analytical Accounting community in Latin America, among others.

Yammer communities are smoothing progress towards the third project milestone, the internal social network. A number of other potential collaborative web scenarios were also worked on in 2011, including the DNA pilot in Argentina.

The Shareholder Relations Office answered a total of 63,142 telephone calls and received over 2,500 enquiries via email, most regarding share prices and stock market performance

Shareholder relations

Telefónica is fully listed on the stock market and its 4,563,996,485 ordinary shares, each with a par value of €1, are held by nearly a million and a half shareholders. Telefónica shares are quoted on the Spanish continuous market (as part of the selective Ibex 35 index) and on Spain's four stock markets (Madrid, Barcelona, Bilbao and Valencia), as well as on the London, Tokyo, New York, Buenos Aires, São Paulo and Lima markets.

In 2011, we earmarked €7.966 billion for shareholder remuneration, equivalent to 86% of free cash flow during the year and around 13% of the Company's year-end market capitalisation. Shareholder remuneration took the form of a cash dividend (€7.580 billion) and a share buyback (€386 million). Full details of shareholder remuneration can be found here

Since 2003, when Telefónica's Board of Directors adopted the Spanish and International Standards for Market Reporting and Disclosures, the company has immediately and simultaneously released to all markets where it is traded any information it deems relevant and which should therefore be reported to the market. These disclosures are published continuously on our website where anyone interested can find all reference information, both current and historical

As well as the website, Telefónica has a number of other communication tools and channels to ensure transparency and fair treatment for retail and institutional shareholders. These are set out in the Telefónica Board Regulations. It is standard practice to engage on Sustainability issues with shareholders and other stakeholders, which helps to mitigate risks, identify new business opportunities and improve financial results. These communication channels operate mostly through two departments: the Investor Office, which looks after individual shareholders, and the Investor Relations department, which deals with institutional shareholders.

Individual shareholders

Through our Investor Office, we ensure transparent and fluid communication with our individual shareholders. At year-end 2011, more than 200,000 shareholders were registered for the Shareholder Service. This entitles them to hold the Shareholder Card identifying them as Company shareholders and to receive the quarterly magazine Acción Telefónica. Acción Telefónica provides financial information and reports on current events and campaigns exclusively for our shareholders. In 2011, we mailed 597,582 copies of the magazine to our shareholders.

Our Investor Office's toll-free number (900 111-004) received 63,142 calls in 2011, or an average of 5,262 calls per month. During the period when our General Shareholders' Meeting was being held, the monthly average number of calls rose to 19,000. In addition to these telephone queries, the Investor Office answered more than 2,500 inquiries sent by e-mail (accion.telefonica@telefonica.es) and regular post.

The topics on which our shareholders most frequently inquired were:

- General Company information: 5.865
- Financial information: 43.960
 - 16,832 inquiries on the General Shareholders' Meeting.
 - 20,505 inquiries on stock market trends and share price.
 - 6,555 inquiries on earnings and significant events.
 - 68 inquiries on capital increases and special financial transactions.
- Exclusive campaigns for shareholders: 11.206
- Other: 2.111

Three key developments for engagement

- Telefónica has incorporated fresh *social media* initiatives in order to identify needs, risks and opportunities when engaging with its customers and shareholders.
- In mid 2011 the Company launched RConversa, an *online* platform created to generate debate on key issues for the Group and its *stakeholders*, complementing the *offline* events organised by Telefónica.
- Since 2003 the Company has been disseminating all relevant information immediately via its website, the Shareholder Relations Office and the Investor Relations department.

In addition, and as has become customary at the Company, the Investor Office was present last year at the Bolsalia and Borsadiner fairs, Spain's most important events for financial professionals, savers and investors.

Institutional investors

We communicate with institutional investors through a dedicated email address (ir@telefonica.es) and the Investor Relations department, reporting directly to the General Manager of Strategy, Finance and Corporate Development. Investor Relations provides personal contact for institutional investors and maintains day-to-day communications with international investment professionals, as well as representing the Company at professional events around the world. It is responsible for keeping markets informed about the Company's key organisational, operational and business strategies, and releasing forecasts for future development, helping to keep stock market prices transparent and sustainable.

In 2011, we held face-to-face meetings with 809 investors and 188 analysts, an increase of 5.6% and 43.5% respectively on 2010. We also represented the Company at nine events for investment professionals in Spain, Europe, Latin America and the US.



A particular highlight was the VIII Investor Conference, held in London on 13 and 14 April and attended by 450 professionals. Around half were there in person, representing around 23% of Telefónica's share capital, and the others followed via webcast. All the Company's top executives were present and managers from across the business were able to interact with those attending, either in main hall presentations or smaller group sessions.

Relations with the regulator: Competition and Regulation

Competition Law

Europe

In 2011, no material cases were decided against Telefónica, nor did the company receive any material sanction. The most significant new legal actions launched in 2011 were as follows:

On 5 January 2011, the European Commission sent a demand for information to Telefónica S.A. regarding its agreements with Portugal Telecom SGPS, S.A. (Portugal Telecom) to buy the latter's stake in the Joint Venture Basilcel, N.V., invested by the two companies and owned by Brazilian company Vivo. On 19 January

and Telefónica Móviles España filed their defence against the draft ruling in November 2011.

Finally, in March 2011 Telefónica Czech Republic received several demands for information from the Czech Competition Authorities, which then began an action for alleged anti-competitive behaviour, specifically price-fixing by a margin squeeze. This action is currently ongoing.

Latin America.

Actions decided against Telefónica included most notably two anti-competitive behaviour cases: one in Chile which resulted in a fine of approximately €2,211,880, and another in El Salvador, resulting in a fine of approximately €187,456.50.

The most significant new legal actions begun in 2011 were in Chile, where the Competition Court began hearing two cases about the anti-competitive impact of differential pricing of off-net and on-net public telephony services and the bundled offer of telecommunications services. These are not adversarial proceedings and any ruling will lay down instructions of general application to the market rather than imposing sanctions or fines.

In Peru in 2011, OSIPTEL launched a suit against Telefónica del Perú for anti-competitive behaviour in respect of alleged tied sales in the fixed telephony and internet market. Telefónica filed its response in September 2011 and the trial is currently in its investigation phase.

Regulation

Europe

In 2011, no material actions were found or filed against Telefónica. Nor was Telefónica subject to any material sanction during the year.

Latin America

In Brazil during 2011, 81 legal actions were brought against Telefónica and 357 were settled against the Company, with sanctions totalling €28,295,381 imposed as a result.

Global Compact Progress Report



Global Compact Progress Report



We telecommunications operators are in the vanguard of the digital revolution, a phenomenon which is changing how we communicate, inform ourselves and relate to one another and bringing about advances in a multitude of areas (commerce, education, health, government...).



The Ten Principles of the Global Compact

HUMAN RIGHTS:

- Principle 1:** Businesses should support and respect the protection of internationally proclaimed human rights within their sphere of influence.
- Principle 2:** Businesses should make sure they are not complicit in human rights abuses.

LABOUR STANDARDS:

- Principle 3:** Businesses should uphold the freedom of association and the effective recognition of the right to collective bargaining.
- Principle 4:** Businesses should support the elimination of all forms of forced or compulsory labour.
- Principle 5:** Businesses should support the effective abolition of child labour.
- Principle 6:** Businesses should uphold the elimination of discrimination in respect of employment and occupation.

ENVIRONMENT:

- Principle 7:** Businesses should follow a preventive approach in favour of the environment.
- Principle 8:** Businesses should encourage initiatives that promote greater environmental responsibility.
- Principle 9:** Businesses should encourage the development and diffusion of environmentally friendly technologies.

ANTI-CORRUPTION:

- Principle 10:** Businesses should work against corruption in all its forms, including extortion and bribery.



The United Nations Global Compact is a strategic policy initiative for businesses that are committed to aligning their operations and strategies with ten universally accepted principles in the areas of human rights, labour, environment and anti-corruption. Telefónica became a signatory to the Global Compact in 2000 and has actively assisted the Global Compact Office in New York and its National Networks present in most of the countries in which we operate in the dissemination and promotion of these principles.

In January 2011 at the World Economic Forum in Davos the Global Compact announced the creation of a new platform to promote sustainability worldwide comprising 54 companies. Telefónica is one of the LEAD companies, which means it is one of the 54 multinationals identified by the United Nations as global leaders in sustainability. We are also members of the LEAD Executive Committee. Spain's only LEAD members are Telefónica, BBVA, Endesa and Acciona.

Our membership of the Global Compact LEAD Group has been recognised by a large group of PRI investors headed by Aviva Investors, Amundi Group, the Swedish national pension funds AP1, AP2, and AP3, Boston Common Asset Management, CPP Investment Board, Cyrt Investments, Dexia AM, DNB, the Government Pension Fund Norway, Guilé Foundation, Keva, KLP, MN Services NV, New Zealand Superannuation Fund, Newton Investment Management, Nordea, Northern Ireland Superannuation Fund, OPSEU Pension Trust, La Caixa Fondos de Pensiones, PGGM Investments, Santa Fe Portfolios, SNS AM, StatewideSuper, Syntrus AM, The Central Church Fund of Finland, The Church of England National Investing Bodies, Trillium AM, USS and Vancity Investment Management.



Principle 1: "Businesses should support and respect the protection of internationally proclaimed human rights"

At Telefónica we welcome the report of the Special Representative of the Secretary General of the United Nations on Human Rights because its implementation enables us to guarantee respect for Human Rights across all areas of the Company.

This is why in 2011 we worked in partnership with BSR The Business of a Better World, which has a proven track record in the development of Human Rights Programmes in the business world, to identify our needs from a global standpoint and to define a plan of action for development over the following year.

The nature of Telefónica's business means that its operations entail a growing number of human rights risks and opportunities. Our challenge is build a common framework throughout the Company, which will involve strengthening our global strategy and, more specifically, our sustainability goals.

Related GRI indicators

GRI	Indicator	2010	2011
S03	Percentage of employees trained in the organisation's anti-corruption policies and procedures	59.7%	48.4% ⁽¹⁾
PR8	Monetary value of fines for failure to comply with data protection regulations	3.832.652	3.851.000

⁽¹⁾ This estimate includes data for the fixed and mobile telecommunications businesses. The decline as a percentage of the total workforce is due to the consolidation of Vivo in Brazil.

Employment rights

Telefónica supports the elimination of all forms of forced, compulsory and child labour and upholds the freedom of association and the effective recognition of the right to collective bargaining.

Principle 2: “Businesses should make sure they are not complicit in human rights abuses”

The events in some countries in 2011 led the General Assembly of the United Nations (ONU) to declare internet access a Human Right, considering it to be (i) an indispensable tool for accelerating development and human progress, and (ii) a universal right that should be freely available to all people. In short, Internet access has become a facilitator of other human rights.

Accordingly, within the framework of our Social Innovation programme, we are promoting the development of initiatives aimed at reducing barriers to the use of ICTs by excluded groups, be they disability-related, economic, geographic, etc-. The different projects developed in 2011 include: the teleinterpretation platform (in Spain), the Compartel initiative (in Colombia), Conexión Amazónica (in Brazil), and Fono Ya and Intégrame (in Peru).

At Telefónica we are committed to applying these principles in our supply chain, as is demonstrated in the corresponding chapter of this report

Related GRI indicators:

GRI	Indicator	2010	2011
HR2	Total number of audits of high risk suppliers	1.163	1.773

Principle 3: "Businesses should uphold the freedom of association and the effective recognition of the right to collective bargaining"

At present there are several international treaties which enshrine the right to freedom of association (direct or indirect). These include the 1948 Universal Declaration of Human Rights and the International Labour Organization's Convention No. 87 concerning Freedom of Association and Protection of the Right to Organise. All these treaties recognise the content of Principle 3 of the Global Compact as one of the fundamental human rights of workers.

Telefónica is committed to guaranteeing that all workers – direct and indirect – have the option to freely and voluntarily establish and join organisations of their own choice, without fear of reprisals or intimidation, in accordance with national law in each of the countries where we operate. In 2011, Telefónica upheld and continued to pursue this commitment to all our professionals, regardless of the countries where they work, guaranteeing their association and employment rights based on our Business Principles and on the Social Protocol on International Agreements in effect with Union Network International (UNI).

In 2011, the employment conditions of 71% of our employees were covered by collective bargaining agreements. Telefónica respects its professionals' privacy rights in respect of their union membership choices, to which end it does not compile membership data. A total of 77,736 employees voted in Telefónica's last union elections (over 27% of the total workforce), underlining the dynamism of union activity at the Company. For more information, please go to the chapter on Freedom of Association.

Related GRI indicators:

GRI	Indicator	2010	2011
LA4	Percentage of employees covered by collective bargaining agreements.	74.9%	71.0%



Principle 4: “Businesses should support the elimination of all forms of forced or compulsory labour”

Telefónica guarantees that forced labour conditions do not exist in any of the Group's companies in any of the countries where we operate. Moreover, our commitment to this guarantee extends beyond our employees and throughout our value chain, where we do all in our power to ensure that our suppliers respect this fundamental right. Although the risk is greater in developing countries, these practices also exist in developing countries and given that the scope of our activities is global, we also fulfil our responsibility at a global level. Accordingly, we have very clear global policies on established working hours, workplace safety and employee remuneration.

The Workplace Satisfaction and Motivation Index in 2011 stood at 76%, two percentage points higher than in 2010. One of Telefónica's priorities as a company is to facilitate work-life balance for our employees and to this end the Company implemented various programmes and initiatives in 2011 including Tiempo para Vos (Time Out for You) in Argentina, Teleworking in Spain and Joined Up People in the UK.

Telefónica endeavours to apply this Principle to our supply chain, promoting improvements in the living and employment conditions of the people involved in our operations and ensuring that their Human Rights are not infringed.

Related GRI indicators:

GRI	Indicator	2010	2011
HR3	Total hours of employee training on policies and procedures concerning aspects of human rights that are relevant to operations, including the percentage of employees trained.	N.A.	84.171 ⁽¹⁾

(1) The figure is an estimate which takes the number of employees who completed the course in the year, with an average of one and a half hours applied for each course carried out.

Principle 5: “Businesses should support the effective abolition of child labour”

In 2011, on World Day against Child Labour, it was reported that some 115 million - 74 million boys and 41 million girls - of the world's 215 million child labourers were involved in work that jeopardises their safety, health and emotional and moral development. The efforts of the International Programme on the Eradication of Child Labour to ensure compliance with the principles of Convention 138 - concerning the minimum age for admission to employment- and Convention 182 - concerning the prohibition and elimination of the worst forms of child labour - of the ILO have resulted in progress being made towards the goal of the effective abolition of child labour by 2016. It is feared, however, that the global economic crisis may cause a slowdown in the pace of reduction, making the target difficult to achieve with fewer than five years remaining. Telefónica does tolerate, either directly or indirectly, any form of child labour in the work environment, in accordance with our Business Principles.

At the same time, we continue to strive externally on two fronts with the aim of contributing to the eradication of child labour in the countries where we operate. On the first, we are working in partnership with our suppliers to achieve sustainable management of our supply chain and to guarantee that child labour is not employed by any of our suppliers, as well as encouraging them to convey this idea to their respective value chains.

This problem is also tackled by the Telefónica Foundation, one of whose principal social aims is the eradication of child labour in Latin America via two specific programmes whose funding was renewed in 2011. access to education and knowledge and to improve the quality of education provision.

Related GRI indicators:

GRI	Indicator	2010	2011
HR6	Operations identified as having significant risk for incidents of child labour, and measures taken to contribute to their elimination.	Proniño Programme ⁽²⁾	Proniño Programme

(2) For more information on this programme see chapter 6.4: Social Projects.

Principle 6: “Businesses should uphold the elimination of discrimination in respect of employment and occupation”

According to the International Labour Organization (ILO), fundamental rights at work are gaining wider recognition among organisations, communities, and enterprises. These rights, which include the elimination of discrimination in respect of employment and occupation, establish benchmark criteria for responsible and sustainable enterprise level practices .

Accordingly, our Business Principles, which govern the conduct of all employees, specifically state that 'we promote equal opportunities and treat all people fairly and impartially, without discriminating on account of race, skin colour, citizenship, ethnic origin, creed, gender, sexual orientation, age, disability or family responsibilities'. Moreover, at Telefónica we view the diversity of our workforce as a genuine value driver. The differing origins, experiences and viewpoints of our human capital constitute a competitive advantage and one of the cornerstones of our success.

The work initiated in 2010 under the umbrella of the global diversity programme (unveiled in 4Q10 by the Business Principles Office) continued in 2011. The project, designed to integrate diversity protocols and sensitivity into all areas of the company, entailed a pilot test at Telefónica Europe last year, the results of which were so satisfactory that the initiative will be rolled out to the other regions in 2012.

Related GRI indicators:

GRI	Indicator	2010	2011
HR4	Total number of incidents of discrimination and actions taken	0	0
LA13	Female executives	16.8%	19,1%
LA13	Employees with some form of disability	1.610	1.568
LA14	Ratio of basic salary and remuneration of women to men	N.A.	95,2% ⁽¹⁾

(1) Spain figure for middle managers.

Principle 7: “Businesses should support a precautionary approach to environmental challenges”

The environmental strategy pursued by Telefónica is part of an integrated Company-wide sustainability policy signed and supported by the Company's senior management. At Telefónica we are fully aware of the huge global challenge posed by Climate Change, which entails both risks and business opportunities in the telecommunications sector. In order to rise to this challenge, we have established a Climate Change and Energy Efficiency Office. This office, represented by corporate and business units, is responsible for the management, control and promotion of all the Company's projects related to energy, climate change and green services. All these endeavours are being pursued with an overriding objective: to reduce our internal emissions via energy efficiency initiatives and to provide products and services that help to reduce greenhouse gas emissions (GGE) by our customers and in strategic sectors of the economy.

In 2011, we were involved in more than 30 global network efficiency projects, resulting in a €7.6 million reduction in our expenditure on energy. Also noteworthy during the year were the free cooling global network efficiency projects (free cooling makes use of outside air to control the temperature in mobile base stations and fixed-telephone exchanges) in Uruguay, Nicaragua, Spain, Argentina and Brazil, with more than 100 initiatives carried out. It is worth noting that Telefónica has now achieved 20% of the network energy consumption reduction goal announced in 2008 for 2015, which translates into a 20% cost saving. For more information please read the Environment chapter of this report.

Related GRI indicators:

GRI	Indicator	2010	2011
AM18	Initiatives to reduce greenhouse gas emissions. (% energy cost saving).	15%	20%

Principle 8: “Businesses should undertake initiatives to promote greater environmental responsibility”

The potential environmental risks associated with our activity at Telefónica are concentrated in network deployment. During operations we must manage network waste and energy consumption, reduce paper and water use and control carbon emissions. We must also manage the useful life of the network and to this end efforts are being made to manage waste, improve energy efficiency and control the visual, environmental and acoustic impact of our installations.



EN01, EN03, EN04, EN08, EN16, EN22, EN23, EN27, EN29, EN30

Consumption of Resources		2009	2010	2011	% Chg
Total consumption of plain paper (including bills)	Tonnes	16,941	14,720	13,171	-10.5
Total consumption of recycled paper	Tonnes	637	523	492	-5.9
Number of customers with e-billing	Thousands	12,597	10,338	29,618	186.5
Water consumption	Cubic metres	4,436,869	4,004,086	3,927,601	-1.9
Waste					
E-waste from devices (Operations)	Tonnes	1,571	2,048	2,180	6.5
E-waste from devices (Customers)	Tonnes	1,895	1,644	1,702	3.5
E-waste from electrical and electronic equipment sent for recycling	Tonnes	3,462	4,056	3,998	-1.4
Energy ⁽¹⁾					
Total fuel consumption ⁽²⁾	Thousands of litres	39,441	45,371	39,555	-12.8
Natural gas consumption: operations & offices	Nm3	6,637,096	6,623,162	5,413,698	-18.3
Total energy consumption ⁽³⁾	MWh	5,828,832	5,853,842	5,987,248	2.3
Renewable energy generated and purchased	MWh	493,678	674,772	740,596	9.8
GHG emissions ⁽¹⁾					
Direct emissions (Scope 1)	tCO2eq	114.604	125.511	110,878	-11.7
Indirect emissions (Scope 2)	tCO2eq	1,564,194	1,604,103	1,612,373	0.5

⁽¹⁾ Data on 2010 energy and emissions verified in 2011. Data on 2011 energy and emissions being verified.
⁽²⁾ Total consumption of gasoline, diesel, ethanol and biodiesel from operations, offices and fleets.
⁽³⁾ Includes consumption from operations and offices.



At Telefónica we view our diverse workforce as a genuine value driver. The differing origins and experiences of our human capital constitute a competitive advantage

Principle 9: “Businesses should encourage the development and diffusion of environmentally friendly technologies”

At Telefónica we recognise that we can contribute to global efforts to mitigate and adapt to climate change and to the implementation of joint initiatives aimed at reducing greenhouse gas emissions (GGE).

To this end we are involved in several sector and cross-sector groups which seek to put green ICTS on the climate change policy agenda and to foster environmental sustainability at the global level. These are: International Telecommunication Union Study Group 5, which is responsible for studying ICT environmental aspects of electromagnetic phenomena and climate change; the Climate Change Group of the Global-E-Sustainability Initiative (GESI), which is at the forefront of work to harness the ICT sector's potential to reduce worldwide carbon emissions; Working Group 2 of the ICT4EE (ICT for Energy Efficiency) Forum, which seeks to enable energy efficiency in other sectors; the Green Power for Mobile Working Group and Energy Efficiency Initiative of the GSMA Association, which seeks to 'extend mobile beyond the grid' through the promotion of renewable energy technologies and energy efficient base stations; the Sustainability and Energy Working Groups of the European Telecommunications Network Operators' Association (ETNO), which are striving to put telecommunications operators and ICT companies at the forefront of efforts to address environmental issues; and the Energy and Climate Change Working Group of the European Roundtable of Industrials (ERT), which is promoting a holistic approach to address the significant challenges posed by climate change.

Principle 10: “Businesses should work against corruption in all its forms, including extortion and bribery”

At Telefónica we are aware of the high cost of corruption. In economic terms, costs increase through the value chain and investment ins discouraged, while on the legal front corruption takes a toll in the form of legal penalties and fines and erodes stakeholder trust. Furthermore, reputational damage can be even more costly than the financial penalties imposed. We are also aware of the medium-long term opportunities that companies with an effective anti-corruption strategy will enjoy. At Telefónica we remain committed, with integrity and transparency via our Business Principles, to a code of ethics that inspires and defines how we do business and our relationship with all stakeholders. More information can be found on the work of our Business Principles, BP training, confidential employee helplines, anti-corruption audits and progress made in the implementation of our code of ethics at new subsidiaries in the Code of Conduct chapter.

Related GRI indicators:

GRI	Indicator	2010	2011
SO4	Measures adopted and incidents of corruption (dismissals)	7	5

Related GRI indicators:

GRI	Indicator	2010	2011
EN6	Initiatives to provide energy-efficient or renewable energy based products and services, and reductions in energy requirements as a result of these initiatives (thousands of euros invested in social and environmental action -LBG-).	640.4	356.9

Telefónica indicators



At Telefónica we have established a set of key environmental management indicators. These are based on material aspects and have been monitored for several years for the purpose of comparison and to measure the company's performance over a long period of time.

Economic dimension		2009	2010	2011	% Chg
Telefónica's Revenue	€ Million	56,731	60,737	62,837	3.5
Technological innovation	€ Million	4,291	4,814	5,091	5.8
Tax contributions ⁽¹⁾	€ Million	11,744	12,894	13,768	6.8
Total salary expenses	€ Million	6,775	8,409	11,080	31.8
Investment in infrastructure ⁽¹⁾	€ Million	7,064	10,844	10,224	-5.7
Volume of purchases awarded	€ Million	23,048	26,828	27,295	1.7
Investment in I+D	€ Million	693	797	983	23.3
Total for local suppliers	%	79.3	87.5	90.2	3.1
Number of employees dismissed for failure to comply with Business Principles	Employees	8	7	5	-28.6
Number of corruption incidents investigated by the Business Principles Office	Incidents	13	5	2	-60.0
Employees trained in Business Principles	%	57.0	59.7	48.4	-19.0
Number of audits performed on at-risk suppliers	Audits	840	1,163	1,773	52.5
Social dimension		2009	2010	2011	% Chg
Total workforce	–	257,426	285,106	291,027	2.1
Permanent staff	–	213,525	231,124	238,783	3.3
Absentee rate ⁽²⁾	Days	6,046	5,56	4,436	-20.2
Thousands of hours of training	–	11,218	13,052	17,438	33.6
Women in workforce	%	50.1%	51.5%	53.9%	4.6
Female executives	%	15.6%	16.8%	19.1	13.7
Number of persons with disabilities	–	1,42	1,61	1,568	-2.6
Total social investment (LBG)	Thousands of euros	108,471	131,959	143,259	8.6
Hours of volunteer work	–	126,122	109,796	112,943	2.9

Environmental dimension		2009	2010	2011	%Chg
Consumption of Resources					
Total consumption of new paper (including bills)	Tonnes	16,941	14,72	13,171	-10.5
Total consumption of recycled paper	Tonnes	637	523	492	-5.9
Customers with e-billing	Thousands	12,597	10,338	29,618	186.5
Water consumption	Cubic metres	4,436,869	4,004,086	3,927,601	-1.9
Waste					
E-waste from devices (operations)	Tonnes	1,571	2,048	2,18	6.5
E-waste from devices (customers)	Tonnes	1,895	1,644	1,702	3.5
E-waste from devices that is sent to be recycled	Tonnes	3,462	4,056	3,998	-1.4
Energy ⁽⁵⁾					
Total fuel consumption ⁽³⁾	Thousands of litres	39,441	45,371	39,555	-12.8
Natural gas consumption: operations & offices	Nm3	6,637,096	6,623,162	5,413,698	-18.3
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Renewable energy generated and purchased	MWh	493,678	674,772	740,596	9.8
Greenhouse gas emissions ⁽⁵⁾					
Direct emissions (Scope 1)	tCO2eq	114,604	125,511	110,878	-11.7
Indirect emissions (Scope 2)	tCO2eq	1,564,194	1,604,103	1,612,373	0.5

1. This figure differs from that given in the Driver of Progress section; here it is expressed according to the accrual criterion and not according to the cash criterion.
2. Absentee rate (AR) AR = (total num. of days missed, for disabilities, during the period / total number of days worked by the workforce during the same period) x 200,000.
3. Total consumption of gasoline, diesel, ethanol and biodiesel from operations, offices and fleets.
4. Includes consumption from operations and offices.
5. Data on 2010 energy and emissions, verified in 2011. Data on 2011 energy and emissions, being verified.

Recognition
of excellence



Telefónica garnered a host of international accolades in 2011 for its unwavering commitment to sustainability management.

Highlights of which are as follows:

- Global**
One of the **sustainability leaders** included in the Dow Jones Sustainability Index 2011.

Sector leader in the **Carbon Disclosure Project (CDP)**.

Top-ranked European operator in energy efficiency solutions in Verdantix's **Green Quadrant** report.

Highest-ranked European operator in Fortune's **"The 2011 World's Most Admired Companies"** list.
- In Germany**
Gold version of the **"Holistic Occupational Health Management System"** (GABEGS) certificate awarded by the government of Bavaria.
- In Argentina**
Special tribute for the **Communication of Progress 2011** of the Argentinian Network of the United Nations Global Compact.

Best-managed telecoms company in Latin America, according to Euromoney.
- In Chile**
Best Company for Working Mothers and Fathers, according to Fundación Chile Unido and Revista Ya, a supplement published with the Chilean daily El Mercurio.
- In Colombia**
ANDESCO award for corporate social responsibility.
- In Ecuador**
Second position in the **Best Place To Work** ranking

Best Practice in **Social and Labour Market Integration of People with Disabilities**, from the Vice-President of the Republic of Ecuador.

Best practices in CSR, awarded by the Province of Pichincha.

- In Spain**
Award for transparency of information in **Annual Reports**, from the business weekly El Nuevo Lunes.

The interactive RETADIS project, awarded the 2011 prize for **"Best initiative for spreading access to and fostering appropriate use of the internet."**

National Award for IT and Health from the Spanish Society for Healthcare Computing.
- In Mexico**
The **"Ethics and Values in Industry"** award in the Best Practices in Social Responsibility category, from the Confederation of Industrial Chambers of Mexico (CONCAMIN) and the Mexican Foundation for Innovation and Technology (FUNTEC).

The Socially Responsible Business seal from the Mexican Philanthropy Centre (Cemefi) .
- In Nicaragua**
First position in the **Best Place to Work** ranking.
- In Panama**
Second in the ranking of the best companies to work for in Latin America and the top operator, according to the Great Place to Work® Institute..
- In Peru**
Prize for Business Eco-efficiency from the Ministry of the Environment.
- In the UK**
O2 became the first mobile network operator to be awarded **Carbon Trust Standard** certificate
- In Uruguay**
First position in the **Best Place to Work** ranking.
- In Venezuela**
First position in the **Best Place to Work** ranking.
- In El Salvador**
Atento occupied second position in the **Best Place To Work** ranking.



GRI Indicators



STANDARD DISCLOSURES PART I: Profile Disclosures

1. Strategy and Analysis

Profile disclosure	Description	Reported 2010	Reported 2011	Location	Explanation for omission
1,1	Statement from the most senior decision-maker of the organization.	√	√	Letter from the Executive Chairman	
1,2	Description of key impacts, risks, and opportunities.	√	√	3. Sustainability at Telefónica	

2. Organizational Profile

Profile disclosure	Description	Reported 2010	Reported 2011	Location	Explanation for omission
2,1	Name of the organization.	√	√	1.1. Principles for the 2011 Sustainability Report	
2,2	Primary brands, products, and/or services.	√	√	1.1. Principles for the 2011 Sustainability Report	
2,3	Operational structure of the organization, including main divisions, operating companies, subsidiaries, and joint ventures.	√	√	Annual Report	
2,4	Location of organization's headquarters.	√	√	1.1. Principles for the 2011 Sustainability Report	
2,5	Number of countries where the organization operates, and names of countries with either major operations or that are specifically relevant to the sustainability issues covered in the report.	√	√	1.1. Principles for the 2011 Sustainability Report	
2,6	Nature of ownership and legal form.	√	√	Corporate Governance Report	
2,7	Markets served (including geographic breakdown, sectors served, and types of customers/beneficiaries).	√	√	Annual Report	
2,8	Scale of the reporting organization.	√	√	Annual Report	
2,9	Significant changes during the reporting period regarding size, structure, or ownership.	√	√	1.2. Report boundary	
2,10	Awards received in the reporting period.	√	√	10. Recognition of excellence	

3. Report Parameters

Profile disclosure	Description	Reported 2010	Reported 2011	Location	Explanation for omission
3,1	Reporting period (e.g., fiscal/calendar year) f or information provided.	√	√	1.2. Report boundary	
3,2	Date of most recent previous report (if any).	√	√	1.2. Report boundary	
3,3	Reporting cycle (annual, biennial, etc.)	√	√	1.2. Report boundary	
3,4	Contact point for questions regarding the report or its contents.	√	√	1.2. Report boundary	
3,5	Process for defining report content.	√	√	1.2. Report boundary	
3,6	Boundary of the report (e.g., countries, divisions, subsidiaries, leased facilities, joint ventures, suppliers). See GRI Boundary Protocol for further guidance.	√	√	1.2. Report boundary	
3,7	State any specific limitations on the scope or boundary of the report (see completeness principle for explanation of scope).	√	√	1.2. Report boundary	
3,8	Basis for reporting on joint ventures, subsidiaries, leased facilities, outsourced operations, and other entities that can significantly affect comparability from period to period and/or between organizations.	√	√	1.2. Report boundary	
3,9	Data measurement techniques and the bases of calculations, including assumptions and techniques underlying estimations applied to the compilation of the Indicators and other information in the report. Explain any decisions not to apply, or to substantially diverge from, the GRI Indicator Protocols.	√	√	1.2. Report boundary	
3,10	Explanation of the effect of any re-statements of information provided in earlier reports, and the reasons for such re-statement (e.g., mergers/acquisitions, change of base years/periods, nature of business, measurement methods).	√	√	1.2. Report boundary	
3,11	Significant changes from previous reporting periods in the scope, boundary, or measurement methods applied in the report.	√	√	1.2. Report boundary	
3,12	Table identifying the location of the Standard Disclosures in the report.	√	√	11. GRI tables	
3,13	Policy and current practice with regard to seeking external assurance for the report.	√	√	11. GRI tables	

4. Gobierno, compromisos y participación de los grupos de interés

Profile disclosure	Description	Reported 2010	Reported 2011	Location	Explanation for omission
4,1	Governance structure of the organization, including committees under the highest governance body responsible for specific tasks, such as setting strategy or organizational oversight.	√	√	Annual Corporate Governance Report	
4,2	Indicate whether the Chair of the highest governance body is also an executive officer.	√	√	Annual Corporate Governance Report	
4,3	For organizations that have a unitary board structure, state the number and gender of members of the highest governance body that are independent and/or non-executive members.	√	√	Annual Corporate Governance Report	
4,4	Mechanisms for shareholders and employees to provide recommendations or direction to the highest governance body.	√	√	5.6. Stakeholder Engagement	
4,5	Linkage between compensation for members of the highest governance body, senior managers, and executives (including departure arrangements), and the organization's performance (including social and environmental performance).	√	√	Annual Corporate Governance Report	
4,6	Processes in place for the highest governance body to ensure conflicts of interest are avoided.	√	√	Annual Corporate Governance Report	
4,7	Process for determining the composition, qualifications, and expertise of the members of the highest governance body and its committees, including any consideration of gender and other indicators of diversity.	√	√	Annual Corporate Governance Report	
4,8	Internally developed statements of mission or values, codes of conduct, and principles relevant to economic, environmental, and social performance and the status of their implementation.	√	√	Annual Report	
4,9	Procedures of the highest governance body for overseeing the organization's identification and management of economic, environmental, and social performance, including relevant risks and opportunities, and adherence or compliance with internationally agreed standards, codes of conduct, and principles.	√	√	3. Annual Corporate Governance Report	
4,10	Processes for evaluating the highest governance body's own performance, particularly with respect to economic, environmental, and social performance.	√	√	Annual Corporate Governance Report	
4,11	Explanation of whether and how the precautionary approach or principle is addressed by the organization.	√	√	4.3. Code of Conduct	
4,12	Externally developed economic, environmental, and social charters, principles, or other initiatives to which the organization subscribes or endorses.	√	√	4.2. Risk management	
4,13	Memberships in associations (such as industry associations) and/or national/international advocacy organizations in which the organization: * Has positions in governance bodies; * Participates in projects or committees; * Provides substantive funding beyond routine membership dues; or * Views membership as strategic.	√	√	Throughout the report	
4,14	List of stakeholder groups engaged by the organization.	√	√	2.1. Matrix of stakeholders and stakeholder engagement process	
4,15	Basis for identification and selection of stakeholders with whom to engage.	√	√	2.1. Matrix of stakeholders and stakeholder engagement process	
4,16	Approaches to stakeholder engagement, including frequency of engagement by type and by stakeholder group.	√	√	2.1. Matrix of stakeholders and stakeholder engagement process	
4,17	Key topics and concerns that have been raised through stakeholder engagement, and how the organization has responded to those key topics and concerns, including through its reporting.	√	√	2.2. Materiality Analysis	

STANDARD DISCLOSURES PART II: Disclosures on Management Approach (DMAs)

G3 DMA	Description	Reported 2010	Reported 2011	Location	Explanation for omission
DMA EC	Disclosure on Management Approach ECONOMY	√	√	4.1. Driver of progress	
DMA EN	Disclosure on Management Approach ENVIRONMENTAL	√	√	5. Environmental impact	
DMA LA	Disclosure on Management Approach LABOUR	√	√	6.1. Our professionals	
DMA HR	Disclosure on Management Approach HUMAN RIGHTS	√	√	4.3. Code of Conduct	
DMA SO	Disclosure on Management Approach SOCIETY	√	√	6.4. Social projects	
DMA PR	Disclosure on Management Approach CUSTOMERS	√	√	4.4. Management of sustainable relationships with our costumers	

STANDARD DISCLOSURES PART III: Performance Indicators

Economic

Profile disclosure	Description	Reported 2010	Reported 2011	Location	Explanation for omission
Economic performance					
EC1	Direct economic value generated and distributed, including revenues, operating costs, employee compensation, donations and other community investments, retained earnings, and payments to capital providers and governments.	√	√	4.1. Driver of progress	
EC2	Financial implications and other risks and opportunities for the organization's activities due to climate change.	√	√	5.2. Environmental Management at Telefónica	
EC3	Coverage of the organization's defined benefit plan obligations.	√	√	6.1. Our professionals	
EC4	Significant financial assistance received from government.	√	√	4.3. Code of Conduct	
Market presence					
EC5	Range of ratios of standard entry level wage by gender compared to local minimum wage at significant locations of operation.	No	√	6.1. Employees	
EC6	Policy, practices, and proportion of spending on locally-based suppliers at significant locations of operation.	√	√	4.1. Driver of progress	
EC7	Procedures for local hiring and proportion of senior management hired from the local community at significant locations of operation.	No	√	6.1. Employees	
Indirect economic impacts					
EC8	Development and impact of infrastructure investments and services provided primarily for public benefit through commercial, in-kind, or pro bono engagement.	√	√	4.7. Innovation at Telefónica	
EC9	Understanding and describing significant indirect economic impacts, including the extent of impacts.	√	√	4.1. Driver of progress	

Environmental					
Profile disclosure	Description	Reported 2010	Reported 2011	Location	Explanation for omission
Materials					
EN1	Materials used by weight or volume.	√	√	5. Environmental impact	
EN2	Percentage of materials used that are recycled input materials.	√	√	Environmental impact	
Energy					
EN3	Direct energy consumption by primary energy source.	√	√	5.Environmental impact	
EN4	Indirect energy consumption by primary source.	√	√	5. Environmental impact	
EN5	Energy saved due to conservation and efficiency improvements.	√	√	5. Environmental impact	
EN6	Initiatives to provide energy-efficient or renewable energy based products and services, and reductions in energy requirements as a result of these initiatives.	√	√	5. Environmental impact	
EN7	Initiatives to reduce indirect energy consumption and reductions achieved.	√	√	5. Environmental impact	
Water					
EN8	Total water withdrawal by source.	√	√	5. Environmental impact	
EN9	Water sources significantly affected by withdrawal of water.	No	No		This indicator does not apply to all of the company's business activities
EN10	Percentage and total volume of water recycled and reused.	No	No		This indicator does not apply to all of the company's business activities
Biodiversity					
EN11	Location and size of land owned, leased, managed in, or adjacent to, protected areas and areas of high biodiversity value outside protected areas.	No	No		This indicator does not apply to all of the company's business activities
EN12	Description of significant impacts of activities, products, and services on biodiversity in protected areas and areas of high biodiversity value outside protected areas.	√	√	5. Environmental impact	
EN13	Habitats protected or restored.	No	No		This indicator does not apply to all of the company's business activities
EN14	Strategies, current actions, and future plans for managing impacts on biodiversity.	√	√	5. Environmental impact	
EN15	Number of IUCN Red List species and national conservation list species with habitats in areas affected by operations, by level of extinction risk.	No	No		This indicator does not apply to all of the company's business activities

Profile disclosure	Description	Reported 2010	Reported 2011	Location	Explanation for omission
Emissions, effluents and waste					
EN16	Total direct and indirect greenhouse gas emissions by weight.	√	√	5. Environmental impact	
EN17	Other relevant indirect greenhouse gas emissions by weight.	√	√	5. Environmental impact	
EN18	Initiatives to reduce greenhouse gas emissions and reductions achieved.	√	√	5. Environmental impact	
EN19	Emissions of ozone-depleting substances by weight.	√	√	5. Environmental impact	
EN20	NOx, SOx, and other significant air emissions by type and weight.	√	√	5. Environmental impact	
EN21	Total water discharge by quality and destination.	√	√	5. Environmental impact	
EN22	Total weight of waste by type and disposal method.	√	√	5. Environmental impact	
EN23	Total number and volume of significant spills.	√	√	5. Environmental impact	
EN24	Weight of transported, imported, exported, or treated waste deemed hazardous under the terms of the Basel Convention Annex I, II, III, and VIII, and percentage of transported waste shipped internationally.	√	√	5. Environmental impact	
EN25	Identity, size, protected status, and biodiversity value of water bodies and related habitats significantly affected by the reporting organization's discharges of water and runoff.	No	No	5. Environmental impact	This indicator does not apply to all of the company's business activities
Products and services					
EN26	Initiatives to mitigate environmental impacts of products and services, and extent of impact mitigation.	√	√	5. Environmental impact	
EN27	Percentage of products sold and their packaging materials that are reclaimed by category.	√	√	5. Environmental impact	
Compliance					
EN28	Monetary value of significant fines and total number of non-monetary sanctions for non-compliance with environmental laws and regulations.	√	√	5. Environmental impact	
Transport					
EN29	Significant environmental impacts of transporting products and other goods and materials used for the organization's operations, and transporting members of the workforce.	√	√	5. Environmental impact	
Overall					
EN30	Total environmental protection expenditures and investments by type.	√	√	5. Environmental impact	

Social: Labor Practices and Decent Work

Profile disclosure	Description	Reported 2010	Reported 2011	Location	Explanation for omission
Employment					
LA1	Total workforce by employment type, employment contract, and region, broken down by gender.	√	√	6.1. Employees	
LA2	Total number and rate of new employee hires and employee turnover by age group, gender, and region.	√	√	6.1. Employees	
LA3	Benefits provided to full-time employees that are not provided to temporary or part-time employees, by major operations.	√	√	6.1. Employees	
LA15	Return to work and retention rates after parental leave, by gender.	No	No		Not available
Labor/management relations					
LA4	Percentage of employees covered by collective bargaining agreements.	√	√	6.1. Employees	
LA5	Minimum notice period(s) regarding significant operational changes, including whether it is specified in collective agreements.	√	√	6.1. Employees	
Occupational health and safety					
LA6	Percentage of total workforce represented in formal joint management-worker health and safety committees that help monitor and advise on occupational health and safety programs.	√	√	6.1. Employees	
LA7	Rates of injury, occupational diseases, lost days, and absenteeism, and number of work-related fatalities by region and by gender.	√	√	6.1. Employees	
LA8	Education, training, counseling, prevention, and risk-control programs in place to assist workforce members, their families, or community members regarding serious diseases.	√	√	6.1. Employees	
LA9	Health and safety topics covered in formal agreements with trade unions.	√	√	6.1. Employees	
Training and education					
LA10	Average hours of training per year per employee by gender, and by employee category.	√	√	6.1. Employees	
LA11	Programs for skills management and lifelong learning that support the continued employability of employees and assist them in managing career endings.	√	√	6.1. Employees	
LA12	Percentage of employees receiving regular performance and career development reviews, by gender.	No	√	6.1. Employees	
Diversity and equal opportunity					
LA13	Composition of governance bodies and breakdown of employees per employee category according to gender, age group, minority group membership, and other indicators of diversity.	√	√	6.1. Employees	
Equal remuneration for women and men					
LA14	Ratio of basic salary and remuneration of women to men by employee category, by significant locations of operation.	No	√	6.1. Employees	

Social: Human Rights

Profile disclosure	Description	Reported 2010	Reported 2011	Location	Explanation for omission
Investment and procurement practices					
HR1	Percentage and total number of significant investment agreements and contracts that include clauses incorporating human rights concerns, or that have undergone human rights screening.	√	√	4.8. Responsibility in the supply chain	
HR2	Percentage of significant suppliers, contractors and other business partners that have undergone human rights screening, and actions taken.	√	√	4.8. Responsibility in the supply chain	
HR3	Total hours of employee training on policies and procedures concerning aspects of human rights that are relevant to operations, including the percentage of employees trained.	√	√	4.3. Code of Conduct	
Non-discrimination					
HR4	Total number of incidents of discrimination and corrective actions taken.	√	√	4.3. Code of Conduct	
Freedom of association and collective bargaining					
HR5	Operations and significant suppliers identified in which the right to exercise freedom of association and collective bargaining may be violated or at significant risk, and actions taken to support these rights.	√	√	4.8. Responsibility in the supply chain	
Child labor					
HR6	Operations and significant suppliers identified as having significant risk for incidents of child labor, and measures taken to contribute to the effective abolition of child labor.	√	√	4.8. Responsibility in the supply chain	
Forced and compulsory labor					
HR7	Operations and significant suppliers identified as having significant risk for incidents of forced or compulsory labor, and measures to contribute to the elimination of all forms of forced or compulsory labor.	√	√	4.8. Responsibility in the supply chain	
Security practices					
HR8	Percentage of security personnel trained in the organization's policies or procedures concerning aspects of human rights that are relevant to operations.	√	√	4.3. Code of Conduct	
Indigenous rights					
HR9	Total number of incidents of violations involving rights of indigenous people and actions taken.	√	√	4.3. Code of Conduct	
Assessment					
HR10	Percentage and total number of operations that have been subject to human rights reviews and/or impact assessments.	No			
Remediation					
HR11	"Number of grievances related to human rights filed, addressed and resolved through formal grievance mechanisms."	No			

Social: Sociedad

Profile disclosure	Description	Reported 2010	Reported 2011	Location	Explanation for omission
Local communities					
S01	Percentage of operations with implemented local community engagement, impact assessments, and development programs.	No			
S09	Operations with significant potential or actual negative impacts on local communities.	No			
S010	Prevention and mitigation measures implemented in operations with significant potential or actual negative impacts on local communities.	No			
Corruption					
S02	Percentage and total number of business units analyzed for risks related to corruption.	√	√	4.3. Code of Conduct	
S03	Percentage of employees trained in organization's anti-corruption policies and procedures.	√	√	4.3. Code of Conduct	
S04	Actions taken in response to incidents of corruption.		√	4.3. Code of Conduct	
Public policy					
S05	Public policy positions and participation in public policy development and lobbying.	√	√	4.3. Code of Conduct	
S06	Total value of financial and in-kind contributions to political parties, politicians, and related institutions by country.	√	√	4.3. Code of Conduct	
Anti-competitive behavior					
S07	Total number of legal actions for anti-competitive behavior, anti-trust, and monopoly practices and their outcomes.	√	√	6.6.3. Relations with the regulator: regulation and competition	
Compliance					
S08	Monetary value of significant fines and total number of non-monetary sanctions for non-compliance with laws and regulations.	√	√	6.6.3. Relations with the regulator: regulation and competition	

Social: Product Responsibility

Profile disclosure	Description	Reported 2010	Reported 2011	Location	Explanation for omission
Customer health and safety					
PR1	Life cycle stages in which health and safety impacts of products and services are assessed for improvement, and percentage of significant products and services categories subject to such procedures.	√	√	4.7. Innovation atTelefónica	
PR2	Total number of incidents of non-compliance with regulations and voluntary codes concerning health and safety impacts of products and services during their life cycle, by type of outcomes.	√	√	6.6.3. Relations with the regulator: regulation and competition	
Product and service labelling					
PR3	Type of product and service information required by procedures, and percentage of significant products and services subject to such information requirements.	√	√	4.4. Management of sustainable relationships with our costumers	
PR4	Total number of incidents of non-compliance with regulations and voluntary codes concerning product and service information and labeling, by type of outcomes.	√	√	4.4. Management of sustainable relationships with our costumers	
PR5	Practices related to customer satisfaction, including results of surveys measuring customer satisfaction.	√	√	4.4. Management of sustainable relationships with our costumers	
Marketing communications					
PR6	Programs for adherence to laws, standards, and voluntary codes related to marketing communications, including advertising, promotion, and sponsorship.	√	√	4.5. Privacy and data protection	
PR7	Total number of incidents of non-compliance with regulations and voluntary codes concerning marketing communications, including advertising, promotion, and sponsorship by type of outcomes.	√	√	4.5. Privacy and data protection	
Customer privacy					
PR8	Total number of substantiated complaints regarding breaches of customer privacy and losses of customer data.	√	√	4.5. Privacy and data protection	
Compliance					
PR9	Monetary value of significant fines for non-compliance with laws and regulations concerning the provision and use of products and services.	√	√	6.6.3. Relations with the regulator: regulation and competition	

Telecommunications sector supplement

Profile disclosure	Description	Reported 2010	Reported 2011	Location	Explanation for omission
Internal operations					
IO01	Capital investment in telecommunication network infrastructure broken down by country/region.	√	√	4.7. Innovation	
IO02	Net costs for service providers under the Universal Service Obligation.	√	√	6.2. Digital inclusion	
IO03	Practices to ensure health and safety of field personnel involved in the installation, operation and maintenance of masts, base stations, laying cables and other outside plant.	√	√	6.1. Employees	
IO04	Compliance with ICNIRP (International Commission on Non-Ionising Radiation Protection) standards on exposure to radiofrequency (RF) emissions from handsets.	√	√	5. Environmental impact	
Providing access					
IO05	Compliance with ICNIRP (International Commission on Non-Ionising Radiation Protection) guidelines on exposure to radiofrequency (RF) emissions from base stations.	√	√	5. Environmental impact	
Technology Applications					
IO06	Policies and practices with respect to Specific Absorption Rate (SAR) of handsets.	√	√	5. Environmental impact	
IO07	Policies and practices on the siting of masts.	√	√	5. Environmental impact	
IO08	Number and types of telecommunication products and services provided to and used by low and no income sectors of the population.	√	√	5. Environmental impact	
PA5	Programmes to provide and maintain telecommunication products and services in emergency situations and for disaster relief.	√	√	6.2. Digital inclusion	
PA6	Polices and practices to manage human rights issues relating to access and use of telecommunications products and services.	√	√	6.3. Responsiveness to emergency situations	
PA7	Polices and practices to manage human rights issues relating to access and use of telecommunications products and services.	√	√	6.2. Digital inclusion	

Profile disclosure	Description	Reported 2010	Reported 2011	Location	Explanation for omission
PA8	Policies and practices to publicly communicate on EMF related issues.	√	√	5. Environmental impact	
PA9	Total amount invested in programmes and activities in electromagnetic field research.	√	√	5. Environmental impact	
PA10	Initiatives to ensure clarity of charges and tariffs.	√	√	4.4. Customer relationship management	
PA11	Initiatives to inform customers about product features and applications that will promote responsible, efficient, cost effective, and environmentally preferable use.	√	√	6.5. Impact of telecommunications services	
Technology applications					
TA1	Provide examples of the resource efficiency of telecommunication products and services delivered.	√	√	6.5. Impact of telecommunications services	
TA2	Provide examples of telecommunication products, services and applications that have the potential to replace physical objects.	√	√	6.5. Impact of telecommunications services	
TA3	Disclose any measures of transport and/or resource changes of customer use of the telecommunication products and services listed above	No	√	6.5. Impact of telecommunications services	
TA4	IDisclose any estimates of the rebound effect (indirect consequences) of customer use of telecommunication products and services.	No	√	5. Environmental impact	
TA5	Description of practices relating to intellectual property rights and open source technologies.	No	√	4.7. Innovation	

Assurance and verification



LBG Assurance Statement – Telefónica

Corporate Citizenship has been asked to provide assurance on Telefónica's application of the LBG measurement model for the year to 31st December 2011.

The LBG model provides a robust and credible framework which measures the real value and impact of corporate community investment to both business and society. It moves beyond charitable donations to include the full range of contributions (in employee time, in-kind, and in cash) made to community causes.

Our work has been limited to assuring the correct application of the LBG model. This is the fifth year that Telefónica has used the LBG model and it continues to be an active member of the LBG España group.

We noted that Telefónica has continued to make progress with the way in which it applies the LBG model. The assurance showed the model being intelligently and being thoroughly applied. The staff we engaged with understand the model fully and apply it correctly. No material error was found in the figures presented to us.

In our opinion, Telefónica continues to show that it understands the LBG model and that it applies its principles to the measurement of community activities at home and abroad. Below we identify some further improvement that can be made as the company develops its application of the model in the future.

Commentary

In applying the LBG model companies initially have to master, understand and apply the principles of LBG. Doing so enables them to develop a complete and accurate map of their contributions, paying due regard all the resources invested. Telefónica has achieved this.

The challenge going forward is to apply this knowledge strategically to Telefónica's programme to increase both efficiency in use of resources and the overall benefit to the community. Also the LBG model can help ensure that the community support appropriately reflects the nature of Telefónica's businesses, their innovation their interests and their responsibilities.

Corporate Citizenship

Corporate Citizenship
www.corporate-citizenship.com
April 2012

MAS Business facilitates LBG España and has supported the assurance process and preparation of this assurance statement.



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INDEPENDENT REVIEW OF THE TELEFÓNICA GROUP'S 2011 ANNUAL CORPORATE SUSTAINABILITY REPORT

To the Human Resources and Corporate Reputation
Committee of Telefónica, S.A.:

Scope of the work

We have carried out the review of the content of the 2011 Annual Corporate Sustainability Report of Telefónica Group (hereinafter Telefónica), which has been prepared based on:

- The Global Reporting Initiative (GRI) Preparation Guide (version 3.1).
- The principles stated in the AA1000 APS 2008 guide issued by AccountAbility (Institute of Social and Ethical AccountAbility).

The scope determined by Telefónica for the preparation of this report is defined in "Consolidation Perimeter" section in the accompanying Report.

The preparation of the accompanying 2011 Annual Corporate Sustainability Report, as well as the information contained therein, is the responsibility of the administrative bodies and management of Telefónica, S.A. They are also responsible for defining, adapting, and maintaining the management systems and internal controls from which the information is obtained. Our responsibility is to issue an independent report based on the procedures applied in our review.

Criteria

Our review was carried out based on:

- Standard ISAE 3000, Assurance Engagements Other than Audits or Reviews of Historical Financial Information issued by the International Auditing and Assurance Standard Board (IAASB) of the International Federation of Accountants (IFAC), with a limited scope of assurance.
- AA1000 AccountAbility Assurance Standard 2008, with a moderate level of type 2 assurance.
- The Guidelines for reviewing Corporate Responsibility Reports, issued by the Official Register of Auditors of Accounts (ICJCE).

Applied procedures

Our review consisted in performing inquiries to the Department of Sustainability and Reputation as well as the various managers of the business units that have participated in the preparation of the 2011 Annual Corporate Sustainability Report, and in applying analytical procedures and sampling review tests as described below:

1. Interviews with the persons in charge of Telefónica's Sustainability and Reputation Department and a selection of managers and key management personnel involved in the Report's preparation. The purpose of these was to obtain an understanding of the Corporate Sustainability objectives and policies, as well as how they are put into practice and integrated into the Telefónica Group's strategy.
2. Review of the main processes and systems through which Telefónica sets its commitments to its stakeholders, as well as the relevance and completeness of the information contained in the Report.
3. Analysis of the adaptation of the structure and content of the Report as indicated in G3.1 Global Reporting Initiative (GRI).
5. Test, on a sample basis, of the quantitative information included in the Report, as well as its adequate compilation from data supplied by information sources. The review tests have been defined to provide assurance levels as described in "Criteria" section in this report. Review Works have been carried out for the operations of Telefónica in Spain, Brazil, Argentina, Peru, Colombia, Mexico, Chile, Venezuela, Ecuador, Uruguay, Panama, El Salvador, Guatemala, Nicaragua, Germany and the UK.

A review is considerably less in scope than a reasonable assurance report. Therefore, the degree of assurance is also less. This report in no case should be considered an audit report.

These procedures have been applied based on the information provided in the 2011 Annual Report on Corporate Sustainability, except for the information relating to energy consumption and emissions that were not included in the scope of our review, on which we express no conclusion.

Our Independence

We have performed our work in accordance with the standards of independence required by the Code of Ethics of the International Federation of Accountants (IFAC).

(Free translation from the Original Report on Independent Review in Spanish dated 28th May 2012. In case of any discrepancy, the Spanish version always prevails)

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Conclusions

As a result of our review of the 2011 Annual Corporate Sustainability Report, carried out with the scope indicated in "Applied procedures" section above, we conclude that:

- No matter came to our attention that would lead us to believe that the Report has not been prepared according to the Guidelines included in the Global Reporting Initiative (GRI) Preparation Guide for Sustainability Reports, as it is stayed on it.
- No matter came to our attention that would lead us to believe that the remaining information and indicators included in the accompanying Report contain significant errors, or that the Report has not been prepared in accordance with the principles established in the AA1000 APS (2008) standard developed by Accountability, such as:
 - ✓ **Inclusivity:** The mechanisms are in place to identify stakeholders, as well as to gain an awareness and understanding of their expectations, as explained in the "Stakeholder matrix and stakeholder engagement procedure" section of the accompanying Report.
 - ✓ **Materiality:** A materiality study has been developed in order to select the most significant matters to be included in the Report, as described in the "Material issues Matrix" chapter.
 - ✓ **Responsiveness:** The necessary mechanisms to design, develop, evaluate, and communicate the responses necessary are in place in order to meet the principal expectations of stakeholders, as reflected in the chapter "Highlights and Challenges" included of the accompanying Report and that reflect the commitments assumed.

Recommendations

Additionally, we also presented to the Telefónica's Corporate Sustainability and Reputation Management our recommendations regarding areas of improvement related to the application of the standard AA1000 APS (2008), as well as to actions taken with main stakeholders identified. The most significant recommendations are related to:

a) Inclusivity:

During the year 2011, measures have been taken to enhance the dialogue channels with stakeholders, especially online channels such as "Dialogue 2.0". Our recommendation is to continue with the expansion of these channels gradually to the various stakeholders and to the principal countries in which it carries out its activities.

b) Materiality:

In the attached report, besides the materiality study, a specific section has been included with the relevant information of the most significant risks identified by the Telefónica S.A.'s Business Principles Office in terms of reputation.

Our recommendation is to continue adapting the process of identifying the most significant risks to the needs of each country in which it carries out its activities.

c) Responsiveness

The ongoing assessment of objectives and the proposal of new challenges which were published in the 2011 Annual Corporate Sustainability Report demonstrate Telefónica's commitment to respond to the expectations of stakeholders. Our recommendation is that Telefónica defines the objectives identification process more clearly to ensure that they are directly in line with the stakeholder's expectations.

We also present below a series of recommendations for actions related to the different stakeholders:

1) Clients:

During 2011 Telefónica has worked on the simplification and clarity of prices and tariffs for services provided. Our recommendation is to improve information related to complaints and claims.

2) Employees:

Information systems to obtain information on the indicators of "health and safety" have been improved, establishing challenges in the area of "diversity". Our recommendation is that Telefónica expands the information on various aspects of compensation, and to develop policies and standards for the management of "diversity".

3) Suppliers:

During 2011 Telefónica continued the development of the "Partners Program" and the application of the "Policy of responsibility in the supply chain", keeping the audit program for providers of risk and also including information on payment terms providers. Our recommendation is to more clearly define the goals and objectives in this area to improve its commitment to the interest group.

4) The community:

During 2011 Telefónica has continued working on its commitment to society, increased its financial contribution to "social action" and launching new programs such as "Think Big" in Europe and other programs related to "digital inclusion". Our recommendation is to establish methods to measure the impact of the projects of "digital inclusion".

4) Environmental matters:

During the year 2011 Telefónica has strengthened the services related to "Green ICT", and unifying the position of Telefónica in this area. Our recommendation is to continue working on these issues and improve the range of information on some indicators.

This report has been prepared solely for the Human Resources and Corporate Reputation Committee of Telefónica, S.A., in accordance with the terms and conditions set out in our engagement letter.

ERNST & YOUNG, S.L.



AA1000
Licensed Assurance Provider
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(Free translation from the Original Report on Independent Review in Spanish dated 28th May 2012. In case of any discrepancy, the Spanish version always prevails)

Telefonica

