Telefonica Europe B.V.

Annual Report
December 31, 2019

Contents

MANAGING DIRECTORS' REPORT

The management herewith submits the Financial Statements of Telefonica Europe B.V. ("the Company") for the financial year ended on December 31, 2019.

Result

During the year under review, the Company recorded a **profit after taxes (EUR 775 thousand) of EUR 2,356 thousand** (2018: EUR 2,790 thousand), which is set out in detail in the enclosed Statement of Income and Expenses.

The financial margin has decreased, from EUR 4,697 thousand in 2018 to EUR 4,358 thousand in 2019 mainly due to a decrease in borrowed and on-lent volumes in average terms.

Operational expenses are EUR 1,227 thousand in 2019 after having increased by 23.3%, when compared to the same period of 2018, mainly due to increases in tax and legal advisory fees associated to: (i) the Update of the Euro Commercial Paper Programme and (ii) the one-off expenses associated to the repurchase and cancelation of hybrid securities that took place on March 15, 2019.

Financing Activity

In regular course of business, the Company continued its financing activities by entering into several financing agreements unconditionally and irrevocably guaranteed by its parent company. The most relevant financing operations formalized during 2019 are the following:

(i) On March 14, 2019, the Company issued **EUR 1,300,000 thousand Undated Deeply Subordinated Guaranteed Fixed Rate Reset Securities** (commonly known as hybrids) 6 years Non-Call and carrying an interest rate of 4.375%;

(ii) On March 15, 2019, the Company **repurchased and cancelled EUR 934,700 thousand across 2 tranches of its Undated Deeply Subordinated Guaranteed Fixed Rate Reset Securities**;

The notional amount repurchased and outstanding (after the cancellation of the notes) per tranche is the following:

- EUR 850,000 thousand issued on December 4, 2014 and with a first call date on December 4, 2019 with an annual coupon of 4.20%: amount repurchased in 2018 EUR 145,200 thousand and amount repurchased in 2019 EUR 586,500 thousand, amount outstanding (after March 15, 2019 repurchase) EUR 118,300 thousand. This security was fully amortized on May 7, 2019, please, find further details at item (iii) below.
- EUR 750,000 thousand issued on March 31, 2014 and with a first call date on March 31, 2020 with an annual coupon of 5.00%: amount repurchased in 2018 EUR 158,200 thousand and amount repurchased in 2019 EUR 348,200 thousand, amount outstanding EUR 243,600 thousand.

(iii) On May 7, 2019, the Company called (following a Substantial Purchase Event contemplated in the Terms and conditions of the instruments) and cancelled in full the total outstanding amount **EUR 118,300 thousand of its Undated Deeply Subordinated Guaranteed Fixed Rate Reset Securities** issued on December 4, 2014 with an annual coupon of 4.20%;

(iv) On September 24, 2019, the Company issued **EUR 500,000 thousand Undated Deeply Subordinated Guaranteed Fixed Rate Reset Securities** (commonly known as hybrids) 8 years Non-Call and carrying an interest rate of 2.875% and

(v) In the short term, the Company continued with its issuing activity under the **EUR 5,000,000 thousand Euro Commercial Paper Programme** and, during 2019 placed, among several international investors 66 ECPs denominated in euro for a notional amount of EUR 3,656,000 thousand. The notional outstanding at December 31, 2019 was EUR 1,390,000 thousand (December 31, 2018: EUR 1,666,060 thousand).

Credit Facilities and liquidity management

On July 11, 2019 the Company notified to the lender the **irrevocable voluntary prepayment of EUR 750,000 thousand** from the EUR 1,500,000 thousand Credit Facility Agreement dated November 28, 2016 entered with China Development Bank. After this prepayment, the notional outstanding borrowed under this credit facility will be EUR 750,000 thousand. On October 17, 2019 the Company notified to the lender the **irrevocable voluntary prepayment of EUR 450,000 thousand,** consequently the notional outstanding borrowed will be EUR 300,000 thousand. On November 13, 2019 a **Side Letter** was issued to the China Development Bank in order to renegotiate the terms and conditions of the EUR 300,000 thousand outstanding amount. Finally, no agreement was reached among the parties and consequently the credit facility was cancelled and fully amortized on December 16, 2019.

Subsequent events

On February 5, 2020, the Company issued **EUR 500,000 thousand Undated Deeply Subordinated Guaranteed Fixed Rate Reset Securities** (commonly known as hybrids) 7.25 years Non-Call and carrying an interest rate of 2.502%, and on February 6, 2020 the Company repurchased and cancelled EUR 232,000 thousand and GBP 128,200 thousand (equivalent to EUR 151,055 thousand) across one Euro denominated and one British Sterling denominated hybrid securities. After the liquidation and cancellation of the repurchased hybrids, and as agreed in the terms and conditions, the Company announced the option to exercise the clean-up call of both series (equivalent to EUR 111,719 thousand). Additionally, the Company has announced the option to exercise the call of the EUR 243,600 thousand of the hybrid issued in March 2014.

Future developments

As performed during 2019 and, subject to financial market conditions, the Company will continue to seek and prospect for new markets and sources of finance for the Telefónica Group, to extend its investor base.

Risks and uncertainties

The main risk and uncertainties the Company will face are summarized as follows:

Liquidity and credit risk:

Liquidity and credit risks management is implemented according to the Telefonica Group policies. As of December 31, 2019 the Company has lent the funds borrowed, to Telefónica, S.A. which guarantees most of the external debt subscribed by the Company. However, from time to time the Company could invest funds in other companies within the Group. In addition, the Company holds cash balances in several financial institutions.

In summary, any substantial credit or liquidity risk would be related to credit risk of Telefónica S.A. and its Group.

Interest rate and Foreign Exchange risk:

Currently, the Company lends money to Telefónica S.A. denominated in the same currency although, from time to time the Company may also lend money to other companies within the Group. At present, all loans granted are denominated in the same currency as the funds it raises on the capital markets. Therefore, the Company is implementing a natural hedge and foreign exchange fluctuation in exchange rates have very limited impact on its financial result.
However, the Company may have a limited foreign exchange risk due to the financial margin earned in several currencies different from Euro (mainly GBP, JPY and USD) and cash positions held in foreign currencies (USD, JPY and GBP).

As of today, the Company policy is to hedge any interest rate exposure arising from funding raised, by investing on the similar terms and conditions (tenors and type of interest, whether it may be floating or fixed interest rates). Nevertheless, if that would not be eventually possible, or the management may not consider it appropriate, the Company may look to mitigate any interest rate risk in other ways (by using derivatives or any other suitable instrument), or eventually decide not to hedge it.

No significant impact regarding risks and uncertainties occurred during past financial year.

Existing or worsening conditions in the financial markets may limit the Telefónica’s Group ability to finance, and consequently, the ability to carry out its business plan.

The operation, expansion and improvement of the Telefónica Group's networks, the development and distribution of the Telefónica Group's services and products, the implementation of Telefónica's strategic plan and new technologies, the renewal of licenses or the expansion of the Telefónica Group's business in countries where it operates, may require a substantial amount of financing.

A decrease in the liquidity of either the Company or Telefónica, or a difficulty in refinancing maturing debt or raising new funds as debt or equity could force Telefónica to use resources allocated to investments or other commitments to pay its financial debt, which could have a negative effect on the Group's business, financial condition, and results of operations and/or cash flows.

Funding could be more difficult and costlier for the Company in the event of a significant deterioration of conditions in the international or local financial markets due to monetary policies set by central banks, including increases in interest rates and/or balance sheet reductions, and oil price instability, or if there is an eventual deterioration in the solvency or operating performance of the Telefónica Group.

Worsening of the economic and political environment could negatively affect Telefonica’s Group business.

Telefónica's international presence enables the diversification of its activities across countries and regions, but it exposes Telefónica to diverse legislation, as well as to the political and economic environments of the countries in which it operates. Any adverse developments or even uncertainties in this regard, including exchange-rate or sovereign-risk fluctuations, may adversely affect the Telefónica's business, financial position, cash flows and results of operations and/or the performance of some or all of the Group's financial indicators.

The macro-financial outlook in Europe showed tighter financing conditions for both the private and public sectors could arise in a scenario of financial stress with a negative impact on disposable income. The trigger for that scenario could be both global factors derived from an economic deterioration, or domestic issues such as the worsening of the fiscal sustainability in some European countries (e.g. Italy).

In Spain there are three sources of uncertainty. First, the outcome of the political situation in Catalonia and its impact on the financing conditions of the Spanish economy given the demanding maturity schedule the country is facing and its significant dependence on the international macroeconomic scenario and investors. A second source of uncertainty stems from the economic policies to be implemented from 2020 onwards, given the high level of parliamentary fragmentation and the lack of agreements on key issues. Finally, being one of the most open countries in the world, from a commercial point of view, and being amongst the top 10 countries in respect of capital outflows and inflows in the world, any situation of protectionist backlash can have significant implications.

Furthermore, the exit process of the United Kingdom from the European Union following the favorable vote in the June 2016 referendum will entail an economic adjustment regardless of the new economic and commercial relationship between the United Kingdom and the rest of Europe in the future. Investment, economic activity and employment would be the main variables affected, as well as volatility in financial markets, which could limit or condition access to capital markets. The situation could worsen depending on the eventual outcome of Brexit, which could lead to an increase in regulatory and legal conflicts in fiscal, commercial, security and employment issues. These changes can be costly and disruptive to business relationships in the affected markets, including those of Telefónica with its suppliers and customers.

Dutch Act on Management and Supervision

The Dutch Act on Management and Supervision indicated target figures for a balanced gender distribution when, of the seats occupied by individuals, at least 30% are occupied by women and at least 30% by men.

Given the law enactment the Company did not meet the above-mentioned gender balance in 2019 (25%) neither in 2018 (25%). The Company will pursue a policy to comply with the guidelines of the act and continue to strive for an adequate and balanced composition of its Board of Directors in future appointments, by considering all relevant selection criteria, including but not limited to gender balance and executive experience.

Audit Committee

The Company has not established an audit committee, as it is delegated in the parent company by using the exemption for subsidiaries as mentioned under article 3 of the legislation as announced on July 26, 2008 (“Koninklijk Besluit 323”).

Average number of employees

During the period under review the Company employed on average 3 persons, one of them working part-time, (2018: 2), none of them working outside The Netherlands.

Signing of the financial statements

The members of the Management Board have signed these financial statements pursuant to their statutory obligations under art. 5:25c(2)(c) Financial Markets Supervision Act. to the best of their knowledge, the financial statements give a true and fair value of the assets, liabilities, financial position and profit or loss of the company in accordance with Title 9 Book 2 of the Dutch Civil Code, and the management board’s report gives a true and fair view of the position and performance of the business of the company, and reflects the significant risks related to the business.

Amsterdam, February 19, 2020

Orginally signed by Mr. C.D. Maroto Sobrado	Orginally signed by Mr. J. Campillo Díaz
Orginally signed by Mrs. M.C. van der Sluijs-Plantz	Orginally signed by Mr. J.M. Hernández Rabbat

BALANCE SHEET
AS AT DECEMBER 31, 2019
(Before appropriation of result)

Euros in thousands

ASSETS	Note	31/12/2019	31/12/2018
Fixed Assets			
Tangible fixed assets	1	1	1
Financial fixed assets	2	9,480,891	10,196,795
Total Fixed Assets		**9,480,892**	**10,196,796**
Current Assets			
Loans receivable	3	1,391,766	1,667,044
Interest receivable		224,907	192,063
Other current assets		658	225
Cash at bank	4	5,369	6,168
Total Current Assets		**1,622,700**	**1,865,500**
TOTAL ASSETS		**11,103,592**	**12,062,296**

SHAREHOLDER'S EQUITY AND LIABILITIES	Note	31/12/2019	31/12/2018
Shareholder's Equity	5		
Issued share capital		46	46
Retained earnings		4,700	4,700
Result for the year		2,356	2,790
Total Shareholder´s Equity		**7,102**	**7,536**
Long Term Liabilities			
Bonds and loans	6	9,480,899	10,196,703
Total Long Term Liabilities		**9,480,899**	**10,196,703**
Current Liabilities			
Short term loans and bonds	7	1,391,766	1,667,044
Interest payable		223,076	190,444
Taxes payable		187	384
Other debts and accrued liabilities		562	185
Total Current Liabilities		**1,615,591**	**1,858,057**
TOTAL EQUITY & LIABILITIES		**11,103,592**	**12,062,296**

STATEMENT OF INCOME AND EXPENSES FOR THE YEAR ENDED DECEMBER 31, 2019

Euros in thousands

	Note	2019	2018
Financial Income and Expenses			
Interest Income		498,035	657,691
Interest Expense		(493,676)	(652,993)
Currency Exchange result		(1)	(1)
Net financial result	8	4,358	4,697
Operational Expenses			
Personnel expenses		(165)	(151)
Administrative expenses	9	(1,062)	(844)
Result from ordinary activities before taxation		3,131	3,702
Taxation	10	(775)	(912)
RESULT AFTER TAXATION		**2,356**	**2,790**

NOTES TO THE FINANCIAL STATEMENTS FOR THE PERIOD ENDED DECEMBER 31, 2019

General Information and Principal Activities

Telefónica Europe B.V. ("the Company"), having its statutory seat and registered office in Amsterdam, The Netherlands, and registered with the Dutch Chamber of Commerce under number 24263798 is engaged in holding and financing activities for related companies. The home member state selected by the Company is Ireland. Against the background of the Brexit, the Company changed its home member state to Ireland as the entity issued bonds at the stock exchange in Ireland as well. This change is in the process of being announced also to the Dutch regulator. The offices of the Company are located in Zuidplein 112, 1077XV, Amsterdam (The Netherlands). The Company was incorporated on October 31, 1996.

The authorized share capital of the Company consists of 100 shares with a par value of EUR 460 each (EUR 46,000). On December 31, 2019 and December 31, 2018, the issued capital of the Company consists of 100 shares, which have been fully paid and which represent a total paid up capital in the amount of EUR 46,000.

Group Affiliation

The Company is a wholly-owned subsidiary of Telefónica, S.A., located in Madrid, Spain. Direct or indirect subsidiaries of Telefónica, S.A. are referred to as related companies.

At December 31, 2019 and December 31, 2018, the Company does not own, directly or indirectly, any capital stock or other equity interests in any subsidiary.

Basis of Presentation

The financial statements are drawn up in accordance with the provisions of Title 9, Book 2 of the Dutch Civil Code and the firm pronouncements in the Dutch Accounting Standards, as published by the Dutch Accounting Standards Board (‘Raad voor de Jaarverslaggeving’).

As most of its activities are carried out in the Eurozone and the Company is domiciled in the Netherlands, the functional currency is the Euro. Therefore, these financial statements are presented in Euro.

Euro Medium Term Note Debt Programme

In 1996, the Company entered into a USD 1,500 million EMTN Debt Issuance Programme, arranged by Morgan Stanley & Co. International Limited, irrevocably guaranteed by Telefónica, S.A. Under the Programme, the Company may from time to time issue instruments in different currencies up to a maximum aggregate principal amount of USD 1,500 million. The total maximum aggregate principal amount was increased in 1998 to USD 2,000 million. In 2000, the total maximum aggregate principal amount was increased to EUR 8,000 million and finally, in July 2003, the maximum aggregate principal amount was increased again to EUR 10,000 million. The notes are listed on the Irish Stock Exchange. The Company has not issued any notes under this programme since 2003. The proceeds of the notes issued are lent o to the parent company or to other related companies within the group of the parent company (Telefónica, S.A.).

As at December 31, 2019, the EMTN Debt Issuance Programme includes:

- Euro Notes due 2033 EUR 500,000,000

Global bonds

On September 21, 2000, Telefónica Europe B.V. issued notes for the notional amounts and coupons of USD 1,250,000,000 7.35% and EUR 1,000,000,000 6.125% due and repaid in 2005, USD 2,500,000,000 7.75% due and repaid in 2010 and USD 1,250,000,000 8.25% due 2030. These bonds are irrevocably guaranteed by the parent company.

As at December 31, 2019, there is only one outstanding note under the programme (USD 1,250 million carrying a semi-annual coupon of 8.25% and maturing on September 2030) and is quoted in Frankfurt and New York.

Euro Commercial Paper Programme (ECP Programme)

On June 29, 2000, the Company entered into a Euro Commercial Paper Programme with a maximum aggregate principal amount of EUR 2,000,000,000 or its equivalent in alternative currencies. The Programme was updated in May 2005 and in May 2012, when its maximum aggregate principal amount outstanding (limit of the programme) was raised from EUR 2,000,000,000 to EUR 3,000,000,000 or its equivalent in alternative currencies. On April 22, 2016, the limit of the Programme was increased again by fixing this maximum outstanding principal amount into EUR 5,000,000,000 or its equivalent in the alternative currencies. On December 17, 2019 the Company entered into an amended and restated agreement with no impact on the limit of the programme fixed on April 22, 2016.

The parent company guarantees in an unconditional and irrevocable basis all issues made under de ECP Programme. Notes may have any denomination, subject to compliance with any applicable legal and regulatory requirements. The minimum denominations are EUR 500,000, USD 500,000, JPY 100,000,000, and GBP 100,000. The tenor of the notes shall be not less than one or more than 365 days.

The notional outstanding amount as at December 31, 2019 is EUR 1,390 million and is composed by ECPs issued in Euros. In the balance sheet the outstanding ECP issues are stated at their discounted notional amounts and were accounting for EUR 1,392 million at year-end.

JPY Dual Currency Loan

The Company borrowed JPY 15,000 million in three loans from a Japanese investor with a maturity on July 2037. Under this agreement interests are payable in USD on a semi-annual basis at a fix annual rate of 4.75%.

Perpetual Hybrid Securities in EUR and in GBP

On September 18, 2013, the Company issued two tranches of perpetual hybrid securities of EUR 1,125,000 thousand and EUR 625,000 thousand respectively. A third issue of GBP 600,000 thousand was completed on

November 26, 2013. On March 31, 2014 the Company issued two tranches of perpetual hybrid securities of EUR 750,000 thousand and EUR 1,000,000 thousand. On December 4, 2014 the Company issued a new tranche of perpetual hybrid securities for EUR 850,000 thousand. On September 15, 2016, the Company issued a new tranche of perpetual hybrid securities for EUR 1,000,000 thousand. On December 7, 2017, the Company issued a new tranche of EUR 1,000,000 thousand of perpetual hybrid securities. On March 22, 2018, when the Company issued two additional tranches of perpetual hybrid securities of EUR 1,250,000 thousand and EUR 1,000,000 thousand. On March 14, 2019, the Company issued a new tranche of perpetual hybrid securities for EUR 1,300,000 thousand. The last issuance of hybrid securities took place on September 24, 2019, when the Company issued a new tranche of perpetual hybrid securities for EUR 500,000 thousand.

On March 23, 2018 the company repurchased and cancelled EUR 1,287,400 thousand and GBP 428,500 thousand (equivalent to EUR 490,848 thousand) across four Euro denominated and one British Sterling denominated hybrid securities. On September 18, 2018, coinciding with the first call date, the Company cancelled EUR 473,300 thousand of the EUR 1,125,000 thousand issued on September 18, 2013 carrying an annual coupon of 6.50%. After this cancelation no amount is due from this hybrid securities, since the Company had already repurchased and cancelled EUR 651,700 thousand in a partial repurchase executed on March 23, 2018.

On March 15, 2019 the company repurchased and cancelled EUR 934,700 thousand of perpetual hybrid securities. The notional amounts repurchased (and cancelled) and premium paid for each of the tranches are the following

Euros in thousands

ISIN	Description	Repurchase Notional amount	Premium	Total amount paid*
XS1148359356	EUR 850,000,000 4.2% perpetual (non-call 5 years) Hybrid Securities	EUR 586,500	EUR 17,818	EUR 604,318
XS1050460739	EUR 750,000,000 5% perpetual (non-call 6 years) Hybrid Securities	EUR 348,200	EUR 17,142	EUR 365,342
Total Euro denominated Hybrid securities		**EUR 934,700**	**EUR 34,960**	**EUR 969,660**

*Excluding accrued coupons.

On May 7, 2019, the Company called (following a substantial purchase event) and cancelled EUR 118,300 thousand of the EUR 850,000 thousand perpetual hybrid securities issued on December 4, 2014 that were originally issued with a first call date on December 4, 2019 and carried an annual coupon of 4.2%. After this cancelation no amount is due from this hybrid securities, since the Company had already repurchased and cancelled EUR 145,200 thousand in a partial repurchase executed last year (on March 23, 2018) and EUR 586,500 thousand in another partial repurchase executed this year (on March 15, 2019).

The perpetual hybrid securities outstanding at December 31, 2019, amounted a total notional amount equivalent to EUR 7,787,787 thousand (the foreign exchange rate for British Sterling hybrid securities is the closing rate as of December 31, 2019). At December 31, 2019 all perpetual hybrid securities issued by the Company are listed for trading on the Irish Stock Exchange.

The main terms of the tranches issued and currently outstanding at December, 31, 2019 are the following:

i. EUR 625,000 thousand issued on September 18, 2013 and with a first call date on September 18, 2021 with an annual coupon of 7.625% (ISIN: XS0972588643). The notional outstanding amount as of December 31, 2019 is EUR 292,700 thousand;

ii. GBP 600,000 thousand issued on November 26, 2013 and with a first call date on November 26, 2020 with an annual coupon of 6.75% (ISIN: XS0997326441). The notional outstanding amount as of December 31, 2019 is GBP 171,500 thousand;

iii. EUR 750,000 thousand issued on March 31, 2014 and with a first call date on March 31, 2020 with an annual coupon of 5.00% (ISIN: XS1050460739). The notional outstanding amount as of December 31, 2019 is EUR 243,600 thousand;

iv. EUR 1,000,000 thousand issued on March 31, 2014 and with a first call date on March 31, 2024 with an annual coupon of 5.875% (ISIN: XS1050461034);

v. EUR 1,000,000 thousand issued on September 15, 2016 and with a first call date on March 15, 2022 with an annual coupon of 3.75% (ISIN: XS1490960942);

vi. EUR 1,000,000 thousand issued on December 7, 2017 and with a first call on June 7, 2023 with an annual coupon of 2.625% (ISIN: XS1731823255);

vii. EUR 1,250,000 thousand issued on March 22, 2018 and with a first call on December 4, 2023 with an annual coupon of 3.000% (ISIN: XS1795406575);

viii. EUR 1,000,000 thousand issued on March 22, 2018 and with a first call on September 22, 2026 with an annual coupon of 3.875% (ISIN: XS1795406658);

ix. EUR 1,300,000 thousand issued on March 14, 2019 and with a first call on March 14, 2025 with an annual coupon of 4.375% (ISIN: XS1933828433) and

x. EUR 500,000 thousand issued on September 24, 2019 and with a first call on September 24, 2027 with an annual coupon of 2.875% (ISIN: XS2056371334).

The annual coupon included for all the securities is until the first call date. After that, they will be reset depending on the swap rates as disclosed in each security listed documentation. The securities are listed on the Irish Stock Exchange.

EUR 1,500 million Facility Agreement

A facility agreement of EUR 1,500,000 thousand with an international financial institution (China Development Bank) and guaranteed by Telefónica, S.A. was entered into November 28, 2016. The facility matures on November 28, 2024 and (as from February 15, 2020 until August 16, 2024) contemplates semi-annual principal repayment instalments coinciding with the interest payment dates. The proceeds of the facility agreement are on lent to the parent company for the ultimate purpose of financing the Group's procurement of telecommunications equipment and related services.

The first drawdown, of EUR 750,000 thousand, took place on January 24, 2017. The second, and last drawdown, of EUR 750,000 thousand, took place on July 18, 2018. After this second disposal the facility (which is not revolving) was fully drawn.

On July 11, 2019 the Company notified to the lender the **irrevocable voluntary prepayment of EUR 750,000 thousand** from the EUR 1,500,000 thousand Credit Facility Agreement dated November 28, 2016 entered with China Development Bank and consequently reclassified this loan to current liabilities. After this prepayment, the notional outstanding borrowed under this credit facility will be EUR 750,000 thousand. On October 17, 2019 the Company notified to the lender the **irrevocable voluntary prepayment of EUR 450,000 thousand,** consequently the notional outstanding borrowed will be EUR 300,000 thousand. On November 13, 2019 a **Side Letter** was issued to the China Development Bank in order to renegotiate the terms and conditions of the EUR 300,000 thousand outstanding amount. Finally, no agreement was reached among the parties and consequently the credit facility was cancelled and fully amortized on December 16, 2019.

Investments of the Company

Substantially all the net proceeds from the principal or notional amounts obtained or borrowed by the Company under its financing activities have been lent on to the parent company.

Cash flow statement

A cashflow statement has not been included in this financial statement as the Company's cash flows are included in the consolidated cash flow statement in the financial statements of the ultimate parent company Telefónica, S.A., which can be obtained from its website www.telefonica.com. This exemption is provided in DAS 360.104.

ACCOUNTING POLICIES

General

The accounting principles of the Company are summarized below. These accounting principles have all been applied consistently throughout the year and the preceding year unless otherwise indicated.

Foreign currencies

Assets and liabilities denominated in foreign currencies are translated into the presentation currency at exchange rates prevailing at the Balance Sheet date. Any resulting exchange differences are recorded in the Statement of Income and Expenses.

Revenues and expenses in the year under review, which are denominated in foreign currencies, are translated into the reporting currency at exchange rates in effect on the transaction date.

Accounting policies in respect of the Balance Sheet

Tangible fixed assets

Tangible fixed assets are stated at their historical cost less accumulated depreciation. Depreciation is provided over the expected useful life of the related asset under the straight-line depreciation method. The estimated useful lives are:

Furniture and office equipment: 3 to 5 years

Long term receivables from related companies

At its initial recognition in the Balance Sheet, long term receivables from related companies are measured at its fair value, which is the transaction price plus the transaction costs that are directly attributable to the issue of the financial asset.

Subsequently, long term receivables from related companies are carried at amortized cost using the effective interest rate method, except where otherwise stated in these notes. Gains and losses are recognized in the income statement when the loans are derecognized or impaired, as well as through the amortization process.

Transactions with related parties

Transactions with related parties are disclosed in the notes insofar as they are not transacted under normal market conditions. The nature, extent and other information is disclosed if this is necessary in order to provide the required insight.

Currently the Company doesn't have any subsidiary. All legal entities that can be controlled, jointly controlled or significantly influenced would be considered to be a related party. Also, entities which can control the Company are considered to be a related party. In addition, statutory directors, other key management of the Company or the ultimate parent company and close relatives are regarded as related parties.

Impairment of financial assets

A financial asset not carried at fair value through profit or loss is assessed at each reporting date to determine whether there is objective evidence that it is impaired. A financial asset is impaired if objective evidence indicates that a loss event has occurred after the initial recognition of the asset, and that the loss event had a negative effect on the estimated future cash flows of that asset that can be estimated reliably.

Objective evidence that financial assets are impaired can include default or delinquency by a debtor, restructuring of an amount due to the Company on terms that the Company would not consider otherwise, or indications that a debtor or issuer will enter bankruptcy.

The Company considers evidence of impairment for receivables at both a specific and collective level. All individually significant receivables are assessed for specific impairment. All individually significant receivables found not to be specifically impaired, together with receivables that are not individually significant are collectively assessed for impairment by grouping together receivables with similar risk characteristics.

An impairment loss in respect of a financial asset measured at amortized cost is calculated as the difference between its carrying amount and the present value of the estimated future cash flows discounted at the asset's original effective interest rate. Losses are recognized in profit or loss and reflected in an allowance account against receivables. When a subsequent event causes the amount of impairment loss to decrease, the decrease in impairment loss is reversed through profit or loss.

Current loans receivables and other payables

As from its initial recognition current loans receivables and payables are carried at amortized cost using the effective interest rate method, except where otherwise stated in these notes.

Interest receivables and interest payables

The Company accrues interest income and expenses in the balance sheet current assets or current liabilities, as it is applicable, when such interests are receivable/due according to the terms and conditions of the instruments subscribed. Following an interest payment, the accrual of interest is derecognized (in the same amount) in balance sheet.

Cash at banks

Cash at banks represent cash in bank balances and deposits with terms of less than twelve months. Overdrafts at banks are recognised as part of debts to lending institutions under current liabilities. Cash at banks is carried at nominal value.

Bonds and loans

At its initially recognition in the Balance Sheet, bonds and loans are measured at its fair value, which is the price of the transaction minus the transaction costs that are directly attributable to the issue of the financial liability.

Subsequently, bonds and loans are carried at amortized cost using the effective interest rate method, except where otherwise stated in these notes. Gains and losses are recognized in the Statement of Income and Expense when the liabilities are derecognized as well as through the amortization process.

Estimates

In applying the principles and policies for drawing up the financial statements, the directors of Telefonica Europe B.V. make different estimates and judgments that may be essential to the amounts disclosed in the financial statements. If it is necessary in order to provide the true and fair view required under Book 2, article 362, paragraph 1, the nature of these estimates and judgments, including related assumptions, is disclosed in the notes to the relevant financial statement item.

Accounting policies in respect of result determination

Interest incomes and expenses

Interest income and expense are recognized in profit or loss using the effective interest rate method. The effective interest rate includes all fees and basis points paid or received that are an integral part of the effective interest rate. This includes transaction costs that are directly attributable to the acquisition or issue of financial assets or liabilities.

Costs and revenues are recognized in the year to which they refer regardless of when paid or received, in accordance with the accrual basis. Differences between amounts received and paid and the corresponding revenue and costs are recognized under the correspondent caption of financial assets or financial liabilities.

Operational income and and expenses are based on the historical cost convention and attributed to the financial year to which they pertain.

Taxation

Taxation is calculated on the reported pre-tax result, at the prevailing tax rates, taking account of any losses carried forward from previous financial years and tax-exempt items and non-deductible expenses and using tax facilities.

Temporary differences between taxation on the result as shown in the Statement of Income and Expense and the taxation on the fiscal result are added or deducted from the provision for deferred taxation.

The Company has entered into an Advance Pricing Agreement with the Tax Authorities. This Agreement, that expires on December 31, 2019, establishes that the Company will pay taxes according to a minimum applicable margin applied to the funds borrowed to Telefónica, S.A. or any other affiliate of Telefónica, S.A.

Accounting policies in respect of Financial Instruments

General

The information included in the notes for financial instruments is useful to estimate the extent of risks relating to on-balance sheet financial instruments. The Company’s primary financial instruments, not being derivatives, serve to finance the Telefonica’s Group operating activities. The principal risks, arising from the Company’s financing operations are, liquidity, credit, interest and foreign exchange risks. These risks are set out in detail below:

i. Liquidity and credit risk

Liquidity and credit risk management is implemented according to the Telefonica Group policies. As of December, 31, the Company has invested the funds borrowed, in Telefónica, S.A. which guarantees most of the external debt subscribed by the Company. However, from time to time the Company could also invest the funds in other companies within the Group. In addition, the Company holds cash balances in several financial institutions. In summary, as any substantial credit or liquidity risk would be related to credit risk of Telefónica, S.A. and its Group.

As of December 31, 2019 and Telefónica, S.A. and Telefónica Europe, B.V. have been granted the same company credit ratings. These ratings are the following:

- Moody's Investors Services: Baa3 for the long term rating and P-3 for the short term rating. Outlook stable and last review November 7, 2016.
- Fitch Ratings: BBB for the long term rating and F-2 for the short term rating. Outlook stable and last review September 5, 2016.
- Standard and Poor's: BBB for the long term rating and A-2 for the short term rating. Outlook stable and last review May 17, 2016.

ii. Interest rate and Foreign Exchange risk

Currently, the Company lends money to Telefónica S.A. although, from time to time, the Company may also lend money to other companies within the Telefonica Group. At present, all loans granted are denominated in the same currency as the funds it raises on the capital markets. Therefore, the Company is implementing a natural hedge. Consequently, foreign exchange fluctuation in exchange rates have a limited impact on its financial result.

However, the Company may have a limited foreign exchange risk due to the financial margin earned in several currencies different from Euro (mainly US Dollar and British Pound) and also due to some cash positions held in foreign currencies (US Dollar and British Pound).

Currently, the Company's policy is to hedge any interest rate exposure coming from funding raised by investing on similar terms and conditions (tenors and type of interest, whether it may be floating or fixed interest rates). Nevertheless, if that would not eventually be possible, or the management may not consider it appropriate, the Company may look to mitigate any interest rate risk in other ways (by using derivatives or any other suitable instrument) or eventually may decide not to hedge it.

1. Tangible Fixed Assets

The tangible fixed assets are comprised as follows:

Euros in thousands

	31/12/2019	31/12/2018
Tangible fixed assets	1	1

The movement in the tangible fixed assets is as follows:

Euros in thousands

	31/12/2019	31/12/2018
Carrying value		
Balance January 1	94	93
Additions	-	1
Balance December 31	**94**	**94**
Accumulated depreciation		
Balance January 1	(93)	(91)
Change for the period	-	(2)
Balance December 31	**(93)**	**(93)**
Net book value	**1**	**1**

2. Financial fixed assets

Euros in thousands

	31/12/2019	31/12/2018
Long term receivables from related companies	9,480,891	10,196,795
Financial Fixed assets	**9,480,891**	**10,196,795**

The movement in the financial fixed assets is as follows:

Euros in thousands

	31/12/2019	31/12/2018
Balance January 1	10,196,795	9,385,213
Deferred Commissions amortization	12,342	13,190
Repayments	(2,553,000)	(2,251,548)
New Loans	1,789,450	2,986,626
Foreign Exchange result	35,304	63,314
Balance December 31	**9,480,891**	**10,196,795**

On March 15, 2019 Telefónica, S.A. pre-amortized EUR 934,700 thousand across two Euro denominated Loans, and on May 7, 2019, following a substantial purchase event, another EUR 118,300 thousand were cancelled. During 2019 the EUR 1,500,000 thousand Credit Facility Agreement was fully amortized in three different prepayment dates: EUR 750,000 thousand on August 16, EUR 450,000 thousand on November 16 and EUR 300,000 thousand on December 16, 2019.

Long term receivables from related companies

The long term receivables from related companies represent loans to Telefónica, S.A. and total **EUR 9,480,891 thousand** on December 31, 2019 (EUR 10,196,795 thousand at December 31, 2018). The average interest rate for the long term receivables is 4.33% for financial year 2019 and 4.50% for financial year 2018.

Euros in thousands

Description	31/12/2019	31/12/2018
USD 1,250,000,000, maturity September 15, 2030	1,106,676	1,084,786
EUR 500,000,000, maturity February 14, 2033	493,925	493,640
JPY 5,000,000,000/USD 42,640,287, maturity July 27, 2037	40,845	39,548
JPY 5,000,000,000/USD 42,640,287, maturity July 27, 2037	40,845	39,548
JPY 5,000,000,000/USD 42,640,287, maturity July 27, 2037	40,845	39,548
EUR 292,700,000, maturity September 18, 2053	292,146	291,856
GBP 171,500,000, maturity November 26, 2053	201,254	191,132
EUR 243,600,000, maturity March 31, 2054	243,527	590,883
EUR 1,000,000,000, maturity March 31, 2054	996,631	995,955
EUR 118,300,000, maturity December 4, 2019	-	704,340
EUR 1,000,000,000 maturity March 15, 2056	997,397	996,290
EUR 1,500,000,000, maturity November 28, 2024	-	1,495,748
EUR 1,000,000,000 maturity June 7, 2058	996,512	995,504
EUR 1,000,000,000 maturity September 22, 2058	994,909	994,263
EUR 1,250,000,000 maturity December 04, 2058	1,244,946	1,243,754
EUR 1,300,000,000 maturity March 14, 2060	1,293,343	-
EUR 500,000,000 maturity September 24, 2060	497,090	-
Total Long term receivable from related companies	**9,480,891**	**10,196,795**

The fair value for the long term receivables from the related companies are not substantially different to the fair value of the long term bonds and loans (disclosed at in note 6), since the terms and conditions of these long term receivables are almost equal to the terms and conditions of the bonds and loans issued.

The calculation of the fair value for the long term receivables from the related companies has been calculated by applying level 2 (of the hierarchy disclosed in note 6) after discounting the cash flows of the loans using an estimated credit spread curve for each applicable currency.

3. Loans receivable

The loans receivable comprises short-term loans due by the shareholder (granted by means of loan agreement dated May 10, 2012) and other related companies (if any) and amounted **EUR 1,391,766 thousand** on December 31, 2019 (EUR 1,667,044 thousand on December 31, 2018). The average interest rate is -0.23% for financial year 2019 and -0.19% for financial year 2018.

Euros in thousands

	31/12/2019	31/12/2018
Short Term Loans to Telefónica, S.A.	1,391,766	1,667,044
Total loans receivable	1,391,766	1,667,044

The fair value of the short term loans to Telefónica does not substantially differ from the book value. Given the short term nature, the impact of the discount is not significant.

4. Cash at bank

The cash at bank is freely disposable and there are not interests obtained from the bank accounts. All the banks we work with have BBB credit rating or higher. The balances on December 31, 2019 and December 31, 2018 are comprised as follows:

Euros in thousands

	31/12/2019	31/12/2018
Current bank account balances	**5,369**	**6,168**

5. Shareholder's equity

The movements in the Shareholder's Equity are comprised as follows:

Euros in thousands

	Issued share capital	Retained earnings	Result for the year	Total Shareholder's Equity
Balance as at January 1, 2018	46	4,700	2,322	7,068
Allocation of result	-	2,322	(2,322)	-
Result for the year	-	-	2,790	2,790
Dividend payment	-	(2,322)	-	(2,322)
Balance as at December 31, 2018	**46**	**4,700**	**2,790**	**7,536**
Balance as at January 1, 2019	46	4,700	2,790	7,536
Allocation of result	-	2,790	(2,790)	-
Result for the year	-	-	2,356	2,356
Dividend payment	-	(2,790)	-	(2,790)
Balance as at December 31, 2019	**46**	**4,700**	**2,356**	**7,102**

6. Bonds and loans

The long term bonds and loans balance is the following:

Euros in thousands

	31/12/2019	31/12/2018
Long term bonds and loans	**9,480,899**	**10,196,703**

The movement in long term liabilities is as follows:

Euros in thousands

	2019	2018
Balance January 1	10,196,703	9,385,428
Prepaid Commissions amortization	12,351	12,827
Repayments	(2,553,000)	(2,251,548)
New issuances	1,789,542	2,986,681
Foreign Exchange result	35,303	63,315
Balance December 31	**9,480,899**	**10,196,703**

On March 15, 2019 the Company pre-amortized EUR 934,700 thousand across two Euro denominated Loans, and on May 7, 2019, following a substantial purchase event, another EUR 118,300 thousand were cancelled. During 2019 the EUR 1,500,000 thousand Credit Facility Agreement was fully amortized in three different prepayment dates: EUR 750,000 thousand on August 16, EUR 450,000 thousand on November 15 and EUR 300,000 thousand on December 16.

The average interest rate for the long term liabilities is 4.30% for financial year 2019 and 4.47% for financial year 2018.

The long term bonds and loans are comprised as follows:

Euros in thousands

Description	31/12/2019	31/12/2018
Global USD 1,250,000,000, 8.250%, maturity September 15, 2030 (ISIN: US879385AD49)	1,106,684	1,084,793
EMTN EUR 500,000,000, 5.875%, maturity February 14, 2033 (ISIN: XS0162869076)	493,935	493,648
JPY/USD Dual Currency Loan A JPY 5,000,000,000/USD 42,640,287, 4.750% on USD basis, maturity July 27, 2037	40,845	39,548
JPY/USD Dual Currency Loan B JPY 5,000,000,000/USD 42,640,287, 4.750% on USD basis, maturity July 27, 2037	40,845	39,548
JPY/USD Dual Currency Loan C JPY 5,000,000,000/USD 42,640,287, 4.750% on USD basis, maturity July 27, 2037	40,845	39,548
EUR 292,700,000 7.625% perpetual (non-call 8 years) Hybrid Securities (ISIN: XS0972588643)	292,083	291,760
GBP 171,500,000 6.750% perpetual (non-call 7 years) Hybrid Securities (ISIN: XS0997326441)	201,215	191,141
EUR 243,600,000 5.000% perpetual (non-call 6 years) Hybrid Securities (ISIN: XS1050460739)	243,527	590,879
EUR 1,000,000,000 5.875% perpetual (non-call 10 years) Hybrid Securities (ISIN: XS1050461034)	996,537	995,842
EUR 118,300,000 4.200% perpetual (non-call 5 years) Hybrid Securities (ISIN: XS1148359356)	-	704,233
EUR 1,000,000,000 3.750% perpetual (non-call 5.5 years) Hybrid Securities (ISIN: XS1490960942)	997,442	996,353
EUR Facility, EUR 1,500,000,000, 3 months Euribor + 0.70%, maturity November 28, 2024	-	1,495,769
EUR 1,000,000,000 2.625% perpetual (non-call 5.5 years) Hybrid Securities (ISIN: XS1731823255)	996,550	995,605
EUR 1,000,000,000 3.875% perpetual (non-call 8.5 years) Hybrid Securities (ISIN: XS1795406658)	994,922	994,277
EUR 1,250,000,000 3.000% perpetual (non-call 5.7 years) Hybrid Securities (ISIN: XS1795406575)	1,244,955	1,243,759
EUR 1,300,000,000 4.375% perpetual (non-call 6 years) Hybrid Securities (ISIN: XS1933828433)	1,293,398	-
EUR 500,000,000 2.875% perpetual (non-call 8 years) Hybrid Securities (ISIN: XS2056371334)	497,116	-
Total long term bond and loans	**9,480,899**	**10,196,703**

The fair value of the long term loans and bonds subscribed by the Company at December 31, 2019 totals **EUR 10,772,998 thousand** (EUR 10.626.074 thousand at 31 December, 2018).

The Company calculates the fair value of the long term loans and bonds using the following fair value hierarchy that reflects the significance of the inputs used in making the measurements.

- Level 1: Inputs that are quoted market prices (unadjusted) in active markets for either: (i) the instruments issued by the Company or (ii) identical instruments to those issued by the company.
- Level 2: Inputs other than quoted prices included within Level 1 that are observable either directly (i.e. as prices) or indirectly (i.e. derived from prices). This category includes instruments valued using: quoted market prices in active markets for similar instruments; quoted prices for identical or similar instruments in markets that are considered less than active; or other valuation techniques in which all significant inputs are directly or indirectly observable from market data.
- Level 3: Inputs that are unobservable. This category includes all instruments for which the valuation technique includes inputs not based on observable data and the unobservable inputs have a significant effect on the instrument's valuation. This category includes instruments that are valued based on quoted prices for similar instruments but for which significant unobservable adjustments or assumptions are required to reflect differences between the instruments.

The Company has calculated the fair value for the bonds issued by applying level 1 of the above hierarchy. The bonds fair value has been calculated using the year-end market price published at the stock exchange where the bonds are admitted for trading.

The fair value of the Loans subscribed by the Company has been calculated by applying level 2 of the above hierarchy, after discounting the cash flows of the Loans using an estimated credit spread curve for each applicable currency.

7. Short term loans and bonds

As at December 31, 2019, the loans and bonds payable comprises the amount due under the Company's EUR 5,000,000 thousand Euro Commercial Paper Program. The balance on December 31, 2019 totals **EUR 1,391,766 thousand** (EUR 1,667,044 thousand at December 31, 2018). The average interest rate is 0.04% for financial year 2019 and 0.05% for financial year 2018.

Euros in thousands

	31/12/2019	31/12/2018
EUR 5,000,000,000 ST European Commercial Paper Program	1,391,766	1,667,044
Balance December 31	**1,391,766**	**1,667,044**

The fair value of the short term bonds and loans does not substantially differ from the book value. Given the short term nature of the loans and bonds, the impact of discount is not relevant.

8. Net Financial Result

The Net Financial Result is comprised as follows:

Euros in thousands

	2019	2018
Interest income	498,035	657,691
Interest expense	(493,676)	(652,993)
Currency exchange result	(1)	(1)
Net Financial Result	**4,358**	**4,697**

Interest income comes in full from related companies as all loan's receivable have been granted to related companies. During both years it also includes a one-off impact to P&L for the repurchase and cancellation of hybrid securities that took place on March 15, 2019 and March 23, 2018.

9. Administrative expenses

At December 31, 2019 the administrative expenses total EUR 1,062 thousand (EUR 844 thousand at December 31, 2018). The increase in administrative expenses at December 31, 2019 (when compared to last year) is mainly due to increases in tax and legal advisory fees associated to: (i) the Update of the Euro Commercial Paper Programme and (ii) the one-off expenses associated to the repurchase and cancelation of hybrid securities that took place on March 15, 2019.

Euros in thousands

	2019	2018
Administrative expenses	(1,062)	(844)
Total	**(1,062)**	**(844)**

10. Taxation

The tax charge on the profit can be broken down as follows:

Euros in thousands

	2019	2018
Corporate income tax 2019	775	-
Corporate income tax 2018	-	915
Corporate income tax 2017	-	(3)
Total	**775**	**912**

The Company is subject to Dutch taxation and tax calculations are made in accordance with an Advance Pricing Agreement signed with the Dutch Tax Authorities, which entered into effect on January 1, 2005, as amended in February 2006, in October 2010 and in September 2015. The renewal request of this Agreement, that expires on December 31, 2019, was submitted to the Dutch Tax Authorities on June 28, 2019.

The main features of this agreement are the establishment of a minimum financial margin for the transactions registered between Telefónica, S.A. and the Company as well as a capped yearly amount of operational expenses.

The effective and applicable tax rates do not differ significantly from those of previous fiscal year.

The applicable tax rate for the current financial statements is 25% (2018: 25%) and the effective tax rate is 24.75% (2018: 24.65%).

Average number of employees

During the period under review the Company employed on average 3 persons, one of them working part-time, (2018: 2), none of them working outside The Netherlands.

Auditor's fees

The auditor's fees for the financial year 2019 audit come up to EUR 34 thousand (EUR 34 thousand in 2018). However, during 2019 the Company has not paid yet any of these fees as they were not invoiced until 2020.

The amount paid in respect of fees for other audit services rendered by PricewaterhouseCoopers Accountants

N.V., amounted to EUR 106 thousand in 2019 (EUR 36 thousand in 2018).

There were no fees other than audit and other audit (hence no consultancy and no tax fees).

Subsequent events

On February 5, 2020, the Company issued **EUR 500,000 thousand Undated Deeply Subordinated Guaranteed Fixed Rate Reset Securities** (commonly known as hybrids) 7.25 years Non-Call and carrying an interest rate of 2.502%, and on February 6, 2020 the Company repurchased and cancelled EUR 232,000 thousand and GBP 128,200 thousand (equivalent to EUR 151,055 thousand) across one Euro denominated and one British Sterling denominated hybrid securities. After the liquidation and cancellation of the repurchased hybrids, and as agreed in the terms and conditions, the Company announced the option to exercise the clean-up call of both series (equivalent to EUR 111,719 thousand). Additionally, the Company has announced the option to exercise the call of the EUR 243,600 thousand of the hybrid issued in March 2014.

Appropriation of Result

The management proposal is to accumulate the net result of year ended December 31, 2019 to the retained earnings.

Board of directors

The Company's board of directors consists of 4 directors (2018: 4), who received a total remuneration of EUR 10 thousand (2018: EUR 10 thousand).

Amsterdam, February 19, 2020

Orginally signed by
Mr. C.D. Maroto Sobrado

Orginally signed by
Mr. J. Campillo Díaz

Orginally signed by
Mrs. M.C. van der Sluijs-Plantz

Orginally signed by
Mr. J.M. Hernández Rabbat

OTHER INFORMATION AS AT DECEMBER 31, 2019

Independent Auditor's report

The independent auditor's report is set out on the next pages.

Statutory provision regarding appropriation of Result

In accordance with Article 14 of the Articles of Association, profit shall be at the disposal of the Annual General Meeting of Shareholders. Profit distribution can only be made to the extent that Shareholder's Equity exceeds the issued and paid-up share capital and legal reserves.

A resolution to distribute profits or reserves is subject to the approval of the managing board. The managing board shall only withheld its approval if it knows or should reasonably expect that following the distribution the Company cannot continue to pay its debts due.

Independent auditor's report

To: the general meeting of Telefonica Europe B.V.

Report on the financial statements 2019

Our opinion

In our opinion, the financial statements of Telefonica Europe B.V. give a true and fair view of the financial position of the Company as at 31 December 2019, and of its result for the year then ended in accordance with Part 9 of Book 2 of the Dutch Civil Code.

What we have audited

We have audited the accompanying financial statements 2019 of Telefonica Europe B.V., Amsterdam.

The financial statements comprise:

- the balance sheet as at 31 December 2019;
- the statement of income and expenses for the year then ended; and
- the notes, comprising the accounting policies and other explanatory information.

The financial reporting framework applied in the preparation of the financial statements is Part 9 of Book 2 of the Dutch Civil Code.

The basis for our opinion

We conducted our audit in accordance with Dutch law, including the Dutch Standards on Auditing. We have further described our responsibilities under those standards in the section 'Our responsibilities for the audit of the financial statements' of our report.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Independence

We are independent of Telefonica Europe B.V. in accordance with the European Union Regulation on specific requirements regarding statutory audit of public-interest entities, the 'Wet toezicht accountantsorganisaties' (Wta, Audit firms supervision act), the 'Verordening inzake de onafhankelijkheid van accountants bij assuranceopdrachten' (ViO, Code of Ethics for Professional Accountants, a regulation with respect to independence) and other relevant independence requirements in the Netherlands. Furthermore, we have complied with the 'Verordening gedrags- en beroepsregels accountants' (VGBA, Dutch Code of Ethics).

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Our audit approach

Overview and context

The Company's main activity is the financing of group companies, through bond offerings on the international capital markets. The repayment of the bonds to the investors is guaranteed by Telefonica S.A. as disclosed in the notes to the financial statements. We paid specific attention to the areas of focus driven by the operations of Telefonica Europe B.V., as set out below.

As part of designing our audit, we determined materiality and assessed the risks of material misstatement in the financial statements. In particular, we considered where managing directors made important judgements, for example, in respect of significant accounting estimates that involved making assumptions and considering future events that are inherently uncertain. In the accounting policies section of the financial statements Telefonica Europe B.V. describes the areas of judgement in applying accounting policies and the key sources of estimation uncertainty. Given the significant estimation uncertainty and the related higher inherent risks of material misstatement in the valuation of the loans issued, we considered this matter as key audit matters as set out in the section 'Key audit matters' of this report. Furthermore, we identified the existence of the loans issued as 'Key audit matters' of the importance of existence for users of the financial statements.

As in all of our audits, we also addressed the risk of management override of internal controls, including evaluating whether there was evidence of bias by managing directors that may represent a risk of material misstatement due to fraud.

We ensured that the audit team included the appropriate skills and competences, which are needed for the audit of a finance company.

Materiality

The scope of our audit is influenced by the application of materiality, which is further explained in the section 'Our responsibilities for the audit of the financial statements'.

Based on our professional judgement we determined certain quantitative thresholds for materiality, including the overall materiality for the financial statements as a whole as set out below. These, together with qualitative considerations, helped us to determine the nature, timing and extent of our audit procedures on the individual financial statement line items and disclosures and to evaluate the effect of identified misstatements, both individually and in aggregate, on the financial statements as a whole and on our opinion.

Based on our professional judgement, we determined the materiality for the financial statements as a whole at € 111,000,000 (2018: € 120,000,000). As a basis for our judgement, we used 1% of total assets. We used total assets as the primary benchmark, a generally accepted auditing practice, based on our analysis of the information needs of the common stakeholders, of which we believe the shareholders and bondholders are the most important ones. Inherent to the nature of the Company's business, the amounts in the financial statements are large in proportion to the income statement line items personnel expenses, administrative expenses and taxation. Based on qualitative considerations we performed audit procedures on those income statement line items, applying a benchmark of 10% of the total of those expenses.

We also take misstatements and/or possible misstatements into account that, in our judgement, are material for qualitative reasons.

We agreed with the managing directors that we would report to them misstatements identified during our audit above € 5,550,000 (2018: € 5,700,000) as well as misstatements below that amount that, in our view, warranted reporting for qualitative reasons.

Key audit matters

Key audit matters are those matters that, in our professional judgement, were of most significance in the audit of the financial statements. We have communicated the key audit matters to the managing directors. The key audit matters are not a comprehensive reflection of all matters identified by our audit and that we discussed. In this section, we described the key audit matters and included a summary of the audit procedures we performed on those matters.

We addressed the key audit matters in the context of our audit of the financial statements as a whole, and in forming our opinion thereon. We do not provide separate opinions on these matters or on specific elements of the financial statements. Any comment or observation we made on the results of our procedures should be read in this context.

Due to the nature of Telefonica Europe B.V., key audit matters do not change significantly year over year. As compared to last year there have been no changes in key audit matters.

Key audit matter	***How our audit addressed the matter***
Valuation of the loans issued *Notes 2 and 3* We consider the valuation of the loans issued, as disclosed in notes 2 and 3 to the financial statements for a total amount of € 10,872,657,000, to be a key audit matter. This is because the managing directors have to identify objective evidence of impairment, which is very important and judgemental, and because of the possible material effect an impairment may have on the financial statements. The managing directors did not identify any objective evidence that a loan is impaired.	We performed the following procedures to test the managing directors' assessment of the expected credit loss to support the valuation of the loans issued to Telefonica S.A. group companies: • For the initial fair value calculation, we determined that the valuation methodology and model applied by Telefonica Europe B.V. are in accordance with the requirements of RJ 290. • We recalculated the amortised cost value based on the effective interest method. • We evaluated the financial position of the counterparties of loans and their ability to repay the notional and interest to Telefonica Europe B.V., by assessing observable data from rating agencies, developments in credit spreads, current financial data (such as recent financial information and cash flows) and other publicly available data and obtaining information from the group auditor. We found the managing directors' assessment to be sufficiently rigorous. Our procedures as set out above did not indicate material differences.

Key audit matter	*How our audit addressed the matter*
Existence of the loans issued *Notes 2 and 3* We consider the existence of the loans issued, as disclosed in notes 2 and 3 to the financial statements for a total amount of €10,872,657,000, to be a key audit matter. Significant auditor's attention is necessary because of the size of the loan portfolio and the importance of existence for users of the financial statements.	We performed the following procedures to support the existence of the loans issued to Telefonica S.A. group companies: • We confirmed the existence of the loans with the counterparties on a sample basis. • We validated the input of loan contracts in the managing directors' calculation of the amortised cost value. • We compared interest receipts with bank statements. Based on the procedures as set out above, we found no material differences.

Report on the other information included in the annual report

In addition to the financial statements and our auditor's report thereon, the annual report contains other information that consists of:

- the managing directors' report; and
- the other information pursuant to Part 9 of Book 2 of the Dutch Civil Code.

Based on the procedures performed as set out below, we conclude that the other information:

- is consistent with the financial statements and does not contain material misstatements;
- contains the information that is required by Part 9 of Book 2 of the Dutch Civil Code.

We have read the other information. Based on our knowledge and understanding obtained in our audit of the financial statements or otherwise, we have considered whether the other information contains material misstatements.

By performing our procedures, we comply with the requirements of Part 9 of Book 2 of the Dutch Civil Code and the Dutch Standard 720. The scope of such procedures was substantially less than the scope of those performed in our audit of the financial statements.

The managing directors are responsible for the preparation of the other information, including the directors' report and the other information in accordance with Part 9 of Book 2 of the Dutch Civil Code.

Report on other legal and regulatory requirements

Our appointment

We were appointed as auditors of Telefonica Europe B.V. following the passing of a resolution by the shareholders at the annual meeting held on 28 February 2017. Our appointment has been renewed annually by shareholders representing a total period of uninterrupted engagement appointment of three years.

No prohibited non-audit services

To the best of our knowledge and belief, we have not provided prohibited non-audit services as referred to in Article 5(1) of the European Regulation on specific requirements regarding statutory audit of public-interest entities.

Services rendered

The services, in addition to the audit, that we have provided to Telefonica Europe B.V. for the period to which our statutory audit relates, are disclosed in note 10 to the financial statements.

Responsibilities for the financial statements and the audit

Responsibilities of the managing directors

The managing directors are responsible for:

- the preparation and fair presentation of the financial statements in accordance with Part 9 of Book 2 of the Dutch Civil Code; and for
- such internal control as the managing directors determines is necessary to enable the preparation of the financial statements that are free from material misstatement, whether due to fraud or error.

As part of the preparation of the financial statements, the managing directors are responsible for assessing the Company's ability to continue as a going concern. Based on the financial reporting framework mentioned, the managing directors should prepare the financial statements using the going-concern basis of accounting unless the managing directors either intend to liquidate Telefonica Europe B.V. or to cease operations, or have no realistic alternative but to do so.
The managing directors should disclose events and circumstances that may cast significant doubt on the Company's ability to continue as a going concern in the financial statements.

Our responsibilities for the audit of the financial statements

Our responsibility is to plan and perform an audit engagement in a manner that allows us to obtain sufficient and appropriate audit evidence to provide a basis for our opinion. Our audit opinion aims to provide reasonable assurance about whether the financial statements are free from material misstatement. Reasonable assurance is a high but not absolute level of assurance, which makes it possible that we may not detect all misstatements. Misstatements may arise due to fraud or error. They are considered to be material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of the financial statements.

Materiality affects the nature, timing and extent of our audit procedures and the evaluation of the effect of identified misstatements on our opinion.

A more detailed description of our responsibilities is set out in the appendix to our report.

Rotterdam, 19 February 2020
PricewaterhouseCoopers Accountants N.V.

Original has been signed by M.P.A. Corver RA

Appendix to our auditor's report on the financial statements 2019 of Telefonica Europe B.V.

In addition to what is included in our auditor's report, we have further set out in this appendix our responsibilities for the audit of the financial statements and explained what an audit involves.

The auditor's responsibilities for the audit of the financial statements

We have exercised professional judgement and have maintained professional scepticism throughout the audit in accordance with Dutch Standards on Auditing, ethical requirements and independence requirements. Our objectives are to obtain reasonable assurance about whether due to fraud or error. Our audit consisted, among other things of the following:

- Identifying and assessing the risks of material misstatement of the financial statements, whether due to fraud or error, designing and performing audit procedures responsive to those risks, and obtaining audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the intentional override of internal control.
- Obtaining an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control.
- Evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the managing directors.
- Concluding on the appropriateness of the managing directors' use of the going-concern basis of accounting, and based on the audit evidence obtained, concluding whether a material uncertainty exists related to events and/or conditions that may cast significant doubt on the Company's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report and are made in the context of our opinion on the financial statements as a whole. However, future events or conditions may cause Telefonica Europe B.V. to cease to continue as a going concern.
- Evaluating the overall presentation, structure and content of the financial statements, including the disclosures, and evaluating whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

We communicate with the managing directors regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit. In this respect, we also issue an additional report to the audit committee in accordance with Article 11 of the EU Regulation on specific requirements regarding statutory audit of public-interest entities. The information included in this additional report is consistent with our audit opinion in this auditor's report.

We provide the managing directors with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

From the matters communicated with the managing directors, we determine those matters that were of most significance in the audit of the financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, not communicating the matter is in the public interest.

Telefonica Europe B.V.

RESPONSIBILITY STATEMENT FOR THE ANNUAL FINANCIAL REPORT

The undersigned, in their capacity of members of the Telefonica Europe B.V. Board of Directors hereby declare that, to their best of their knowledge, the financial statements for the year ended December 31, 2019, are prepared in accordance with the applicable set of accounting standards, give a true and fair view of the assets, liabilities, financial position and profit or loss of Telefónica Europe B.V. and the management report includes a fair review of the development and performance of the business and the position of Telefonica Europe B.V. together with a description of the principal risks and uncertainties that Telefonica Europe B.V. faces.

Amsterdam, February 19, 2020

/s/
C.D. Maroto Sobrado
Director

/s/
M.C. van der Sluijs-Plantz
Director

/s/
Mr. J. Campillo Díaz
Director

/s/
J.M. Hernández Rabbat
Director