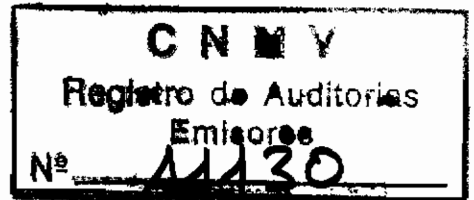
Acknowledgement of Independent Certified Public Accountants

We agree to the inclusion in Telefónica Finance USA, LLC's 2008 Financial Report of our report dated March 10, 2009, with respect to the financial statements of Telefónica Finance USA, LLC. We understand that the Financial Report and the Management Report will be filed with the Comisión Nacional del Mercado de Vaores.

Ernst & Young LLP

Ernst & Young LLP

Miami, Florida
April 15, 2009




# Management Report and Financial Statements

Telefónica Finance USA, L.L.C.
For the Years Ended December 31, 2008 and 2007
With Report of Independent Certified Public Accountants

0904-1049326

Telefónica Finance USA, L.L.C.

Management Report and Financial Statements

For the Years Ended December 31, 2008 and 2007

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# Management Report

# Management Report

## Telefonica Finance USA, L.L.C.
## (Delaware)

The Management herewith submits the Financial Statements of Telefonica Finance USA, L.L.C. (the Company) for the financial year ended December 31, 2008.

**Net income**

For 2008, the Company's net income totaled €97.887.039, which represents an increase over 2007 net income of €86.756.897, which is set out in detail in the accompanying Financial Statements.

As in previous years, during 2008 the sole income source of the Company is generated from the 2002 €2 billion Intercompany Loan Agreement signed with Telefonica Europe B.V. During 2008, the company generated interest income of €109.945.444, as compared to €98.814.555 for 2007.

Interest rates were generally higher during 2008 versus 2007. As a result, the Company obtained €11.130.889 in additional interest income during 2008 when compared to 2007.

There are no significant changes to report in comparison to the 2008 Profit and Loss Report. The Company's expenses come mainly from the paid fees of a liquidity agreement signed together with the underwriters of our preferred capital securities. The Company administrative expenses have increased by 5.75% totaling €59.425.

**Dividends payment**

€97.970.000 preferred dividends were paid during 2008. It represents an increase of 13.01% compared to 2007 preferred dividends payment. This increase has been possible due to our net income increase.

**Assets**

No relevant changes have been registered. At December 31, 2008 the €2 billion Loan remains the same outstanding amount as compared to 2007. No capital repayment has been done.

**Liabilities**

The minor decrease in our current liabilities it's due to a variation of the dividends payable which have decreased. The Company has not incurred in long term liabilities.

No significant variations have occurred in the Company's equity. A minor decrease (€18.405) in equity has occurred as a result of a retained earnings decrease.

**Risk Management**

Company operations have always been structured taking into account potential risk variables.

**Foreign Currency risk**

Since Company's functional currency is the Euro (EUR), and there aren't any significant foreign currency denominated financial assets or liabilities in the Balance Sheet, fluctuations in foreign exchange rates will not have a significant impact on our accounts.

**Interest Rate Risk**

The Company's preferred shares pay preferred dividends quarterly. These dividends are index to the 3 month-Euribor (European Interbank Offered Rate). Preferred shares were issued including a cap of 6,823% for the calculation of the dividend, as well as a floor on 4,184%. The Company also incorporated the same cap and floor on its Intercompany Loan Agreement, thus avoiding potential cash-flow mismatches with respect to interest rates fluctuations. The Intercompany Loan Agreement earns interest based on the 3-month Euribor plus a margin (0,603%) and is subject to a cap and floor as previously mentioned.

**Future developments**

No significant variation of granted loans or outstanding liabilities is expected.

There are no plans for any new intercompany loans, but it could change during 2009 fiscal year attending to the Telefonica's group financing needs. Telefonica Finance USA, L.L.C. is a wholly owned subsidiary of Telefonica Europe B.V. which, in turn, is a wholly owned subsidiary of Telefonica, S.A.

Delaware, April 15, 2009

# Financial Statements with Report of Independent Certified Public Accountants

0904-1049326

ERNST & YOUNG

Ernst & Young LLP
201 South Biscayne Blvd.
Suite 3000
Miami, Florida 33131-4330

Main tel: +1 305 358 4111
Direct fax: +1 305 415 1424
www.ey.com

# Report of Independent Certified Public Accountants

The Board of Trustees and Securityholders
Telefónica Finance USA, L.L.C.

We have audited the accompanying balance sheets of Telefónica Finance USA, L.L.C. (the Company), as of December 31, 2008 and 2007, and the related statements of operations and retained earnings and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing 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 over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Telefónica Finance USA, L.L.C. at December 31, 2008 and 2007, and the results of its operations and its cash flows for the years then ended, in conformity with U.S. generally accepted accounting principles.

Ernst + Young LLP

March 10, 2009

0904-1049326



A member firm of Ernst & Young Global Limited

Telefónica Finance USA, L.L.C.

Balance Sheets

| | | December 31 | |
|---|---|---|---|
| | | **2008** | **2007** |
| **Assets** | | | |
| Current assets: | | | |
| Cash | | **€ 18,671** | € 36,832 |
| Accrued interest receivable | | **531,889** | 596,444 |
| Total current assets | | **550,560** | 633,276 |
| | | | |
| Loan to Telefónica Europe B.V. | Note 3 | **2,000,000,000** | 2,000,000,000 |
| Total assets | | **€ 2,000,550,560** | € 2,000,633,276 |
| | | | |
| **Liabilities and stockholders' equity** | | | |
| Current liabilities: | | | |
| Accounts payable | | **€ 4,487** | € 4,241 |
| Notes payable | | **12,000** | 12,000 |
| Preferred dividends payable | | **464,889** | 529,444 |
| Liquidity fee payable | | **66,661** | 66,663 |
| Total current liabilities | | **548,037** | 612,348 |
| | | | |
| Stockholders' equity: | | | |
| Common capital | Note 4 | **95** | 95 |
| Preferred shares | Note 5 | **2,000,000,000** | 2,000,000,000 |
| Retained earnings | | **2,428** | 20,833 |
| Total stockholders' equity | | **2,000,002,523** | 2,000,020,928 |
| Total liabilities and stockholders' equity | | **€ 2,000,550,560** | € 2,000,633,276 |

*See accompanying notes.*

Telefónica Finance USA, L.L.C.

Statements of Operations and Retained Earnings

| | Years Ended December 31 | |
|---|---|---|
| | **2008** | **2007** |
| Revenues: | | |
| Interest income | **€ 109,945,444** | € 98,814,555 |
| Operating expenses: | | |
| Liquidity fee | **12,000,000** | 12,000,000 |
| Administrative expenses | **59,425** | 56,192 |
| Total operating expenses | **12,059,425** | 12,056,192 |
| Other expense: | | |
| Gain (loss) on currency exchange | **1,020** | (1,466) |
| Net income | **97,887,039** | 86,756,897 |
| Preferred dividends | **(97,905,444)** | (86,754,555) |
| Net (loss) income attributable to common securityholder | **(18,405)** | 2,342 |
| Retained earnings – beginning of year | **20,833** | 18,491 |
| Retained earnings – end of year | **€ 2,428** | € 20,833 |

*See accompanying notes.*

Telefónica Finance USA, L.L.C.

Statements of Cash Flows

| | Years Ended December 31 | |
|---|---|---|
| | **2008** | **2007** |
| **Operating activities** | | |
| Net income | **€ 97,887,039** | € 86,756,897 |
| Adjustments to reconcile net income to cash provided by operations: | | |
| Changes in operating assets and liabilities: | | |
| Decrease (increase) in accrued interest receivable | **64,555** | (64,555) |
| Increase (decrease) in payables | **245** | (501) |
| Cash provided by operating activities | **97,951,839** | 86,691,841 |
| **Financing activities** | | |
| Payment of preferred dividends | **(97,970,000)** | (86,690,000) |
| Cash used in financing activities | **(97,970,000)** | (86,690,000) |
| (Decrease) increase in cash | **(18,161)** | 1,841 |
| Cash – beginning of year | **36,832** | 34,991 |
| Cash – end of year | **€ 18,671** | € 36,832 |
| **Supplemental disclosure of noncash financing activities** | | |
| Accrued dividends on preferred capital securities | **€ (64,555)** | € 64,555 |

*See accompanying notes.*

Telefónica Finance USA, L.L.C.

Notes to the Financial Statements

December 31, 2008

## 1. General

Telefónica Finance USA, L.L.C. (the Company) was formed under the laws of the State of Delaware on June 27, 2002. The Company commenced operations on December 30, 2002. The Company is a wholly owned subsidiary of Telefónica Europe B.V. (Telefónica Europe) which, in turn, is a wholly owned subsidiary of Telefónica, S.A. (Telefónica). Telefónica is a Spanish corporation that operates in the telecommunications, internet, and media businesses. The Company was established for the purpose of issuing preferred capital securities and common capital securities and to use substantially all of the proceeds thereof to enter into loan agreements with Telefónica Europe or other non-U.S. affiliates of Telefónica.

## 2. Summary of Significant Accounting Policies

The Company's functional currency is the Euro. The following summarizes the significant accounting policies:

***Cash***—Cash represents cash with original maturities of three months or less.

***Revenue Recognition***—Interest income is recognized as earned, based upon the principal amount outstanding on an accrual basis.

***Fair Value of Financial Instruments***—Presented below is a brief summary of the significant management estimates relating to the fair value of financial instruments:

***Cash***—The recorded amounts of cash approximate fair value due to the short-term nature of these instruments.

***Loan to Telefónica Europe B. V.***—The estimated fair value for the loan receivable, which is separately disclosed elsewhere, is based on directly or indirectly observable market based inputs used in models or other valuation methodologies.

## 2. Summary of Significant Accounting Policies (continued)

***Estimates and Assumptions***—Preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect amounts reported in the financial statements and related notes. Actual results may differ from those estimates.

***Income Taxes***—The Company is a partnership for federal income tax purposes. As such, the income tax effects of the results of operations of the Company accrue directly to the owners. Accordingly, the accompanying financial statements do not include any effects for income taxes.

***New Accounting Pronouncements***—In September 2006, the Financial Accounting Standards Board (FASB) issued SFAS No. 157, *Fair Value Measurements* (SFAS No. 157). SFAS No. 157 defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles and expands disclosures about fair value measurements. SFAS No. 157 is effective for the Company on January 1, 2008.

Effective January 1, 2008, the Company adopted Statement of Financial Accounting Standards (SFAS) No. 157, "Fair Value Measurements" (SFAS No. 157) to measure the fair value of our financial assets and financial liabilities. SFAS No. 157 defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

SFAS No. 157 establishes a fair value hierarchy that distinguishes between (1) market participant assumptions developed based on market data obtained from independent sources (observable inputs) and (2) an entity's own assumptions about market participant assumptions developed based on the best information available in the circumstances (unobservable inputs). The fair value hierarchy consists of three broad levels, which gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1) and the lowest priority to unobservable inputs (Level 3). The three levels of the fair value hierarchy under SFAS No. 157 are described below:

Level 1: Quoted prices (unadjusted) in active markets for identical assets or liabilities. The Company used Level 1 assumptions for our cash. The valuations are based on quoted prices that are readily and regularly available in an active market, and accordingly, a significant degree of judgment is not required.

## 2. Summary of Significant Accounting Policies (continued)

Level 2: Directly or indirectly observable market based inputs used in models or other valuation methodologies. The Company used Level 2 assumptions for the valuation of our loan receivable, using directly or indirectly observable market based inputs used in models or other valuation methodologies. These inputs include interest rates, yield curves, credit risk and liquidity risk.

Level 3: Unobservable inputs that are supported by little or no market data and require the use of significant management judgment. As of December 31, 2008, we did not have any Level 3 financial assets or liabilities.

The fair value in accordance with SFAS No. 157 as of December 31, 2008 was €2,097,140,447 compared to a carrying value of €2,000,000,000. This compares with a fair value as of December 31, 2007 of €1,984,413,896 compared to a carrying value of €2,000,000,000.

In February 2007, the Financial Accounting Standard Board (FASB) issued SFAS No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities – Including an amendment of FASB Statement No. 115*, which provides companies with an option to report selected financial assets and liabilities at their fair values. The objective is to improve financial reporting by providing entities with the opportunity to mitigate volatility in reported earnings caused by measuring related assets and liabilities differently without having to apply complex hedge accounting provisions. This Statement is expected to expand the use of fair value measurement, which is consistent with FASB's long-term measurement objectives for accounting for financial instruments. The company did not elect the fair value option under this standard.

## 3. Loan to Telefónica Europe B.V.

On December 30, 2002, the Company made a loan of €2 billion to Telefónica Europe in exchange for a promissory note. The note, which matures on December 30, 2012, bears interest at a rate equal to the three-month Euro Interbank Offered Rate (Euribor) plus a margin (0.603%), provided, however, that the three-month Euribor effective rate shall in no event be less than 4.184% or more than 6.823%. Interest shall be due and payable quarterly in arrears on March 30, June 30, September 30, and December 30. The effective interest rate of the loan was 4.787% as of December 30, 2008 and 5.389% as of December 30, 2007.

**4. Common Capital Securities**

The Company has issued 10 common capital securities to Telefónica Europe. Common capital securities are allocated 100% of all net losses of the Company (in the event such should occur) and all gains and losses resulting from the disposition of assets from the Company. The net profits of the Company are allocated to the preferred capital securities until the amount so allocated equals the amount of dividends declared for the year on the preferred capital securities. Any net profits in excess of the amount allocated to the preferred capital securities are allocated to the common capital securities.

**5. Preferred Capital Securities**

The Company is authorized to issue and sell preferred capital securities having an aggregate initial liquidation preference of €2 billion. This amount may be amended or restated by resolution of the Board of Directors. Holders of preferred capital securities are entitled to receive, when and if declared by the Board of Directors out of the Company's net profits, cash dividends that will be paid at such rates as will be determined by the Board of Directors prior to the first issuance of these securities. Dividends on the preferred capital securities are noncumulative.

Preferred capital securities possess no voting rights. However, in the event that the Company fails to pay dividends in full on the preferred capital securities (and the guarantor fails to make a corresponding payment under the guarantee) for five consecutive dividend periods, then the holders of the preferred capital securities have the right to alter the composition of the Board of Directors as prescribed in the Amended and Restated Limited Liability Company Agreement of the Company (the Agreement).

Preferred capital securities may not be sold or otherwise transferred to persons in the United States of America except pursuant to sales or other transfers that satisfy the requirements of Regulation S under the Securities Act of 1933 (the Securities Act) or that are otherwise exempt from the registration requirements of the Securities Act.

In the event of any voluntary or involuntary liquidation of the Company, the holders of the preferred capital securities will be entitled to receive out of the assets of the Company available for distribution to securityholders, an amount equal to the liquidation preference per preferred capital security, plus accrued and unpaid dividends thereon for the then-current dividend period, if any, to the date of liquidation. This distribution will occur before any distribution of assets is made to holders of common capital securities or any other class of securities ranking junior to the preferred capital securities.

## 5. Preferred Capital Securities (continued)

On December 30, 2002, the Company completed the issuance of two million preferred capital securities and received proceeds of €2 billion from the issuance. Preferred capital securityholders are entitled to receive dividends at a rate equal to the three-month Euribor effective rate, provided, however, that the three-month Euribor effective rate shall in no event be less than 4.184% or more than 6.823%. Dividends are payable quarterly in arrears on March 30, June 30, September 30, and December 30. The preferred capital securities shall not be redeemed by the Company prior to December 30, 2012, with the exception of certain tax-related events, as defined in the Agreement. In the event the preferred capital securities are not redeemed on December 30, 2012, preferred capital securityholders are entitled to receive dividends at a rate equal to the three-month Euribor rate plus an effective annual rate of 4%. All costs related to this transaction were incurred by Telefónica and will not be charged to the Company. Telefónica is the guarantor of these securities.

## 6. Liquidity Fee

In December 2002, the Company entered into a Contrato de Liquidez (the Liquidity Fee Agreement) with the underwriters of its preferred capital securities offering. Pursuant to the Liquidity Fee Agreement, the Company is committed to pay a quarterly liquidity fee of 0.15% of the outstanding principal amount of the preferred capital securities to certain financial institutions.

## 7. Related-Party Transactions

Pursuant to the Agreement, Telefónica Europe is responsible for, and will pay; substantially all expenses of the Company to the extent such expenses are not paid by the Company. The expenses covered by the Agreement include administrative and organization costs as well as any costs resulting from any litigation against the Company. Minimal expenses were paid on behalf of the Company in 2008 and 2007.

As discussed in Note 3, the Company's loan to Telefónica Europe B.V. is with a related party.

Puglisi & Associates, under the terms of a Vendor Agreement dated October 24, 2002, provides accounting, accounts payable, treasury functions, and related administrative functions for the Company. The related vendor fee amounts to $28,500 per year. Under the terms of a Lease Agreement dated October 24, 2002, Puglisi & Associates also provides office space to the

**7. Related-Party Transactions (continued)**

Company. The office lease expense amounts to $1,500 per year. Puglisi & Associates is a sole proprietorship owned by Donald J. Puglisi, who is a director of Telefónica Finance USA, LLC. The related director fee amounts to $6,000 per year.

Had the Company operated autonomously the financial position, results of operations, and cash flows may have differed from what is presented here in these financial statements.

**RESPONSABILITY STATEMENT TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED DECEMBER 31, 2008.**

*(Article 8.1.b. of Royal Decree 1.362/2007)*

The members of the Board of Directors of Telefónica Finance USA, L.L.C. hereby declare that, to the best of their knowledge:

(i) the Annual Financial Statements for the year ended December 31, 2008, approved at the meeting held on March 10, 2009, and 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 Finance USA, L.L.C.

(ii) the management report includes a fair review of the development and performance of the business and the position of Telefónica Finance USA, L.L.C. and the undertakings included in the consolidation taken as a whole, together with a description of the principal risks and uncertainties that Telefónica Finance USA, L.L.C. faces.

On April 20, 2009

Mr. Fernando Rodríguez Álvarez-Cantón
**Director of Telefónica Finance USA, L.L.C.**

Mr. Donald J.Puglisi
**Director of Telefónica Finance USA, L.L.C.**