Risk Management Policy

Approved by the ExCom of the Telefonica Group in June 2008.

Telefónica, S.A.

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1. Introduction

Risks are inherent in all business and company activities. Effective risk management contributes both to value creation and to the development of the business through an appropriate balance between growth, performance and risk; while allowing for the identification of opportunities.

In accordance with the COSO ERM 2017[1] framework, risk is defined as the possibility that events will occur and affect the achievement of strategy and business objectives. Likewise, risk management is defined as the culture, capabilities, and practices, integrated with strategy-setting and its performance, that organizations rely on to manage risk in creating, preserving, and realizing value.

In accordance with the provisions of the references on the management and governance of Telefónica, S.A. (hereinafter, Telefónica or the Company or the Company), such as the Bylaws, the Regulations of the Board of Directors and the Responsible Business Principles[2], and with the aim of managing risks efficiently, this Policy establishes the principles for the identification, evaluation, management and reporting of risks that could affect the achievement of the main objectives and strategy of the Group, as well as of the companies that comprise it.

2. Scope

This Policy is global in scope and of direct and mandatory application to all the companies of the Telefónica Group without prejudice to the particularities derived from the legislation applicable to each one of them. For this purpose, the Telefónica Group shall be understood as those companies in whose share capital Telefónica has, directly or indirectly, the majority of the shares, participations or voting rights, or in whose administrative body it has appointed or has the power to appoint the majority of its members, in such a way that it controls the company effectively.

The different Telefónica Group Companies, together with their management bodies, may adapt the provisions of this Policy to their own reality, as well as to the local legislation applicable in each of the countries in which the Telefónica Group operates.

Telefónica, S.A., in its capacity as parent company of the Group, is responsible for establishing the bases, instruments and mechanisms required for proper and efficient coordination between this Company and the other companies which make up the Group. All without detriment to or any decrease of the capability of autonomous decisions corresponding to each of these Companies, in accordance with the social interest of each one of them and the fiduciary duties the members of its management bodies maintain towards all their stakeholders.

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[1] COSO ERM Framework, Enterprise Risk Management - Integrating with Strategy and Performance, published in September 2017 by the Committee of Sponsoring Organisations of the Treadway Commission (COSO). COSO is one of the most important references on internal control, enterprise risk management and fraud deterrence.

2 The responsible business principle on "Internal Control and Risk Management" states that "we have laid down appropriate controls to evaluate and manage all relevant risks for Telefónica".

3. Risk Management Principles

The basic principles that guide Telefonica’s risk management are as follows:

- Train and involve employees in the risk management culture, encouraging them to identify risks and actively participate in their mitigation.

- Automating and structuring the risk management activities and processes in a methodical way, throughout the organization.

- Facilitate the identification, assessment and management of the following risk categories:

    - Business: risks related to the sector and especially to the company's strategy, such as the evolution of competition and market consolidation, the regulatory framework, the supply chain, technological innovation, data privacy, adaptation to changing customer demands and/or the development of new ethical or social standards.

    - Operational: risks related to cybersecurity, climate change, natural disasters and other factors that may cause physical damage to our technical infrastructure that may cause network failure, service interruptions or loss of quality; customer-related risks; people-related risks, as well as operational management.

    - Financial: risks arising from adverse movements in the economic environment or financial variables, and from the company's ability to meet its commitments, make its assets liquid and have the financing capacity to carry out the business plan, including fiscal issues.

    - Legal and Regulatory Compliance: risks related to litigation and regulatory compliance, including anti-corruption legislation; as well as compliance with legal obligations and the Company's own environmental, social and governance (ESG) objectives.

4. Risk Management Framework

The Corporate Risk Management Framework is based on the COSO framework (Committee of Sponsoring Organizations of the Treadway Commission) and aligned with the best international practices.

Telefónica's Risk Management is also aligned with the Company's strategy, in accordance with the requirements of the COSO ERM 2017 framework.

The main objectives of the Telefónica Risk Management Framework are the following:

- Identify and assess risks both from a global Group perspective and from a specific perspective (in its main operations).
- Define and supervise a reasonable response to risks.

- Having information on the main risks and their management. Efficient risk management is a key component of the internal control system and supports the organization's commitment to its shareholders, customers and society in general.

The risk management process takes the company's strategy and objectives as the starting point for identifying the main risks that could affect their achievement. Once identified, the risks are assessed qualitatively and/or quantitatively in order to prioritize the monitoring and response to them, either through mitigation plans or actions to avoid or transfer these risks.

As part of the risk management process, significant risks are reported on the basis of their impact and probability, both globally and locally, in the Group's main operations. This information on the main risks facilitates:

- Complete the risk reports that must be reported internally or externally.
- Guide the action and management against risk: through global and/or specific response actions, both those coordinated globally from the respective corporate or transversal areas, as well as specific actions of the directly affected operations.
- Prioritize the activities of Internal Audit, in regard to its planning of activities for the supervision of the internal control structures.

5. Roles and responsibilities

All people within the organization have a responsibility to contribute to risk management, which entails embedding risk management into the organisation and into each individual's job description and accountabilities. In order to coordinate these activities, the following roles and responsibilities are distributed in relation to risk management:

5.1 Supervision of the risk management system

The Regulations of the Board of Directors of the Company establish that the primary duty of the Audit and Control Committee of Telefónica (ACC) shall be to support the Board of Directors in its supervisory duties, including the following competencies, among others:

- To supervise the effectiveness of the systems for the control and management of financial and non-financial risks relating to the Company and the Group (including operational, technological, legal, social, environmental, political and reputational risks and corruption-related risks).

  In that regard, it shall be responsible for proposing to the Board of Directors a risk control and management policy, which shall identify at least the following:

  a) the types of financial (including contingent liabilities and other off-balance sheet risks) and non-financial (operational, technological, legal, social, environmental, political and reputational, including corruption-related) risks to which the Company is exposed;

b) a multi-level risk control and management model;

c) the setting of the risk level that the Company deems acceptable; the

d) measures contemplated to mitigate the impact of identified risks, should they materialize; and

e) the internal control and information systems to be used to control and manage the above-mentioned risks.

- Supervise the risk control and management unit, which shall perform the following duties:

  a) ensure the proper operation of the risk control and management systems, and particularly to ensure that all material risks affecting the Company are identified, managed and quantified

  b) actively participate in preparing the risk strategy and in important decisions regarding the management thereof; and

  c) endeavor to ensure that the risk control and management systems properly mitigate risks within the framework of the policy determined by the Board of Directors.

In this regard, to support the development of these supervisory activities by the Audit and Control Committee, a risk management function has been established within the Internal Audit area, independent of management, which has a global structure and local managers in the main companies, in order to promote, support, coordinate and verify the application of the provisions of this Policy both at Group level and in its main operations, also assisting the Audit and Control Committee in any matters it may require. To that end, this function shall perform the following activities:

- Coordinate and standardize the methodologies for identifying, assessing and reporting risks in the Telefónica Group, including the preparation of the Corporate Risk Management Procedure.
- Supervise the procedures and functions involved in risk management.
- Analyze and aggregate the risk reports, in coordination with the management areas accountable for the risks, obtaining the risk information for its submission to the relevant decision-making bodies: Executive Committees and Audit and Control Committee, at least annually.
- Channel to the Audit and Control Committee all issues related to the risk management system, its execution and implementation.
- Foster the risk management culture within the Group.
- Work together with the corporate areas in the preparation of the public reports of the Company, related to risks.

The risk management function does not own the risks nor assumes any responsibility for the risk management, mission entrusted to the areas responsible for the risks.

5.2 Risk owners

Risk owners are actively involved in the risk strategy and major risk management decisions. To this end, each of the identified risks will be assigned a risk owner (usually senior management) with overall responsibility for the risk and its management, developing a plan for its mitigation and effectively monitoring its evolution. In the event that the controls or mitigation plans relating to that risk fall outside its scope, the role of the risk owner will be to identify the person responsible for that control or mitigation plan and to oversee that it is designed and operates effectively.

The management areas at global level (Global Group areas) and local level (Operating Businesses - OBs) are responsible for:

- Identify the main risks, both from a Group's perspective (top-down) and from a specific perspective of the main OBs that compose the Group (bottom-up).
- Assess the risks, considering both their likelihood and qualitative and quantitative impact, suppported by indicators, metrics, trends, future outlook, level of assurance and any additional element that may help to prioritize risks. In assessing the potential impact of risks, both economic, compliance, reputational, and environmental, social and governance (ESG) impacts are considered.
- Establish mitigation actions against risks, considering both global actions and those defined locally by the Group's operating businesses.
- Monitor the evolution of the risks and the action plans to mitigate them.

The information on the main risks and the determination of the broad outlines of the strategy and response to them shall be validated, at least annually, by the Executive Committees of the Group operating businesses (OBs).

6. Acceptable risk level

The acceptable risk level is defined as the level of exposure the Company is willing to assume insofar as it enables the value creation, getting the suitable balance between growth, performance and risk. According to this, risk management, applied to the strategy set-up, helps the Company management to select a consequent strategy with its acceptable risk level.

7. Effective date and development of this policy.

This new version of the policy will enter into force after its approval by the Board of Directors of Telefónica SA., and it is developed through the Corporate Risk Management Manual and those remaining rules of the Group, whose subject or content is related to risk management.

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