

Solvency and Financial Condition Report

(for the financial year ended 31 December 2019)

Telefónica Insurance S.A.

Approved by the Governance Board of Telefónica Insurance S.A.
29 May 2020

INDEX

SUMMARY

A. BUSINESS AND PERFORMANCE

- A.1 BUSINESS
- A.2 UNDERWRITING PERFORMANCE
- A.3 INVESTMENT PERFORMANCE
- A.4 PERFORMANCE OF OTHER ACTIVITIES
- A.5 ANY OTHER INFORMATION

B. SYSTEM OF GOVERNANCE

- B.1 GENERAL INFORMATION ON THE SYSTEM OF GOVERNANCE
- B.2 FIT AND PROPER REQUIREMENTS
- B.3 RISK MANAGEMENT SYSTEM INCLUDING THE OWN RISK AND SOLVENCY ASSESSMENT
- B.4 INTERNAL CONTROL SYSTEM
- B.5 INTERNAL AUDIT FUNCTION
- B.6 ACTUARIAL FUNCTION
- B.7 OUTSOURCING
- B.8 ANY OTHER INFORMATION

C. RISK PROFILE

- C.1 UNDERWRITING RISK
- C.2 MARKET RISK
- C.3 CREDIT RISK
- C.4 LIQUIDITY RISK
- C.5 OPERATIONAL RISK
- C.6 OTHER MATERIAL RISKS
- C.7 ANY OTHER INFORMATION

D. VALUATION FOR SOLVENCY PURPOSES

- D.1 ASSETS
- D.2 TECHNICAL PROVISIONS
- D.3 OTHER LIABILITIES
- D.4 ALTERNATIVE METHODS FOR VALUATION

E. CAPITAL MANAGEMENT

- E.1 OWN FUNDS
- E.2 SOLVENCY CAPITAL REQUIREMENTS AND MINIMUM CAPITAL REQUIREMENT
- E.3 USE OF THE DURATION-BASED EQUITY RISK SUB-MODULE IN THE CALCULATION OF THE SOLVENCY CAPITAL REQUIREMENT
- E.4 DIFFERENCES BETWEEN THE STANDARD FORMULA AND ANY INTERNAL MODEL USED
- E.5 NON-COMPLIANCE WITH THE MINIMUM CAPITAL REQUIREMENT AND NON-COMPLIANCE WITH THE SOLVENCY CAPITAL REQUIREMENT

SUMMARY

The new regulatory regime for Insurance and Reinsurance undertakings in the European Union, known as Solvency II, came into force with effect from 1 January 2016. This new legal framework is defined on the Directives 2009/138/EC and 2014/51/EU and its corresponding Delegated Acts and related regulation and its transposition into national law.

The regime requires new reporting and public disclosure arrangements to be put in place by insurers and some of that is subject to public disclosure. This document is the first version of the Solvency and Financial Condition Report (“SFCR”) for the year 2018 for Telefónica Insurance S.A. (hereafter “Telefónica Insurance” or ‘the Company’). This document is available to general public on the Company’s website.

For insurance companies regulated by the Commisariat Aux Assurances of Luxembourg, the Solvency and Financial Condition Report is produced in accordance with Article 82 of the “ Loi du 7 Decembre 2015 sur le Secteur des Assurances”, Articles 290 to 303 of the Commission Delegated Regulation (EU) 2015/35 and the EIOPA guidelines on reporting and public disclosure (B05-15-109).

This report covers the Business and Performance of the Company, its System of Governance, Risk Profile, Valuation for Solvency Purposes and Capital Management.

The ultimate Administrative Body that has the responsibility for all of these matters is the Company’s Board of Directors. The Board of Directors of Telefónica Insurance has set up various executive and supervisory bodies and control functions to ensure full compliance with the requirements of Solvency II legal framework

The Company’s financial year runs to 31 December each year and it reports its results in Euros.

A. BUSINESS AND PERFORMANCE

A.1 BUSINESS

Telefonica Insurance S.A., was constituted in Luxembourg in December 15th 2004 as a public liability company and registered at the “Registre de Commerce et des Sociétés de Luxembourg” at section B, with number 105162. The company initially named Altaïr Assurances S.A. changed its name to Telefónica Insurance S.A. in December 2011.

The object of the company is to undertake insurance and reinsurance operations for all type of risks excluded Life Insurance. Telefónica Insurance S.A. is authorized and regulated by the Commisariat Aux Assurances domiciled at 7 boulevard Joseph II à Luxembourg L-1840.

The company’s Head Office is domiciled at 23, Avenue Monterey L-2163. Telefónica Insurance passports activities and operates in Spain, UK and Germany through to its branches located at,

- United Kingdom: Telefónica Insurance S.A. UK Branch 260 Bath Road, Slough, Berks SL1 4DX Registered in UK No. FC029774; BR014757. The Company is regulated by the Financial Conduct Authority for the conduct of business in the UK. FCA reference number 430933.

On 11 January 2019 the Prudential Regulation Authority at the Bank of England (PRA) confirmed that Telefonica Insurance S.A. had notified of its entry into the Temporary Permissions Regime (TPR) if the UK leaves the EU without an implementation period. The PRA considers that Telefonica Insurance S.A. (the ‘Firm’) has notified the PRA, in accordance with the direction made by the PRA under regulation 14(2) of the EEA Passport Rights (Amendment, etc., and Transitional Provisions) (EU Exit) Regulations 2018 (the “TPR Regulations”), that the Firm wishes to be treated in accordance with regulation 8 of the TPR Regulations. The PRA therefore confirms that regulation 8 is to apply to the Firm. The TPR Regulations provide that regulation 8 will apply for a period beginning at exit day (11pm on 29 March 2019 or any other agreed later). During the period that regulation 8 applies the Firm will be treated as if it has permission under Part 4A of the Financial Services and Markets Act 2000 (the “2000 Act”) to carry on in the United Kingdom the regulated activities which, immediately before exit day, the Firm is authorized to carry on in the United Kingdom by virtue of section 31(1)(b) or (c) of that Act.

- Germany: Telefónica Insurance S.A. Direktion für Deutschland. Georg-Brauchle-Ring 23-25 80992 München. HRB Nr. 198 107. The Company is regulated by the BaFin for the conduct of business in Germany.
- Spain: Telefónica Seguros Sucral en España. Distrito Telefónica Ronda de la Comunicación s/n 28050 Madrid. The Company is regulated by the Dirección General de Seguros for the conduct of business in Spain. N° Registro: E0206

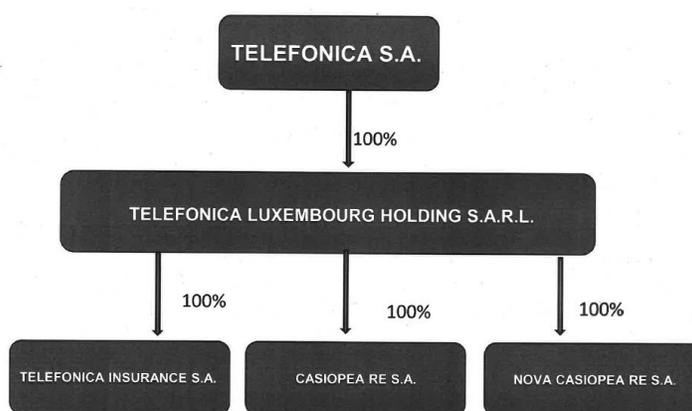
The company is as well authorized to operate from Luxembourg in the European Union under the provision of freedom of services.

The appointed auditor of the company is Price Waterhouse Coopers, Société Cooperative, domiciled 2 rue Gerhard Mercator, Luxembourg L-1014. The annual accounts of Telefónica Insurance are included in the

financial statements accounts of Telefónica S.A., the parent company of Telefónica Group, domiciled at Gran Vía 28, 28013 Madrid, Spain.

Telefónica Insurance makes part of Telefónica Group, a diversified telecommunications group which provides a comprehensive range of digital services through one of the world largest and most modern telecommunications networks, focused on providing telecommunications services with presence principally in Europe and Latin America.

The shareholding structure of the company is described on the following graph,



Telefónica Insurance S.A. commits to offer innovative insurance policies, linked to telecommunication and digital services provided by Telefónica Group. The company is specialized in device insurance, holding around 1.5 million mobile phones and tablets insured in Europe. The company also participates in Telefónica Group Risk Management, underwriting insurance policies to cover Group subsidiaries domiciled in the European Union.

Telefonica Insurance business principles aim to set, encourage and sustain high standards of corporate responsibility in everything the company does across its operations, including promoting and ensuring good product standards. Telefonica Insurance believes that this not only makes business sense, it also has the potential to place the customer at the core, aiming to deliver services and solutions that achieve their utmost satisfaction and contributes to sustainable development.

Telefónica Insurance has a series of general principles based on: honesty, integrity, trust and respect for the law that defines the way in which the company undertakes its activities and its relations. Telefónica Insurance strongly respects and supports the principles of the UN Universal Declaration of Human Rights, as well as the declarations of the International Labor Organization, and we do not tolerate, either directly or indirectly, any type of child labor, forced labor, threats, coercion, abuse, violence or intimidation in its work environment.

A.2 UNDERWRITING PERFORMANCE

Telefónica Insurance main line of business is the device insurance (hereinafter also named as MPI) defined as an insurance product that covers certain insured events arising in relation to mobile phones and tablets. MPI provides coverage against some kind of damage (loss, theft, physical damage, etc.) of mobile phones. It commonly covers eventualities that are not already covered by the guarantee of the mobile phone device. The company predominantly sells products through Telefónica Group mobile phone operators.

In 2019, the company continued to develop satisfactorily its underwriting activities on MPI. The number of clients reached by 31 December 2019 around 1.5 million insurance policies.

The image below shows the geographical distribution of the device insurance policies across Europe as of December 31 2019.



Further to the MPI, the Company underwrites under the provision of freedom of services two policies covering the operations of Telefónica Group companies in Spain and the United Kingdom on the branches of Fire and Miscellaneous

The volume of premiums issued by the Company reached 156.627.515 Euros, which represents a decrease of 12% in comparison with the previous financial year (178.019.496 Euros). The following table presents the breakdown of Gross Written Premiums per country

| <i>Gross premiums written</i> | EUR |
|-------------------------------|-------------------|
| Germany | 29.272.202 |
| Spain | 29.650.464 |
| Suisse | 668.947 |
| UK | 97.035.902 |
| Total | <hr/> 156.627.515 |

For purpose of comparison the table below shows the same information for the financial year ended December 31st 2018,

| <i>Gross premiums written</i> | EUR |
|-------------------------------|-------------------|
| Germany | 36.771.180 |
| Spain | 36.767.071 |
| Ireland | 454.619 |
| UK | 104.026.625 |
| Total | <hr/> 178.019.496 |

The table below shows the allocation of the activity of insurance of the company by group of branches. It is worth to mention that around 99% of the Gross Written Premiums concentrates the Handset Insurance business which is fully allocated in the Miscellaneous Financial Losses branch.

| | Public liability | | Fire | Miscellaneous financial losses | Total |
|--------------------------|------------------|---------|-----------|--------------------------------|--------------|
| | Automobile | Other | EUR | EUR | EUR |
| | EUR | EUR | | | |
| Gross premiums written | | 672.783 | 111.990 | 155.842.742 | 156.627.515 |
| Gross premiums earned | | 672.783 | 110.725 | 156.910.505 | 157.694.013 |
| Gross claims incurred | 18.466 | 507.074 | (229.292) | 67.965.057 | 68.261.305 |
| Gross operating expenses | | 643.517 | 8.053 | 66.136.815 | 66.788.385 |
| Reinsurance's balance | --- | 137.262 | (386.916) | (16.013.359) | (16.263.013) |

For purpose of comparison the table below shows the same information for the financial year ended December 31st 2018,

| | Public liability Automobile EUR | Other EUR | Fire EUR | Miscellaneous financial losses EUR | Total EUR |
|--------------------------|---------------------------------------|--------------|-------------|--|--------------|
| Gross premiums written | 0 | 10.336 | 107.750 | 177.901.410 | 178.019.496 |
| Gross premiums earned | 62.797 | 74.401 | 107.546 | 178.264.381 | 178.509.124 |
| Gross claims incurred | 47.206 | 163.653 | 159.715 | 114.110.309 | 114.480.882 |
| Gross operating expenses | 5.920 | 7.379 | 7.546 | 67.271.707 | 67.292.552 |
| Reinsurance's balance | --- | (1.047.598) | (917.347) | (2.432.379) | (4.397.323) |

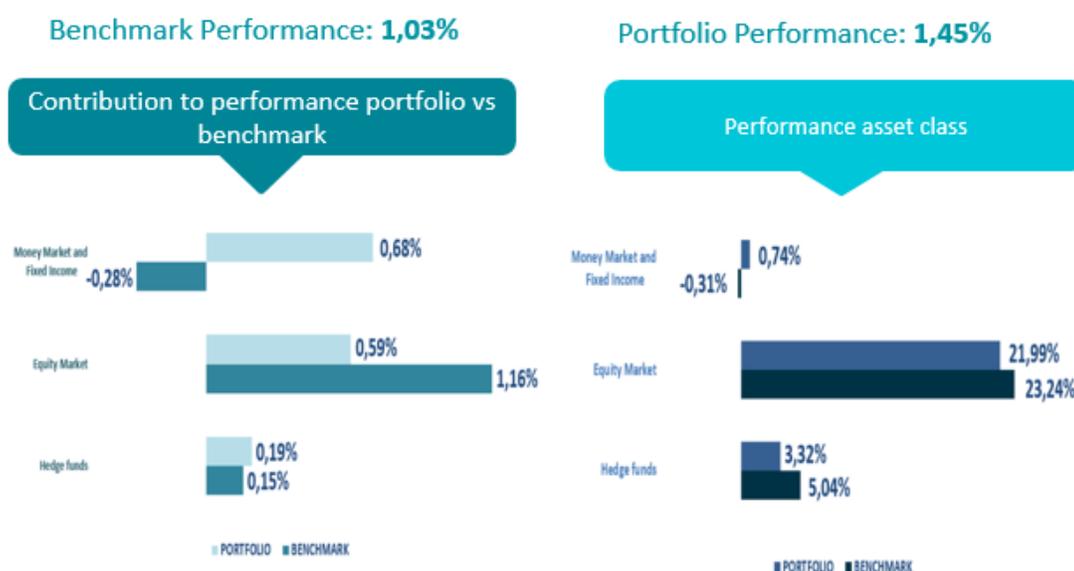
The balance on the technical account for non-life insurance amounted to Eur. 8.248.135 representing an increase of 27,8% with respect to 2018 balance Eur 6.452.442, following a significant improvement in terms of combined loss ratio which reached 82% compared to a 91% in 2018.

A.3 INVESTMENT PERFORMANCE

It was mostly a good year for investors around the world, as developed international and emerging markets strengthened. The MSCI World Index gained 24% last year. Bonds (9%), gold (18%), and oil (27%) all rebounded from declines in 2018

The company's investment policy aims to secure the financial assets and to deploy allocations over instruments offering limited volatility and risks and high liquidity. The investment in fixed income markets and money markets cannot be less than 90% of the total portfolio with a duration no higher than 2 years. On the other hand, the maximum investments in equity market is 10% and Hedge Funds investments cannot be greater than 5%. The sum of these asset classes (equity and HF) cannot exceed a 10% of the total portfolio of Telefónica Insurance. The graphs below show the performance per class of asset of the company compared to the benchmark for the financial year 2019.

Performance ytd benchmark vs portfolio (december 19)



Assets included under the item "Investments" are valued according to the following accounting principles,

| <i>Nature of investments</i> | <i>Method of evaluation</i> |
|--|-------------------------------------|
| Deposits with ceding undertakings | Nominal value |
| Shares and other variable income securities and units in unit trusts | Lower between cost and market value |
| Debt securities and other fixed income securities | Amortization of agios and disagios |

Debt securities and other fixed-income securities are recorded at acquisition cost. Where the acquisition cost exceeds the amount repayable at maturity the difference is charged to the profit and loss account in instalments over the period remaining until repayment. Where the acquisition cost is lower than the amount repayable at maturity the difference is released to the profit and loss account in instalments over the period remaining until repayment.

A.4 PERFORMANCE OF OTHER ACTIVITIES

No other activity was registered in 2019.

A.5 ANY OTHER INFORMATION

Other than as noted above, no other events occurred in 2019 which had a material impact on the business or performance.

Statement on COVID-19

Though the eventual impact of the COVID-19 (coronavirus) is difficult to predict at this time, and will depend on future events, highlighting among them the level of expansion and the severity of the virus and the effectiveness of both announced and already ongoing measures to contain its impact, we are periodically assessing its developments and potential effects in the going-concern of the company.

The company business profile is reliant on handset insurance sales. Whereas it is expected a decrease on commercial activity as a result of the crisis, underwriting performance of the company should not be significantly affected. The company has activated business continuity plans, including measures to mitigate disruptions on the supply chain in order to guarantee claims fulfillment and customer service.

This pandemic has led to widespread economic uncertainty and volatility in financial markets. The Board of Directors, through the Investment Committee of the company, monitors closely the evolution on the financial markets to mitigate the exposure of the investment portfolio of the company.

B. SYSTEM OF GOVERNANCE

B.1 GENERAL INFORMATION ON THE SYSTEM OF GOVERNANCE

Introduction

The objective of the Governance system is to ensure a healthy and prudent management. Its two guiding principles are effectiveness and proportionality under an Internal Control structure that ensures compliance with the regulations, the efficiency and effectiveness of operations and the availability and reliability of the financial and non-financial information. In order to achieve this, with reasonable safety, the following objectives are strategic; control, monitoring; operating; information and communication and compliance.

The Governance system of the Company is aligned with the European Insurance and Occupational Pensions Authority ("EIOPA") Guidelines.

Management and administration of the company

Telefónica Insurance has an organizational and operational structure which aims at supporting the strategic objectives and operations of the undertaking. The structure is formed by the supervisory, management and administration bodies of the company which are described below,

The General Shareholders meeting is the highest deliberative body of the Company, through which the corporate will is expressed and the shareholders exercise their right to participate in the Company's decision-making

The shareholders acting at the General Shareholders' Meeting have the power to deliberate upon and adopt resolutions on all such matters as legal provisions and the By-Laws reserve for decision thereat, and, in general, on all matters which fall within the scope of powers assigned by law to the shareholders and are submitted at the General Shareholders' Meeting at the behest of the Board of Directors and of the shareholders themselves, in such instances and in such manner as are provided in the law and the By-Laws

The Board of Directors is, as set forth in the Act and the Articles of Association, the highest Body of administration and representation of the Company. It thus being empowered to perform, within the scope covered by the corporate object defined in the Articles of Association, any acts or legal transactions of administration and disposal, by any juridical title, except for this reserved by the Act or the Articles of Association to the exclusive competence of the General Meeting of Shareholders. The powers reserved by the Law or the By-Laws exclusively to the Board of Directors, or any other powers required for the responsible exercise of its basic supervisory and controlling duties, may not be delegated. Specifically, the Board of Directors of the company approves the general policies and strategies of the Company, particularly:

- Strategic plans, management objectives and annual budget.
- Definition of the structure of the Group of Companies.
- Investment Policy
- Underwriting Plan
- Product Management Policy
- Corporate governance policy.

The Board of Directors organizes the execution of the policies and strategies of the Company, through the following bodies,

- The Executive Committee takes all relevant decisions pursuing the execution of the strategic plan of the company
- The Investment Committee is responsible for the management of the investment portfolio in compliance with the Investment Policy of the company
- The Governance Board is in charge of the overall governance of the company

This organization provides the Board of Directors greater efficiency in performing its duties, providing it the necessary support through the work it carries out and guaranteeing the appropriate segregation of duties and responsibilities.

The Executive Committee takes all relevant decisions pursuing the execution of the strategic plan of the company. The executives Committee meets monthly and is formed by

- Two members of the board
- The Authorized Manager
- The Head of Business Developments and Operations department
- The Head of Legal Affairs
- The Secretary of the board

The Investment Committee is responsible for the management of the investment portfolio in compliance with the Investment Policy of the company

- Two members of the board
- The Authorized Manager
- The Finance Manager

The Investment Committee meets quarterly. The Committee is responsible for the execution of the investment policy of the company. Among its functions is in charge of defining,

- The quantitative limits on assets and exposures, including off-balance sheet exposures, that need to be established to ensure the company complies with security, quality, liquidity, profitability and availability of its portfolio;
- The link between market risk and other risks in adverse scenarios;
- The liquidity risk management;
- The assessment of non-routine investment activities;
- The implementation and monitoring of control processes of the investment strategy of the company, either on regulated financial market or with complex products.

The Governance Board is in charge of the overall governance of the company and makes sure that the undertaking has a set of policies and procedures in place required by the Solvency II Directive. The Governance Board is formed by,

- Two members of the board
- The Authorized Manager
- A representative of Telefónica Group Corporate Risk and Insurance department
- The Head of Legal Affairs
- The Secretary of the Board of Directors

The governance board is responsible to assess the appropriate implementation of the key functions defined by the Solvency II Directive. The GB meets whenever it deems it advisable or appropriate to ensure a punctual follow-up of Solvency II Pillar 2 related matters, and in any case at least once a year. The functions and responsibilities are defined as follows,

- General governance requirements

- Interact with the senior management, the functional committees in place, the key functions of the undertaking by proactively asking information and challenging them when necessary.
- Assess the potential impact of changes in group structure on the entity and adjust the company in timely manner (when necessary)
- Gather adequate knowledge of the group structure, the links between the various entities and the business model in order to take appropriate decisions
- Involve at least two persons who effectively run the undertaking in the decision making process
- Appropriately document the decisions taken at the level of the GB and how information from the risk management system has been taken into account in this process
- Discuss and approve the internal review of the system of governance
- Make sure that the undertaking has a set of policies and procedures in place required by the Solvency II Directive

- Fit and proper.

Assure that the company has fit and proper procedures in place to assess the persons that effectively run the undertaking, key functions (including the key functions that have been outsourced) and the members of the GB

- Risk management

Bear the ultimate responsibility for ensuring the effectiveness of the risk management system, setting the undertaking's risk appetite and overall risk tolerance limits as well as approving the main risk management strategies and policies

- Own fund requirements

Monitor the medium-term capital plan

- Internal control,

Include the results and conclusions of the monitoring and reporting mechanisms of the internal control system in the decision making process

- Internal audit,

Review the annual internal audit report and take appropriate action to remedy the identified shortcomings. Refrain from influencing the internal audit function in order not to impair their independence and impartiality

- Actuarial Function,

Review the annual actuarial report and take appropriate action to remedy the identified deficiencies

- ORSA,

Take actively part in the development and maintenance of the ORSA model. Take into account the results and conclusions of the ORSA model in the decision making process.

The Control and Audit Committee

Pursuant to article 52 of the modified law of July 23rd, 2016 of the audit profession, the Board of Managers of the sole shareholder of Telefónica Insurance, Telefónica Luxembourg Holding S.à.r.l. set up on December 27th 2016 an Audit and Control Committee which also acts on behalf of the subsidiaries of the Company that is to say: CASIOPEA RE, NOVA CASIOPEA RE and TELEFONICA INSURANCE.

The primary duty of the Audit and Control Committee shall is to support the Board of Directors in its supervisory duties, in accordance with the provisions of law and the internal policies of Telefónica Group.

As regards the subsidiaries of the Company, that are deemed to be PIE (Public Interest Entities), which is the case of Telefónica Insurance S.A. as defined by applicable law, it performs all duties of the Audit Committee at any time contemplated by applicable law.

The Authorized Manager The representation of the company is granted by the Authorized Manager (Dirigeant Agréé). The Board of Directors has entrusted the Dirigeant Agréé the powers of representation and management to the extension established on the law.

Organizational chart Telefónica Insurance keeps an updated organizational chart at all the times. Following the requirements of Solvency II, this chart identifies the key functions and represents the responsibility of each area in relation with risk management and internal control system.

Documentation of decisions taken at the level of the Supervisory, Administration and Management bodies

Telefónica Insurance appropriately documents the decisions taken at the level of the Governance Board of the company and how information from the risk management system has been taken into account.

Internal review of the system of governance

Telefónica Insurance determines the scope and frequency of the internal reviews of the system of governance taking into account specificities of the entities (nature, scale, business complexity) at individual and at group level. The scope, findings and conclusions of the review is properly documented and reported to the Governance Board. Suitable feedback loops are necessary to ensure follow-up actions are undertaken and recorded.

Policies

Telefónica Insurance aligns all policies required as part of the system of governance with each other and with its business strategy. Each policy should at least set out:

- The goals pursued by the policy;
- The tasks to be performed and the person or role responsible for them;
- The processes and reporting procedures to be applied;
- The obligation of the relevant organizational units to inform the risk management, internal audit and the compliance and actuarial functions of any facts relevant for the performance of their duties.

The policies cover the key functions. Telefónica Insurance also addresses the position of these functions within the undertaking, their rights and power.

Key functions of the governance system

It corresponds to the operational structure of the governance system of identification processes that involve significant risks, their assessment and the establishment of way they have to run, including the responsibilities and information flows, with ensure adequate monitoring and control of them.

The basic functions of the governance system of Telefónica Insurance are,

- Risk management function;
- Compliance function;
- Internal audit function;
- Actuarial function.

Remuneration Policy

Telefónica Insurance remuneration policy is defined at Group level through the Telefónica Group compensation policies and procedures which ensures:

Remuneration arrangements with service providers do not encourage risk-taking that is excessive in view of the undertaking's risk management strategy.

Remuneration awards do not threaten the undertaking's ability to maintain an adequate capital base.

Telefónica Group ensures that the composition of the remuneration committee enables it to exercise a competent and independent judgment on the remuneration policy and its oversight.

B.2 FIT AND PROPER REQUIREMENTS

Telefónica Insurance S.A. has the procedures in place which ensure that individuals who effectively run the company or have other key functions (not limited to the four key functions mentioned in the Solvency II Directive), including members of the Board of Directors and all the executive and management bodies comply with the fit and proper requirements defined by Law.

The company takes account of the respective duties allocated to individual persons to ensure appropriate diversity of qualifications, knowledge and relevant experience so that the undertaking is managed and overseen in a professional manner. In short, fitness relates to professional competence.

Telefónica Insurance ensures that the members of the Board of Directors and the members of the executive and management bodies collectively possess qualification, experience and knowledge about at least the subjects below in order to be able to provide for sound and prudent management of the business:

- Insurance and financial markets
- Business strategy and business model
- System of governance
- Financial and actuarial analysis
- Regulatory framework requirements

When assessing whether an individual is 'proper', the company runs an assessment of that person's honesty and financial soundness based on relevant evidence regarding their character, personal behavior and business conduct including any criminal, financial and supervisory aspects regardless of jurisdiction. The proper requirement is phrased as a person being of good repute and integrity.

Telefónica Insurance keeps an updated register on the compliance with the fit and proper requirements which includes relevant records of all members of the board and the executive and management of the company. The register is regularly reviewed by the Governance Board who reports the status of the review to the Board of Directors.

B.3 RISK MANAGEMENT SYSTEM INCLUDING THE OWN RISK AND SOLVENCY ASSESSMENT

Telefónica Risk Management system is aligned with the principles defined on the Risk Management System of Telefónica Group. The Group Risk Management Framework is aligned with best practice in Internal Control (COSO1 II Report and Draft BS311002 Code of Practice for Risk Management) and develops Telefónica Group Business Principles regarding risk management. Furthermore, Good Corporate Governance recommendations regarding Risk Management have been taken into account. Telefónica S.A. and its operating businesses must have a process for the early identification, management and reporting of risks, with management accountability for risk identification and management in their business areas.

The risk management framework of Telefónica Insurance includes:

- The strategic decisions and policies on risk management
- The company's risk appetite and overall risk tolerance limits defined by the Governance Board
- The identification, measurement, management, monitoring and reporting of risks

The Governance Board is ultimately responsible for ensuring the effectiveness of the risk management system, setting the undertaking's risk appetite and overall risk tolerance limits as well as approving the main risk management strategies and policies, making sure that they are consistent with the company's structure, size and specificities. It also has to guarantee that the specific operations, which are material, and associated risks are covered. Finally, it should safeguard that an integrated, consistent and efficient risk management is put in place.

Telefónica Insurance has a process for the early identification, management & reporting of risks, with management accountability for risk identification and management in their business areas.

Risks are inherent in all business and company activities. The goal of this Policy is to manage risks in the most efficient way, always supporting and facilitating the achievement of the objectives of the company.

Effective risk management is not only a key component of the internal control system. It also supports and complements the achievement of business objectives and underpins the organizations commitment to shareholders and customers.

Telefónica Insurance has in place a risk management procedure, which contains the following elements:

- Risk categories and methods to measure the risks
- Outline of how the company will manage each risk category
- Risk tolerance limits within all risk categories in line with the company's risk appetite
- Reinsurance and other risk mitigation techniques
- Description of the connection with the solvency needs assessment (based on the company's ORSA)
- The content and frequency of regular stress tests
- Heat maps
- Annual reporting process
- Specific treatment of materialized risks

The Risk Management Procedure main output is the Risk Map of the company, which is updated at least once per year and reviewed and ratified by the Governance Board and the Board of Directors.

Own Risk Solvency Assessment

In accordance with Luxembourg Insurance Act “Loi 7/12/2015 sur le secteur des assurance” transposing Solvency 2 directive, Telefónica Insurance properly assesses own short and long term risks and the amount of funds necessary to cover them. This assessment, defined as ORSA (Own Risk Solvency Assessment) is approved by the management, administration and supervisory bodies of the company and reported to the regulator. The ORSA can be defined as “the entirety of the processes and procedures employed to identify, assess, monitor, manage, and report the short and long term risks a (re)insurance undertaking faces or may face and to determine the own funds necessary to ensure that the undertaking’s overall solvency needs are met at all times.”

The ORSA provides a prospective view (typically 3- to 5-years horizon, aligned with Business Plan) of the adequacy of its own funds to cover all risks it is or might be exposed to. It is updated every year (or in case of significant change in the business). The results of the ORSA and the underlying assumptions are documented in a specific report. The analysis covers the overall risk profile of the local entity (i.e. both those subject to SCR such as underwriting or market and any other relevant risk such as strategic reputation or liquidity). The ORSA is approved by the Board of Directors.

B.4 INTERNAL CONTROL SYSTEM

In line with the regulatory framework of Telefónica Group, Telefonica Insurance has implemented the internal control system which applies the following main principles,

- The application of Business Principles of the Telefónica Group.
- The application of General Controls: control environment, risk evaluation, information and communication, monitoring...
- The application of Specific Controls by Business Cycle: reviewed the processes impacting the financial information in view of compliance with the requirements of Section 404 of the Sarbanes-Oxley Act.

Within the policies and procedures of the Company the Internal Control System of the company establishes a control check point mechanism. Most significant check points cover the following aspects:

- Decision-making in the company.
- Payments made by the company to third parties, customers or employees.
- The reporting process variations in the company.
- Customer billing, group companies or third parties who cause damages or damage to the company.
- Conducting financial transactions.
- Situations of unfair competition and control in order to avoid irregular activities

As a relevant part of the Internal Control, the Company has set up the compliance function. Its primary mission is to ensure that the Company, in the development of its activities, respects and complies with the relevant legislation and regulations of the countries where it operates and to warn for the risk of normative weakness.

The scope of the Compliance Function of Telefónica Insurance is the following:

- Identify regulations and assess their impact on processes and procedures of the Company in the countries where it operates
- Advise all the bodies of the Company and guarantee compliance with laws, regulations, administrative dispositions and internal rules that have an effect on the development of the Company in the countries where it operates
- Identify, evaluate and assess the risk of non-compliance
- Assess the adequacy and efficiency of the organizational measures taken to mitigate the risk of failure and propose necessary changes to improve the risk review
- Monitor and evaluate the impact(s) of policy evolutions or changes in the legal environments on the Company in the countries where it operates
- Advise in launching new products or processes
- Prepare an annual report to the Board of Directors, which includes the result of the periodic reports required by sectorial legislation and summarizes the legal changes that have taken place in the countries where the Company operates

The Compliance prepares annually a report including a control check lists outlining the periodic reports required by general and sectorial legislation. The report is presented to the Governance Board and approved ultimately by the Board of Directors

B.5 INTERNAL AUDIT FUNCTION

Telefónica Insurance outsources the internal audit function to Telefónica Group Corporate Audit.

Telefónica, S.A. has a modern conception of internal audit, conceived as the body advising management on finding the best way to achieve greater efficiency by improving the policies, methods, processes and procedures organization. Internal Audit must act independently and without authority hierarchical or functional link with the audited units. The "Statute of the Corporate Internal Audit Function" defines "The Internal Audit shall appear on the organizational structure as a body under the General Secretariat hierarchically and functionally reporting to the Audit and Control Committee of Directors, who shall report the results of their work. It will not have any hierarchical or functional link with the audited units ..."

The priority objective of Internal Audit will be to facilitate support to the Board of Directors and the Directorate in their responsibilities related to the assurance of governance, risk management and the internal control system of the Group and of its Companies. Internal Control consists of all those processes that reasonably guarantee:

- The compliance with laws, regulations and internal norms,
- The reliability of the information,
- The efficacy and efficiency of operations,
- The integrity of the company's assets.

Every year the Audit and Control Committee will approve a Work Plan for the Corporate Internal Audit Directorate, considering the strategy of the Telefónica Group as a digital telco. This will include, among others, the following responsibilities:

- Develop an annual internal audit work plan for the Telefónica Group that takes into consideration new businesses and the evolution of the Digital area, using an adequate methodology based on risks assessment, in order to define the priorities of the internal audit activity.
- Periodic review of the different functions and Companies of the Group in order to ensure that the internal regulations and procedures (of management, of the organization and of quality) approved by the Directorate are being complied with, and that the said functions are being performed in an effective and efficient manner.

- Verification and analysis of the correction of accounting and operating Internal Control Systems.
- Review of the controls designed for the protection of the Group companies' assets.
- Identification of the problems and opportunities for improvement in the course of the operational audit reviews performed.
- Verification of the existence of adequate controls in the information systems.
- Review of observance of internal corporate governance regulations and the Code of Ethics of the Group.
- Perform consulting services required by the Directorate and included in the function of internal auditing activity, in accordance with "International Standards for the Professional Practice of Internal Auditing".
- And, at any time, and within the scope of internal auditing functions, those other timely matters/investigations of interest to the Board of Directors or to the Directorate: legal compliance, reports and demands (lawsuits, thefts, etc.), attending to the whistleblowing channel, analysis of vendors, clients, problems with fraud, etc.

The internal auditing activity will comply with the "International Standards for the Professional Practice of Internal Auditing", as well as its Code of Ethics. For this reason, internal auditors, additionally to their Company's Code of Ethics, will also observe the principles and rules of conduct which are compulsory to internal auditors, being these: Integrity, Objectivity, Confidentiality, and Diligence.

When auditing Telefónica Insurance S.A., the internal audit department will pay special attention to the policies and procedures listed in the Solvency II Directive and alignment of the Company in general with this Directive. In this respect the Internal Audit function monitors the following aspects.

Internal audit Pillar 1

The Internal Audit function assesses the design and effectiveness of the existing controls in the process of obtaining quantitative elements that are part of Pillar I: balance sheet, Solvency Capital Requirements and Minimum Capital Requirements.

Internal audit Pillar 2

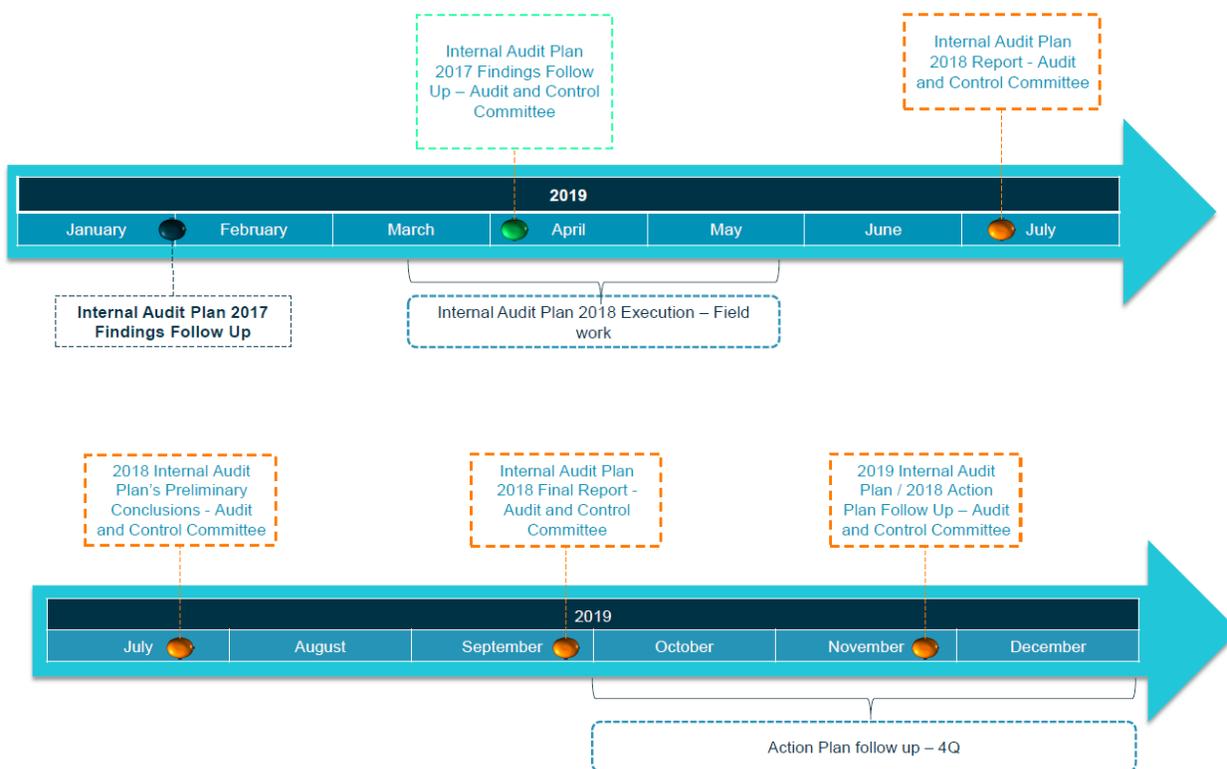
The Internal Audit function evaluates the following aspects of the governance system:

- Decision-making process and organizational structure
- Flow of information and communication between the different levels of the company
- Written policies on risk management, internal control, outsourcing, and any other policy required by the Solvency II Directive
- Means to verify compliance with the objectives of the governance system; and means to identify and evaluate emerging risks
- Verification of the existence of adequate controls in information systems, review of existing measures and ensure continuity and regularity in the performance of the activities of the company
- Identification of problems and opportunities for improvement while conducting the internal audit of the governance system
- Assessment of the risk management system and the existing procedures in the company to ensure compliance with the applicable regulations
- Monitoring internal control systems to ensure the quality of the data used in important processes of the company

Internal audit Pillar 3

The Internal Audit function monitors compliance with reporting obligations to the competent Supervisory Authority and the publication of the annual report on solvency and the financial condition of the company , as well as quantitative models if applicable.

A first complete internal audit of the company has been set up through the period 2017-2019. The Internal Audit department reports regularly to the Audit and Internal Control Committee. The diagrams below describe the schedule of internal audit activities and Audit Committee meetings performed in 2019.



B.6 ACTUARIAL FUNCTION

The actuarial team of Telefónica Insurance is in charge of the execution of the Actuarial Function of the Company. In this regard, the actuarial team,

- Coordinates / oversees the calculation of the pricing of products (according our previous experience in similar lines of business. The actuarial team checks if the premiums cover the risk)
- Coordinates / oversees the calculation of technical provisions (assess the uncertainty associated with estimates);
- Assesses the sufficiency and quality of the data used in the calculation of technical provisions (assess whether the information technology systems used sufficiently support the actuarial and statistical procedures);
- Compares best estimates against experience (review the quality of past best estimates and use the insights gained from this assessment to improve the quality of current calculations);
- Calculates the Solvency II capital requirements. The actuarial report and the MCR (Minimum Capital Requirement) are calculated on Solvency II basis;

- Provides support with the ORSA: perform base case projections of Profit & Losses, balance sheet and Solvency II ratio, as well as applying stress scenarios to those projections; the ORSA contains both a qualitative as well as a quantitative part.
- Provides its opinion on the underwriting policy and the reinsurance arrangements of Telefónica Insurance, to take into consideration the interrelations with the technical provisions.

The company outsources part of the works described to independent authorized actuarial consultants. For the calculation of SCR and MCR Telefónica engages the services of Act-Unity S.A. The company engages the services of Area XXI S.A. to support the works on the calculation of pricing of products.

The actuarial team reports at least annually to the Board of Directors.

B.7 OUTSOURCING

Telefonica Insurance outsources some operational activities in relation with the distribution and administration of the mobile phone insurance. Most relevant outsourced functions are,

Selling
Billing
Policy Administration
Customer relationship
Claims handling and fulfillment

This outsourcing pursues to offer the best service to its customer and it is based upon the principle of selecting the best-in-class partner. The nature of its operations and the business model of the company highly recommend this structure,

The activities subject to outsourcing correspond to the commercial business undertaken by the company on different territories of the European Union. In this context, the company engages partners established and with a record proof of high-quality service and expertise on the functions at stake.

Telefónica Insurance follows a procedure for the selection of all its business partners. This procedure is framed on the corporate regulation of Telefónica Group in outsourcing to third parties.

The procedure establishes among other relevant aspects the following requirements mandatory for the business partners,

- Operational risk management standard
- Business continuity plans
- Service level
- Once the tender-process for the selection of partner is completed the business partner is contractually subject to the service obligations summarized on two basic aspects,
 - Compliance with service level established on the SLA (“service level agreements”) including the formal periodic reporting to Telefónica Insurance. These services comprise the measurement and reporting of the “Customer satisfaction”.
 - Compliance with the legal and regulatory framework, including the consumer protection, personal data privacy and professional secrecy, and open-books policy to the supervision of the competent authority.
- The business partner, during the exercise of its services, is periodically subject to verification surveys and audits on Information Technology Systems, Operations and Procedures.

When choosing the service provider, The Company ensures that,

- a detailed examination is performed to ensure that the potential service provider has the ability, the capacity and any authorization required by law to deliver the required functions or activities satisfactorily, taking into account the company's objectives and needs;
- the service provider has adopted all means to ensure that no explicit or potential conflict of interests jeopardize the fulfilment of the needs of the outsourcing company;
- a written agreement is entered into between the insurance or reinsurance company and the service provider which clearly defines the respective rights and obligations of the company and the service provider;
- the general terms and conditions of the outsourcing agreement are clearly explained to the company's administrative, management or supervisory body and authorized by them;
- the outsourcing does not entail the breaching of any law in particular with regard to rules on data protection;
- the service provider is subject to the same provisions on the safety and confidentiality of information relating to the company or to its policyholders or beneficiaries that are applicable to company.

The company carries out periodically control and audits on third party providers set up on a risk-based approach described on the diagram below.



Telefonica Insurance outsources to the Telefonica Group, certain functions, which according to the Corporate Governance System of the Group are centralized on the corporate services as the Internal Audit and the Risk Management

B.8 ANY OTHER INFORMATION

Other than as noted above, no other information has a relevant impact on the system of governance.

C. RISK PROFILE

The company has a process for the early identification, management and reporting of risks with management accountability for risk identification and management in all the business areas of the company. The process is under the responsibility of the Risk Manager of the company reporting to the Governance Board and ultimately to the Board of Directors

The process initiates with the identification of risks. This process is conducted by the Risk Manager of Telefónica Insurance, through workshops with the Heads of the business areas of the company. The risks identified are included on the risk register of the company. In parallel, the Risk Owners and the Risk Manager assess every risk and define the appropriate controls and action plan aiming to eliminate, transfer or mitigate.

The risk assessment is carried out under the following principles: An inherent level of risk is determined through the combination of probability of occurrence of the risk, and its impact, that is, the estimation of the economic value of the risk in case this materializes.

The primary outcome of the risk management is the Risk Map of the company, which includes a detailed sheet for each of the risks included on the register. Every sheet includes the description and assessment of the risk and the controls and action plan. Overall results are shown on the Heat map, representing the resulting qualitative and quantitative evaluations of the probability of risk occurrence and the impact of every risk

The Risk Profile of the company is presented following the categories defined by the prudential regulation; Article 309 of Commission Delegated Regulation (EU) 2015/35. For each category, the different risks are described and quantified both, as determined in the Risk Map of the company and, where applicable, by the Solvency Capital Requirement, resulting of the application of the standard formula.

C.1 UNDERWRITING RISK

Underwriting risk is the risk of making losses on the activity of insurance either in assessing the risks it provides policies for or in quantifying claims that occur. Telefónica Insurance defines the following elements on underwriting and reserving risk management:

- The types and characteristics of the insurance business, such as the type of insurance risk the undertaking is ready to accept;
- How the adequacy of premium income to cover expected claims and expenses is to be ensured;
- The identification of the risks arising from the undertaking's insurance obligations,
- How, in the process of designing a new insurance product and the premium calculation, the undertaking takes account of the constraints related to investments;
- How, in the process of designing a new insurance product and the premium calculation, the undertaking takes account of reinsurance or other risk mitigation techniques.

Risk measures

The underwriting risks are identified in the Risk Register of the Company under Chapter 5 "Risk of underwriting and development of new products". The risks were measured by the Risk Map reporting of the company. According to the tolerance threshold defined by the company these risks were categorized as,

- Likelihood, Very Possible (30% - 50%)
- Severity, Medium (1-5 million euros)

The underwriting risk is defined under the standard formula of the Solvency II directive. Telefónica Insurance results as of December 31st 2019 are in thousands of euros,

| Composition of SCR Non Life | 2019 |
|-------------------------------------|--------|
| Catastrophic risk | 0 |
| Lapse risk | |
| Premium & reserve risks | 15.340 |
| SCR Non life before diversification | 15.340 |
| SCR Non life | 15.340 |

According to the provision of stated on the Commission Delegated Regulation (EU) 2015/35,Annex XII Groups of obligations and risk factors for the sub-module for other non-life catastrophe risk, the device insurance is not exposed to Catastrophe Risks. The company insurance contracts do not include an option for early surrender for a contractually fixed amount. Therefore the Lapse risk equals to zero.

Risk concentrations

The scale and scope of the main line of business of Telefónica Insurance , handset insurance main line of business (with insurance written in overseas branches in Spain, Germany and United Kingdom) results in quite relevant diversification of underwriting risks, due to the independence of the risks insured, mobile phones.

Risk mitigation

The main element of mitigation for the underwriting risk of the company is the purchase of reinsurance. Telefónica Insurance cedes significant underwriting risks through proportional reinsurance treaties. Average risk ceded amounts around 71% in 2019. The level of this reinsurance cover is reviewed and approved annually.

Additional mitigation items are, pricing guidelines which ensure accurate and consistent setting of premiums across the company and the review and assessment of reserving and regular reviews by management of the underwriting results by line of business, with actions taken on growing or reducing the businesses based on the performance.

Sensitivities

The main sensitivities for underwriting risks as at December 31st, 2019 were defined and assessed within the ORSA analysis. The ORSA analysis shocked a decrease of the Gross Written Premium.

C.2 MARKET RISK

Market risk can be defined as the potential loss of economic capital arising from adverse financial market movements. This risk arises from the assets and financial liabilities whose values are subject to such movements. This is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices. As defined on the legal framework of Solvency II the market risk is divided on the following submodule The main risk elements of the market risk as defined on Solvency II legal framework are,

- Interest rates

This risk measures the sensitive to a change in interest rate, of the term structure of interest rates. Assets submitted to this scenario are bonds, the part of reinsurers in technical provisions as well as the debtors linked or not to reinsurance operations.

- Equities
The risk measured is that market prices for equities and real estate will move adversely resulting in unexpected losses. Exposure to these risks arises from holdings of common stocks and equity unit trusts and from direct holdings in property, as well as investments in listed property companies and property funds
- Property
The risk measured is that market prices for real estate will move adversely resulting in unexpected losses. Exposure to these risks arises from direct holdings in property, as well as investments in listed property companies and property funds
- Credit Risk
This risk is analyzed under Section C.3 Credit Risk
- Currency exchange rates
The currency exchange risk is the financial risk of an investment's value changing due to the changes in currency exchange rates.
- Concentration
The concentration risk foresees the allocation of a capital risk to cover either a lack of diversification of assets or a significant exposure to Default risk of one or more counterparties.

Risk measures

1. Risk mapping

- Interest rate risk

The interest rates risk is identified in the 2019 Risk Map of the Company under Register #15 "Risk of interest rates". According to the tolerance threshold defined by the company these risks were categorized as,

- Likelihood, Very Possible (30% - 50%)
- Severity, Very Low (0- 0.5 million Euros)

- Equity risk

The Equities risk is identified in the 2019 Risk Map of the Company under Register #14 "Market risks". According to the tolerance threshold defined by the company these risks were categorized as,

- Likelihood, Very Possible (30% - 50%)
- Severity, Low (0.5 – 1 million Euros)

- Currency risk

The Currency exchange risk is not identified in the 2019 Risk Map of the Company, as following corporate mandate, all foreign exchange exposure is permanently hedged.

- Concentration risk

The Company is not exposed to Property risk, other than the value of stock on mobile handsets which is deemed immaterial. Therefore the property risk is not identified in the 2019 Risk Map of the company.

2. Standard Formula

The market risk is defined under the standard formula of the Solvency II directive. Telefónica Insurance results as of December 31st 2019 are in thousands of euros,

| Sub-modules | 2019 |
|--|--------------|
| Interest rate risk | 244 |
| Equity risk | 1.928 |
| Concentration risk | 748 |
| Spread risk | 355 |
| Currency risk | 280 |
| Property risk | 2 |
| SCR Market before diversification | 3.556 |
| Diversification | 1.121 |
| SCR Market | 2.435 |

Risk concentrations

There were no material risk concentrations at December 31, 2019 as the company allocates its financial investments through investment funds, allowing significant diversification.

Risk mitigation

The main elements of mitigation for the market risk are set up on the Investment Policy of the company. In compliance with article 114 of the Insurance Law and the related CAA regulation, the Investment Policy of the Company is governed by the general investment principle of the prudent person. The Investment Policy ensures the security, quality, liquidity and profitability of the investment portfolio. The Strategic Asset Allocation defined on the investment policy includes limits on exposures to each type of asset classes. The Investment Committee is responsible for the execution of the investment policy of the company. The Investment Committee meets quarterly to monitor the investment portfolio of the company. The Investment department produces monthly reports to follow up the performance and the compliance with the quantitative limits on assets and exposures, of the portfolio. The company enters into a forward exchange rate contract with the Group to cover the exposure currency exchange rates.

Sensitivities

Market risk sensitivities may include macro and micro economic trends, political framework, environmental factors and a wide range of other factors. The Investment Committee follows-up and monitors market sensitivities by the bias of the reports produced by the Telefónica Group Capital Markets and Economic studies departments and the financial institutions which provide services to the company

C.3 CREDIT RISK

Credit risk is defined in Solvency II under a twofold approach, spread risk and counterparty default risk. The spread risk represents a change in the volatility of credit spreads over the risk-free rate interest rate term structure. The counterparty risk is defined as the potential loss of economic capital arising from counterparties failing to fulfill their financial obligations. Financial assets exposed to counterparty are classified in three main groups.

1) Reinsurance assets

The exposures to this risk are balances due under existing reinsurance contracts. Such contracts have been entered in accordance with the reinsurance strategy.

The counterparties are reinsurance companies and the risk measured is that these counterparties would default on their obligations. The potential loss of value due to rating migration risk is also measured; this is the potential reduction in the value of reinsurance assets if counterparties were downgraded.

2) Receivables due from policyholders, agents and intermediaries, and other insurance companies

The exposures are premiums due from counterparties and amounts due on insurance arrangements and other contractual obligations. The counterparties are policyholders, brokers, intermediaries and other insurance companies and the risk measured is that the counterparties would default on their obligations.

3) Cahs at bank, deposits with ceding undertakings and other legally binding commitments called up but unpaid ordinary share capital and preference shares, called up but unpaid legally binding commitments to subscribe and pay for subordinated liabilities, called up but unpaid initial funds, members' contributions or the equivalent basic own-fund item for mutual and mutual-type undertakings, called up but unpaid guarantees, called up but unpaid letters of credit, called up but unpaid claims which mutual or mutual-type associations may have against their members by way of a call for supplementary contributions

Risk measures

The credit risk is identified in the 2019 Risk Map of the Company under Register #14 "Credit risk" and Register #10 Client bad debt. The risks were measured by the Risk Map reporting of the company. According to the tolerance threshold defined by the company these risks were categorized as,

14 Credit Risk

- Likelihood, Possible (11% - 30%)
- Severity, Low (0,5 – 1 million euro)

10 Client bad debt Risk

- Likelihood, Very Possible (31% - 50%)
- Severity, Low (0,5 – 1 million euro)

The Credit risk is defined under the standard formula of the Solvency II directive in two separate risk sub-modules, spread risk and counterparty default risk. Spread risk results at December 31st 2019 was shown in the section Market Risks, Counterparty default risk results are shown below,

| SCR Default composition | 2019 |
|------------------------------------|--------------|
| Risk of default type 1 | 4.381 |
| Risk of default type 2 | 3.415 |
| SCR Default before Diversification | 7.796 |
| SCR Default | 7.300 |

Risk concentrations

The largest value individual holdings are cash at Banks at BGL BNP Paribas and Société Générale Bank & Trust.

Risk mitigation

The main elements of mitigation for the credit risk are set up on the Investment Policy of the company. In compliance with article 114 of the Insurance Law and the related CAA regulation, the Investment Policy of the Company is governed by the general investment principle of the prudent person. The Investment Policy ensures the security, quality, liquidity and profitability of the investment portfolio. The Strategic Asset Allocation defined on the investment policy includes limits on exposures to each type of asset classes. The Investment Committee is responsible for the execution of the investment policy of the company. The Investment Committee meets quarterly to monitor the investment portfolio of the company. The Investment department produces monthly reports to follow up the performance and the compliance with the quantitative limits on assets and exposures, of the portfolio.

Sensitivities

The main sensitivities for credit risks as at December 31st, 2019 were defined and assessed within the ORSA analysis. No further sensitivity analysis for credit risks was carried out in 2019.

C.4 LIQUIDITY RISK

Liquidity risk is defined as the risk of insufficient liquid financial resources being available to meet financial obligations of the company.

The company defines the following elements on liquidity risk management:

- The process to determine the level of mismatch between the cash inflows and the cash outflows of both assets and liabilities, including expected cash flows of direct insurance and reinsurance such as claims, lapses or surrenders
- The consideration of total liquidity needs in the short and medium term including an appropriate liquidity buffer to guard against a liquidity shortfall

- The consideration of the level and monitoring of liquid assets, including a quantification of potential costs or financial losses arising from an enforced realization
- The identification and assessment of the cost of alternative financing tools
- The consideration of the effect on the liquidity situation of expected new business

Risk measures

The Liquidity risk is identified in the Risk Register of the Company under Chapter 18 “Credit Risk” The risks were measured by the Risk Map reporting of the company. According to the tolerance threshold defined by the company these risks were categorized as,

- Likelihood, Remote (0% - 10%)
- Severity, Very Low (0 – 0,5 million euro)

The Liquidity risk is not explicitly defined under the standard formula of the Solvency II directive.

Risk mitigation

The company uses the following elements to monitor and mitigate the liquidity risk,

- The cash-flow position is monitored and reported monthly to the Management of the Company and to the Group Financial Office
- Minimum cash available threshold
- Credit Risk analysis of the Financial Institutions where cash and financial assets are held
- The cycle of premium collection and claims and expenses disbursement is regularly monitored

Sensitivities

The company carries out annually a liquidity risk stress test on the financial investment portfolio. Among other elements, the methodology factors the market depth and the variation of the bid-ask spread for every category of asset. No relevant exposure to liquidity risks were identified through the 2019 stress test.

C.5 OPERATIONAL RISK

The operational risk is defined as the potential loss of economic capital resulting from inadequate or failed internal processes or systems, failure of personnel, or impact from external events such as failures in outsourcing arrangements, changes in legislation or tax laws, or external fraud including cyber-attacks.

The company defines the following elements on operational risk management:

- The identification and quantification of the operational risks it is or might be exposed to and assessment of the way to mitigate them
- The activities and internal processes for managing operational risks, including the IT system supporting them
- The risk tolerance limits with respect to the undertaking’s main operational risk areas

Telefónica puts in place processes to identify, analyze and report on operational risk events. For this purpose, a process for collecting and monitoring operational risk incidents and resolutions follow-up will be developed.

Risk measures

The Risk Register of the Company identifies a number of risks that can be included under the category Operational risks according to the definition of Solvency II. The following table presents these risks as assessed under the Risk Map of the Company.

| # | Risk description | Likelihood | Severity |
|----|-------------------------------------|-------------------------|--------------------------------|
| 2 | Regulator and administration risks | Possible (11%-30%) | High (5-10 million euros) |
| 3 | Customer and business conduct risks | Possible (11%-30%) | Medium (1-5 million euros) |
| 4 | Supply chain dependency | Very Possible (31%-50%) | Medium (1-5 million euros) |
| 6 | Information quality | Possible (11%-30%) | Medium (1-5 million euros) |
| 7 | Taxes | Possible (11%-30%) | Low (0,5-1 million euros) |
| 8 | Data protection | Possible (11%-30%) | Very high (>10 million euros) |
| 9 | Insuficiencia de recursos | Very Possible (31%-50%) | Low (0,5-1 million euros) |
| 13 | Invoice management | Remote (0%-10%) | Very Low (0-0,5 million euros) |
| 17 | Cybersecurity | Very Possible (31%-50%) | High (5-10 million euros) |

The Operational risk is defined under the standard formula of the Solvency II directive. Telefónica Insurance results as of December 31st 2019 are in Euros thousands,

| | |
|---------------|--------------|
| SCR Op | 4.731 |
|---------------|--------------|

Risk mitigation

The Risk Management function of the company monitors and reports the mitigation actions for operational risks. Among different mitigations elements are, business continuity plans, insurance, SLA and KPI's definitions and on outsourced services etc.

C.6 OTHER MATERIAL RISKS

The Risk Register of the Company identifies three risks that can be included under the category Other Material risks.

1 Business model risk. The risk is defined as the negative impact on the activities of the company caused by the high dependence on the Telefónica Group strategy. The Risk Map assesses the Brexit Risk as follows,

- Likelihood, Very Possible (31% - 50%)

- Severity, Very High (> 10 million euro)

11. Market environment The risks is defined as the negative impact on the activities of the company caused by the increase of competence within the insurance market mostly due to the digitalization of the economy and the appearance of new actors, widely defined as the InsurTech.

- Likelihood, Possible (11% - 30%)
- Severity, Low (0,5 – 1 million euro)

16 Brexit risk. The Brexit risk is defined as the negative impact on the activities of the company caused by the withdrawal of the United Kingdom from the European Union. Assuming that the Brexit will lead to the automatic withdrawal of the European Passport to carry out activities under both the freedom of services and the freedom of establishment provisions, the company will effectively be unable to carry on insurance services on the United Kingdom. The Risk Map assesses the Brexit Risk as follows,

- Likelihood, Very Probable (81% - 100%)
- Severity, Low (0,5 – 1 million euro)

C.7 ANY OTHER INFORMATION

There is no any other relevant information in this section.

D. VALUATION FOR SOLVENCY PURPOSES

See ANNEX 1

E. CAPITAL MANAGEMENT

See ANNEX 1

ANNEX 1 – SECTIONS D & E

Prepared by ACT-UNITY Luxembourg S.A.

1.Context

The European Commission has published the 10th of October 2014 the Delegated Regulation (UE) 2015/35. This document supplements the directive 2009/138/CE of the European Parliament (solvency II).

This report drafts the Chapter D and E of the SFCR report (articles 296 and 297).

This report describes the assumptions and the calculation of the available capital and the Solvency Capital Requirement of Telefónica Insurance S.A., based on 12/2019 financial statements.

2.Solvency 2 Balance sheet

2.1. Balance sheet in economic value

In summary, the table compares the statutory consolidated Balance sheet with the economic one evaluated according to the Solvency 2 technical specifications.

| Accounting | | Economic | |
|----------------|----------------|----------------|---------------|
| Assets | | Assets | |
| Investment | 11.202 | Investment | 11.694 |
| RI Recoverable | 17.276 | RI Recoverable | 7.802 |
| Debt | 27.345 | Debt | 27.345 |
| Other Assets | 52.387 | Other Assets | 52.387 |
| P and A Income | 3.005 | P and A Income | |
| Other | 773 | Other | |
| Total | 111.988 | Total | 99.228 |

| Liabilities | | Liabilities | |
|--------------------|----------------|--------------------|---------------|
| Basic Own Fund | 62.094 | Basic Own Fund | 62.113 |
| Tech. Provision | 21.637 | Tech. Provision | 11.106 |
| Debt | 20.388 | Debt | 20.388 |
| Prov. for Taxation | 5.615 | Prov. for Taxation | 5.621 |
| Reg. Account | 2.255 | Reg. Account | |
| Other | | Other | |
| Total | 111.988 | Total | 99.228 |

The economic valuation gives an available capital of 62.113 k€. We describe in the following chapters the assumptions and methods used to get the economic values of each item.

2.2. Evaluation of Assets for Solvency purposes

The market valuation of the assets (equities, government bonds and corporate bonds) is done by the custodian bank. They subsequently send the information to our Asset managers who prepare a report.

The assets are split by type (Fixed Income, Equities, Emerging Market equities, and cash).

The table below gives the comparison between the statutory value and the economic value.

| <i>Following Financial Statement</i> | EconomicBS | Statutory BS | Delta | % |
|--------------------------------------|-------------------|---------------------|---------------|------------|
| Cash and deposits | 52.079 | 52.079 | | 0% |
| Bonds | | | | |
| Equities | 11.670 | 11.177 | 493 | 4% |
| Participation | | | | |
| Properties | | | | |
| Tot Portfolio | 63.749 | 63.256 | 493 | 1% |
| Def Acquisition Cost | | 3.005 | -3.005 | -100% |
| Other Inv | 21 | 21 | | 0% |
| Accr Interest | | | | |
| Asset Subj S2 | 63.769 | 66.282 | -2.512 | -4% |

2.3. Evaluation of Technical Reserves for Solvency purposes

2.3.1. Segmentation

Telefónica Insurance S.A. (Telefónica, hereafter) is a Non-Life undertaking that covers the following programs:

1. Property Damage and Business Interruption affiliated to the line of business “Fire and other damage to property insurance“ (S4),
2. General liability (professional liability) affiliated to the line of business “General liability insurance” (S5),
3. Reputation risk affiliated to the line of business “Miscellaneous financial loss insurance” (S9),
4. Handset affiliated to the line of business “Miscellaneous financial loss insurance” (S9);
5. Accidents, Corps VTA affiliated to the line of business “Motor vehicle liability insurance” (S1),
6. The assistance risk for the motor vehicle affiliated to the line of business “Motor vehicle liability insurance” (S1),
7. Motor vehicle liability affiliated to the line of business “Motor vehicle liability insurance” (S1).

Therefore, we consider a total of 4 lines of business on the basis of Annex I to Regulation 201/035 of the European Commission. Telefónica cedes a part of these risks to the following reinsurers:

- CHUBB EUROPEAN GROUP LIMITED,
- Nova Casiopea Re S.A.,

- ZURICH INSURANCE PLC.

2.3.2. Methodology

The methodology used to evaluate the gross & net best estimate (undiscounted) of claims provision is based on accounting claim provisions. The (statutory) gross claims provisions are equal to 5.929 k€ and the ceded claims provisions are equal to 5.479 k€. The undiscounted best estimate for claims (gross of reinsurance) considered in the calculation is equal to 2.444 k€ and the undiscounted reinsurers' share of technical provisions for claims amounts to 2.000 k€.

To compute the Best Estimate of gross premium provisions, we have determined the claims resulting from the unearned premiums and the expected profit due to future premiums. The loss-ratios used are the following:

| | | Loss Ratios (gross) |
|-----------------------------------|---------|---------------------|
| Miscellaneous financial loss | Spain | 45,8% |
| | Germany | 47,8% |
| Fire and other damage to property | | 100,0% |

The table below gives the BE undiscounted (gross and net) by line of business:

| Best Estimate - Undiscounted | | | | | Gross | | Net | |
|--|----------|----|-------|-------|-------|-------|-------|-------|
| | | | | | Prem | Claim | Prem | Claim |
| Assurance directe et réassurance proportionnelle des branches: | | | | | 7.221 | 2.444 | 1.455 | 444 |
| Motor vehicle liability insurance and proportional reinsurance | NON_LIFE | S1 | - | 81 | - | 81 | | |
| Fire and other damage to property insurance and proportional reinsurance | NON_LIFE | S4 | 26,16 | 50 | 3,01 | 2 | | |
| General liability insurance and proportional reinsurance | NON_LIFE | S5 | - | 46 | - | 2 | | |
| Miscellaneous financial loss insurance and proportional reinsurance | NON_LIFE | S9 | 7.195 | 2.268 | 1.452 | 358 | | |

2.3.3. Discounting & Risk Margin

The best estimate is defined in Solvency II as the average of future cash-flows taking account of the time value of money, using the relevant risk-free interest rate term structure. This curve is given by EIOPA. To evaluate the corresponding Best Estimate, we have used the following payment patterns:

| | | Payment Pattern (in years) | | | | | | | | |
|-----------------------------------|---------|----------------------------|-----|-----|----|----|-----|-----|-----|----|
| | | 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 |
| Miscellaneous financial loss | Spain | 0% | 98% | 2% | | | | | | |
| | Germany | | | | | | | | | |
| Fire and other damage to property | | 29% | 42% | 22% | 5% | 1% | 0% | 0% | 0% | |
| Motor vehicle liability | | | | | | | | | | |
| General liability | | 2% | 26% | 21% | 5% | 4% | 14% | 10% | 18% | 1% |

The table below gives a comparison between the statutory claims provisions (in €'000) and the economic value with the discounting effect.

| | Economic | Statutory | % | Delta |
|----------------------------------|---------------|---------------|---------------|----------------|
| BE Claims Net | 444 | 450 | -1,4% | -6 |
| BE Premium Net | 1.471 | 3.910 | -62,4% | -2.440 |
| BE Net | 1.915 | 4.360 | -56,1% | -2.446 |
| BE Claims Ceded | 1.999 | 5.479 | -63,5% | -3.480 |
| BE Premium Ceded | 5.803 | 11.797 | -50,8% | -5.994 |
| BE Ceded | 7.802 | 17.276 | -54,8% | -9.474 |
| BE Claims Gross | 2.443 | 5.929 | -58,8% | -3.486 |
| BE Premium Gross | 7.274 | 15.707 | -53,7% | -8.434 |
| BE Gross | 9.717 | 21.637 | -55,1% | -11.920 |
| Risk Margin | 1.390 | | | 1.390 |
| Equalization Reserve | | | | |
| PB Reserve | | | | |
| Technical Provision Gross | 11.106 | 21.637 | -48,7% | -10.530 |

The technical provisions gross of reinsurance (discounted Best Estimate + risk margin) are equal to 11.106 k€. Compared with the statutory account, it means a reduction of 10.530 k€.

For the risk margin valuation, we apply the simplification defined as a proportional approach based on best estimates (as described in the technical specifications). This means:

- For the UW SCR, the Premium and Cat risk are taken into account only the next 12 months. We approximate the UW Reserve SCR for future years by using a proportional approach based on the development of the net best estimate.
- For the Default risk, we only take into account the reinsurance default risk and we approximate the Default SCR for future years by using a proportional approach based on the development of the ceded best estimate.
- We approximate the Operational SCR for future years by using a proportional approach based on the development of the gross best estimate.
- We do not take into account any Market risk.

2.4. Valuation of other liabilities

The value of the provision for taxation is 6 k€; it represents the provision for differed taxes and its solvency II value is evaluated by applying the tax rate 24,94% to the delta investments, other assets, technical provisions, the equalization provision and other liabilities.

| | |
|------------------------|----------|
| Eco - DTL - Net | 6 |
|------------------------|----------|

| S2 Added Value | Total |
|-------------------------------|---------------|
| Investments & Cash | 493 |
| Reins. recoverables | -9.474 |
| Receivables | |
| Other Assets | -3.778 |
| Best Estimate | 11.920 |
| Risk Margin | -1.390 |
| Eq. Reserve | |
| Other Liabilities | 2.255 |
| Total | 25 |

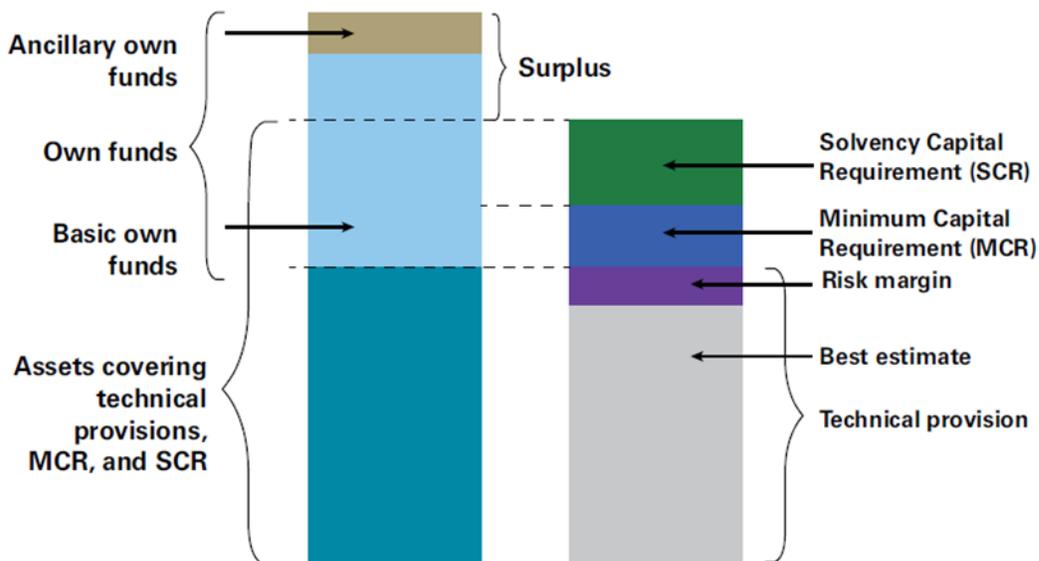
2.5. Any other material information

No more information are relevant.

3. Information on Capital Management

3.1. Evaluation of the available capital

The Solvency II balance sheet can be summarized as follows:



The Basic own funds are the balance sheet items as excess of assets over liabilities, subordinated liabilities (with own fund character), deductions (for instance own shares).

The Ancillary Own Funds are off balance sheet items as unpaid share capital, letters of credit, guarantees...

The Basic own funds have been evaluated at 62.113 k€ and the table below gives the difference between the booked value and the Solvency II.

| | | | |
|--|---------------|-----------------|------------------|
| Excess Asset Over Liabilities | 62.113 | | |
| Capital and reserves | 35.775 | | |
| Subscribed Capital | 8.250 | | |
| Share Premium Account | 27.525 | | |
| Reconciliation Res - Statutory | 26.319 | | |
| Legal Reserve | 42 | | |
| Contingency Reserve | 825 | | |
| Result For The Year | 5.549 | | |
| Deferred Income | 19.903 | | |
| An amount equal to the value of net deferred tax assets | | Economic | Statutory |
| Reconciliation reserve - S2 | 19 | Economic | Statutory |
| Investment, Cash, Acc Int | 493 | 63.779 | 63.286 |
| Reinsurer's Recoverables | -7.219 | 7.802 | 15.021 |
| Def Tax Assets | | | |
| Other Assets | -773 | 47.164 | 47.937 |
| Technical Provision | 7.525 | 11.106 | 18.631 |
| <i>Best Estimate</i> | 8.915 | 9.717 | 18.631 |
| <i>Risk Margin</i> | -1.390 | 1.390 | |
| <i>Equalisation Provision</i> | | | |
| Def Tax Liab | -6 | 6 | |
| Other Liabilities | | 45.519 | 45.519 |

3.2. Eligibility of Own Funds

The classification of funds is done in according to their capacity to absorb losses:

- Tier 1 means permanently available to fully absorb losses in case of winding up and on a going concern basis,
- Tier 2 relates absorb losses in the case of a winding-up of the undertaking (not on a going concern basis),
- Tier 3 relates to own funds which do not have the characteristics of the first two tiers.

We consider the own funds as permanent available because their sufficient duration, their absence of incentives to redeem, their absence of encumbrances. The amount of 62.113 k€ has been classified in Tier 1.

4. Solvency Capital Requirement (SCR)

Here is the summary of the SCR results at December 2019:

| | ARS Q4 2019 | ARS Q4 2018 |
|-----------------------|-------------|-------------|
| SCR | 25.559 | 37.304 |
| Adj Differed taxes | -6 | |
| SCR Operational | 4.731 | 5.355 |
| Basic SCR | 20.834 | 31.949 |
| Market Risks | 2.435 | 4.410 |
| Default Risks | 7.300 | 8.418 |
| Underwriting Health | | |
| Underwriting Non Life | 15.340 | 25.349 |
| Intangible Asset Risk | | |
| Capital Available | 62.113 | 55.964 |
| Solvency Ratio | 243% | 150% |

The SCR is estimated at 25.559 k€ (37.304 k€ in 2018), more details of the calculation are given in the following chapters. The Solvency ratio is then 243% (150% in 2018). The MCR is evaluated at 6.390 k€.

4.1. Market risks

The market risks are evaluated at 2.435 k€. The decrease of the market risk compared to last year is mainly due to the currency risk. There is an integration of derivatives to reduce the currency risk (which slightly increase the default risk type I).

| Market Risks | 2.435 | 4.410 |
|------------------------|--------|--------|
| Interest Rate Risk | 244 | 378 |
| Equity Risk | 1.928 | 1.445 |
| Property Risk | 2 | 5 |
| Spread Risk | 355 | 625 |
| Concentration Risk | 748 | 865 |
| Currency Risk | 280 | 3.271 |
| Diversification Effect | -1.121 | -2.179 |

4.1.1. Interest Rate risk

The table below gives the initial value, the shock up & down of Assets having a potential interest rate risk and the BE liabilities. The interest rate risk amounts to 244 k€.

| | Initial | Up | Down |
|-------------|---------|-------|-------|
| Assets | 7.023 | 6.747 | 7.073 |
| Liabilities | 1.915 | 1.882 | 1.916 |
| NAV | 5.108 | 4.865 | 5.158 |
| Delta NAV | | 244 | -49 |
| Mktint | | 244 | - |

4.1.2. Equity risk

The table below represents the shock on equities.

| | Global | Other |
|----------------|--------------|--------------|
| Assets | 1.431 | 3.015 |
| Assets Shocked | 874 | 1.540 |
| Shock | 557 | 1.475 |
| Shock % | 39% + -0,08% | 49% + -0,08% |

With the correlation parameters, the equity risk is equal to 1.928 k€. The shock is based on:

- A basic shock of 39% for Global and 49% for Other Equities;
- Plus a symmetric adjustment of -0,08%.

4.1.3. Property risk

The table below gives the initial asset value and the shock amount. The property risk is equal to 2 k€.

| | Global |
|----------------|--------|
| Assets | 9 |
| Assets Shocked | 7 |
| Shock | 2 |
| Shock % | 25% |

4.1.4. Currency risk

Around 9% of the investments and 15% of liabilities are in other currency. The currency risk is equal to 280 k€ with an integration of derivatives (1.138 k€ without derivatives).

| | Initial Value | Other Curr | Shock |
|------------------------|---------------|--------------|------------|
| Assets | 56.695 | 4.839 | 56.406 |
| Liabilities | 1.915 | 289 | 1.905 |
| NAV | 54.780 | 4.551 | 54.501 |
| Delta NAV | | | |
| Shock | | 280 | 280 |
| Average Shock % | 0% | 6,14% | |

4.1.5. Spread risk

The table below gives the split of the portfolio having a potential spread risk. The spread risk is equal to 355 k€.

| | Bonds & Loan |
|------------------------|--------------|
| Assets | 7.023 |
| Assets Shocked | 6.668 |
| Shock | 355 |
| Average Shock % | 5,05% |

4.1.1. Concentration risk

The concentration risk is equal to 748 k€, as shown in the following table:

| | Global |
|----------------|------------|
| Assets | 11.478 |
| Assets Shocked | 10.730 |
| Shock | 748 |

4.2. Underwriting risk Non-Life and Health

4.2.1. Premium & Reserve Risk

For the premium risk, the premium volume is defined as being the maximum between the Net Earned premium of 2019 and 2020. We consider a geographical diversification in the calculation (DIVs).

SCR Premium & Reserve – Non Life

| | |
|--------------------------------------|---------------|
| Premium and Reserve risk | 15.340 |
| Function of the standard deviation | 38,87% |
| Standard deviation | 12,96% |
| Volume measure | 39.461 |
| Volume measure - Premium Risk | 45.853 |
| Volume measure - Reserve Risk | 444 |

SCR Premium & Reserve – Health

The Premium & Reserve risk for health is not applicable as Telefónica Insurance S.A. doesn't cover health business.

4.2.2. Lapse risk

The lapse risk is not applicable.

4.2.3. Catastrophe Risk

At the end of December 2019, the company is not exposed to the Catastrophic risk. Indeed, all the risks covered are excluded from the calculation of the catastrophic risk in accordance with the Standard Formula.

4.3. Default risk

The Default risk is based of 2 types of exposures.

Type 1 exposures

- Reinsurance arrangements: recoverables and debtors arising out of reinsurance operations;
- Cash: cash at bank;
- Derivatives used to mitigate the currency risk;
- Risk mitigating impact: on one hand, from the premium & reserve risks and on the other hand, from the Cat scenarios;

Type 2 exposures

- Other Debtors arising out of customers or intermediaries.

We give here below the Default SCR by type:

| | ARS Q4 2019 | ARS Q4 2018 |
|----------------------|--------------|--------------|
| Default Risks | 7.300 | 8.418 |
| Type 1 | 4.381 | 2.784 |
| Type 2 | 3.415 | 6.126 |

The risk of default type 1 increases due to a higher exposure in cash at bank and the intra-group loan which has a BBB rating. The decrease of default risk type 2 is driven by the reduction of debtors arising out of accepted operations.

4.4. Operational risk

The application of the standard model gives the following result:

| | |
|--------------------------------|--------------|
| SCR Op | 4.731 |
| a) SCR based on TP | 292 |
| b) SCR based on Earned Premium | 4.731 |
| 30% * SCr Base | 6.250 |

The operational risk is realized on the premium component.

4.5. Adjustment for deferred taxes

The adjustment for the loss-absorbing capacity of deferred taxes is equal to the change in the value of deferred taxes that would result from an instantaneous loss of an amount that is equal to the following amount: BSCR + SCROp.

| | |
|-------------------|---------------|
| Base | 25.565 |
| BSCR | 20.834 |
| Operational Risk | 4.731 |
| Adj Tech Prov | |
| Tax Rate | 24,94% |
| Tot Base1 | 6.376 |
| Tot Base2 | 6 |
| Adjustment | 6 |

As we limit the adjustment of deferred taxes to the economic valuation of deferred taxes, the Adjustment for deferred taxes associated to tax rate of 24,94% amounts to 6 k€.

4.6. Minimum Capital Requirements

The MCR is realized in the floor of 25% of the SCR.

| | |
|-------------------------|---------------|
| MCR | 6.390 |
| Cap of 45% SCR | 11.501 |
| Floor of 25% SCR | 6.390 |
| MCR linear | 5.908 |
| MCR Min Absolute | 3.700 |